NetDragon (0777.HK) 2022 Annual 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. Vin Riera, CEO of Promethean
Mr. Lin Chen, Group Senior Vice President

Moderator:

Dear friends. Good morning. Thank you for joining us for NetDragon Websoft Holdings Limited 2022 annual results presentation. Our presentation PPT will be broadcast on the live-streaming platform. And 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 hosting today.

We have:

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

We have:

Mr. Ben Yam, Group CFO.

We have:

Mr. Lin Chen, Group Senior VP.

We have:

Mr. Vin Riera, CEO of Promethean.

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

Simon Leung:

Thank you. First of all, welcome. Thank you for calling in. I have to apologize that I'm not dressed for the occasion like my other colleagues. They're joining us from different parts of the world. Vin is from Seattle, Lin Chen is in Fuzhou, Ben is actually being isolated at his home because he got Covid. He doesn't look like it, but he's recovering. So, Ben, thank you for joining even though you are not well.

But anyway, why don't we go straight to the chat out. Today it is kind of interesting. We'll go through 2022. We'll look at the outlook. Let's flip to the next page. It is the end of March. We are talking about 2022. So, I think that when I will refer to 2023, it's more like an outlook. If I can look back at 2022, if I may quote the *Tale of Two Cities*, it was

the best of time. And sometimes it's not so much the worst of times, but it's not so good as a time because there's actually a lot of things happened in 2022.

The good news, the upshot is actually we are seeing good growth in our education segment. But frankly, that's not without some challenges. But given the fact that we have a very good team under Vin Riera, then we were able to pull out very solid growth and respectable results which is actually very good. You got to think back on 2022 in Europe. So, there's a war between Ukraine and Russia. It actually caused some issues. Economy got hit in Europe and all that, and followed by some currency issues because of the devaluation, a lot of the European currency compared to a very strong US currency. We still were dealing with some of the aftermath of Covid. But regardless of all those challenges, it is actually a very good result.

If you look at our revenue growth it's 12% year over year. That is with very, very good growth in education, offset by a small decline in our gaming sector. We are not the only one, actually we are declining slower than our competitors, which is good news from that end. But at the end of the day, we don't like declining results, so we're going to work very hard this year, Lin Chen is going to take you through what we plan to do in 2023. If you look at our profit, we chose to show the non-GAAP because we took some hit on some of our investments, which Ben will go through. But from an operational standpoint, even with some decline on the gaming sector, we maintain the same kind of profit, more or less, year over year. And we have a small growth in operating cash flow that shows you we have a very solid business in terms of both education and gaming and also operationally we performed very, very well.

So, with that I'll go through the highlights a little bit. I did talk about education, very solid growth. Good news also is actually we maintained the number one global position in the panel outside of China. One thing we're very happy that we started to do even before the big AI kind of wave is actually embracing the AI technology, which Vin will talk at a high level, what we are doing. We may set up some other time later in the year, to take you through the details on what we plan to do both from a strategic standpoint and also from a product standpoint. On the gaming side, even though we declined, but we declined slower than the market, which is not bad. We also significantly invest in our people so we can position ourselves for our future growth. Again, Lin Chen is going to take you through some of the details. So, with that, I'm going to turn it over to Ben, who is recovering from Covid, but he's going to do his best to take you through some of the highlights. Ben.

Ben Yam:

Thank you, Simon. Okay. First, I'm going to quickly go through the overall P&L, and then I'll talk about our segmental financials. So, our overall revenue growth for the year was 11.8% in a year of macro challenges, especially the gaming business. Gaming is down 5.8% while education was up 34%. I will let Lin Chen and Vin to go through the details on what's behind the top line performance. On the expense side, we continued

to benefit from the operating leverage as all three of the SG&A expenses went down as a percentage of revenue. In terms of bottom line, on a non-GAAP basis, our EBITDA went down by 10.8%, and operating profit went down by 12.7%. Non-GAAP profit attributable to owners of the company was down by a slight 2.2%. But I wanted to point out that our operating cash flow actually saw a moderate growth of 4.2% for the year as we continued to manage our cash flow with a disciplined approach. And also, we had 3.7 billion RMB of Cash and Cash Equivalents on our balance sheet as the end of 2022. Onto the next slide.

Okay. On this slide, I'm going to talk about the segmental financial for education and gaming. First, on the education business, while we saw strong topline growth, our gross margin actually dropped by 7.6%. That is mainly due to a couple of factors that is outside of our control. One is tariff accounting. The other one is currency impact given a strong US dollar against the GBP and the Euro. If we look at the adjusted gross margin which takes out tariffs and assumes foreign exchange on a neutral basis, adjusted gross margin is 29.2% for the year compared to 30.7%, which is a very slight decrease. And that is actually because of a slight increase in the material cost per unit as we launched our new ActivPanel 9 in June, 2022. And this is the product that is actually faster, more powerful, and comes with industry leading new features, which Vin will talk about. The other reason for the drop is that while we launched ActivPanel 9 in June, we had to sell down ActivPanel 7, which is our existing model, and so we had to sell down that inventory with a lower ASP than in 2021. In addition, there is also a one-off accounting write-off of warranty inventory in 2022, which also impacted the gross margin. Overall, in terms of the segmental bottom line, our core segmental loss for education narrowed by 27% to 299 million as a result of our continuous effort in cost management.

On the gaming side, what I want to highlight is that, we continued to invest in R&D in 2022, as we saw our R&D expense increased by 16.7% during the year. We believe that our increased investment in R&D will enable us to continue to grow our pipeline, both in terms of quality and also in terms of quantity. And then on the SG&A side, we also continued to look for cost reduction opportunities in selling and marketing and also our administrative expense. As a result, you can see that both of these expenses also decreased during the year. Okay. With that, I'm going to pass the time to Lin Chen, who is going to take you through the gaming business.

Lin Chen: [Translated from Mandarin]

Thank you, Ben. Hello everyone, I'm Lin Chen. I will introduce to you NetDragon's gaming performance in 2022.

In 2022, while under economic pressure due to the pandemic, our gaming business had a relatively stable year. Our total gaming revenue decreased by 5.8% as market revenue went down 10%. At the same time, however, our strategy and products over the past few years had become increasingly validated by the market. First of all, our

overseas revenue achieved a YOY growth of 6.5%, accounting for 15.7% of total revenue. The growth in overseas revenue as a percentage of the total revenue for five consecutive years had made our gaming business composition much healthier.

Meanwhile, a lot had been done in terms of optimization last year, achieving good performance for our user base and paying user structures. For example, on the PC end, our APA saw a 16.4% increase. We are also quite optimistic about the growth in the post pandemic macro recovery. Over the past year, we have significantly strengthened and recalibrated our R&D team by adding new talents, to put us in a better position of developing pipeline games. We expect our gaming business will resume to the growth trajectory in 2023 and 2024.

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On the PC end, due to its particular user structure, our *Eudemons Online* was affected by the pandemic. It will recover soon, however, as the economy recovers from the pandemic. In terms of mobile games, there was only a 0.2% decrease comparing to the year before. We interacted with our users more quickly through more efficient content iteration and integrated marketing efforts. In this sense, I believe the scale, loyalty and stickiness of the *Eudemons* IP user base have been great. We have also significantly outperformed the market on the mobile front.

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I would like to talk about the overall performance of our *Eudemons* IP first. *Eudemons* is our longest-term IP in the MMO category to which we have dedicated great effort. While its PC revenue went down by (7.9%), we are putting more emphasis on user retention and stickiness. *Eudemons* IP had actually achieved great optimization and growth in terms of paying user base and its structure. Meanwhile, the DAU of *Eudemons Online Cross Platform Version*, increased significantly, implying that even though the in-game spending had been under pressure during the economic slowdown last year, the overall user engagement kept growing. This provided a favorable foundation for our long-term operation.

On the mobile end, the overall mobile revenue went up 3.6% YOY, of which *Eudemons Pocket Version* contributed a relatively large amount of growth in revenue. *Eudemons Pocket Version* saw improvement last year in terms of its optimization on integrating development and operation, and the frequency and quality of its content updates. Meanwhile, we obtained more users through user acquisition and optimized content marketing. *Eudemons Pocket Version* performed very well last year and saw significant YOY improvement on revenue, online users and new users. I'm sure we will see even better performance in 2023. We have continued to produce content and launched 6 expansion packs for the entire *Eudemons* IP.

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For *Eudemons*, in the MMO genre, we attach great importance to long-term operation strategy, while building a system integrating development and operation. For users,

what matters most is the quality of the content we produce, for which we provide IP-crossovers and charity events aside from the expansion packs. Meanwhile, our overall integrated marketing is dedicated to maximize results from different dimensions. For example, we have expansion packs that dig deep into the gameplay and continuously provide new experiences to users. We also cooperated with various charity projects to enhance our public image, and we have IP crossover with movies to promote spending. We will do a better job of user acquisition and user retention based on everything above, and "break through the circle" (破圈) to win more users through innovative marketing initiatives. As you can see, the overall marketing expense to revenue ratio dropped year on year, meaning that our development, operation, and marketing have become more effective.

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Here I would like to focus on two aspects. The first one is continuously updating expansion packs. As can be seen from the data, every update of our key expansion packs significantly improved our user retention, new users and user payment. Therefore, we are keeping the pace of updating expansion packs at 3-4 months. I believe we can bring higher quality experiences to users with our upgraded content.

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Another aspect refers to what we achieved through the constant development efforts on IP-crossover projects. Our crossover with the famous movie *A Chinese Odyssey* was one example. Our annual revenue from IP crossover has been on the rise constantly, and so has our user engagement and reputation. In our crossover project with *A Chinese Odyssey* this year, we focused more on user penetration rate and overall brand image. Our ultimate goal for the crossover would be to improve user reputation and revenue simultaneously. With our experiences grew, we expect the IP crossover events will bear more fruit this year.

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In terms of the *Eudemons* titles, on March 23 we successfully launched the open beta of *Eudemons Mobile II*, most anticipated new mobile title since the launch of *Eudemons Mobile* in 2017. The open beta launch was very successful, with its first day gross billings exceeding RMB10M, and overall user appointment surpassing 6M. These are impressive achievements for MMO products, demonstrating our capabilities in the MMO genre and the loyal user base of the *Eudemons* IP.

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To us, *Eudemons* is more than just an IP, but also a brand that we are hoping to build in the long run. Aside from our existing product lines, we have formulated a more detailed plan for our *Eudemons* IP strategy this year, consisting of three categories that have been proven successful by the market.

For example, for the category of classic *Eudemons*, there are the PC version, the

pocket version, and the mobile version. From the market perspective, our most loyal *Eudemons* users would love the product line with a classical taste. Meanwhile, we have allocated additional resources to the categories of "quality upgrade" and "product evolution". For quality upgrade, there are *Eudemons Remake Version*, *New PC Eudemons*, and *Eudemons Pocket 2.0*. This product line will launch in 2024 and expand our overall user base and content products.

Lastly, for product evolution, we will continue to refine the world view building for the *Eudemons* IP and launch new *Eudemons* titles with an open view instead of the traditional 2.5D view, by developing an open world version of *Eudemons*. We are also laying out the ecosystem for *Eudemons* and striving towards the *Eudemons Metaverse*. We do believe MMO is the genre with highest affinity to the concept of metaverse, with rich online and offline social interactions. We are hoping to build a *Eudemons Metaverse* in the long run centered around our IP and continued investments.

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Next, I would like to introduce our *Conquer* IP. The *Conquer* IP has maintained its long-term revenue growth, especially for the overseas market, with its overall revenue up 9.5% and MAU up 7%, thanks to the successful implementation of our "MMO+" strategy. First of all, as we expanded to different countries, we would develop many innovative "MMO+" gameplay, such as "MMO+ light", "MMO+ casual", etc., allowing us to adapt to different cultures and user habits as well as blend into local communities and environments. We will continue to promote these strategies to drive growth, as they are already proven by our business results in the past 2-3 years.

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In terms of overseas strategy, I would like to discuss roughly in two parts, our existing businesses, and new businesses. For our existing businesses, we have come across "blue ocean" opportunities overseas for *Eudemons* and *Heroes Evolved*. We are focusing more on the construction of long-term competition barriers. For example, there are long-term offline promotions to engage users. Most of these offline operators are our distributors as well. They are all part of our ecosystem, ensuring our long-term sustainable growth. I believe it has also become even more resilient under the impact of the pandemic. As we further execute our overseas plan, we have started to produce more refined and vertical content. It has been validated in *Heroes Evolved* and *Conquer*, allowing us to make bigger investments in the future. That's our existing business.

For new businesses, our existing product *Under Oath* has signed a cooperation agreement with a well-known AAA game publisher to expand into overseas markets. This and the *Neopets Metaverse* will add new revenue streams for us. We will also step up our efforts in mergers and acquisitions, extending our validated strategies and scaling our revenue. These are also part of our plans for this year. I believe our overseas revenue will see better growth in 2023 and 2024 by implementing these

strategies.

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These are our pipeline for 2023 and 2024. Thanks to our increased investment in R&D last year, the number of products we release each quarter will be on the rise as well. They can be divided into two categories, the relatively stable product line consisting of new titles under existing IP like *Heroes Evolved*, *Conquer* and *Eudemons*, and the innovative category, under which we are still digging deeper into MMO+, covering new genres such as idle card games and other idle games. These genres are relatively in line with our "DNA", as they are relatively long-term and can fully leverage our advantage in the MMO category. The launch and distribution of these IP product lines will be favorable to our growth. For January and February 2023, we have been seeing very good trend for our overall revenue. I believe there will be much more to see in our financial reports this year.

In addition, I would also like to add some comments about the macro environment. In terms of policy direction, the positive role of gaming in technology innovation has been well affirmed. As the issuing of *Ban Hao* has become normalized, I believe the gaming industry is seeing a much brighter future. Meanwhile, we believe the AIGC technology recently emerged will be a huge favorable factor as well. We are already making use of the AIGC technology to reduce cost and increase efficiency for graphical and gameplay designs. It will obviously play an important role in our future production efforts. We also attach great importance to its part in creating brand new gaming experiences. Users ask for a large amount of content and benign social interactions in MMO, our main genre, and we are very positive about applying the AIGC technology to build intelligent NPCs, virtual hosts and virtual idols. These will be great opportunities for us as well. Driven by these macro trends, the technology waves and more importantly our solid pipeline, the gaming business of NetDragon will definitely see better performance in 2023 and 2024.

Thank you. I will hand it over to Vin.

Vin Riera:

Great. Thank you. Good morning, good afternoon, good evening, everybody. My name is Vin Riera. I'm the CEO of Promethean. I'm going to be talking about two things today. I'm going to talk about 2022 performance and review the highlights of last year. And I'm also going to be talking about what we're focused on in a go forward basis in 2023 and beyond. Next slide, please.

We saw a nice growth across our three main categories that we track. Revenue was up 31% year over year. We finished the year at 585 million dollars in revenue. We shipped over 253,000 interactive flat panels last year. That was a 38% increase year over year. And we're also able to increase our market share from 23 to 23.7%. So, across all three categories, we saw a nice level of growth.

Next slide. I talk a lot about our global footprint in these calls and looking at where we're number one. Simon already mentioned that we're the number one provider of interactive displays globally, excluding China. And I'm pleased to share that we're number one in nine of our top 10 markets by revenue contribution. This is a really important metric for us for a couple of reasons. The first is, we want to be number one in a market, we want to be the thought leader, and we want to be the market leader. but also equally as important as we build out a new pipeline of products, we want a strong installed base to go sell our new products. And what this shows is we have deep relationships globally with customers in our largest markets.

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We also launched our ActivPanel 9 in June, and we were able to launch it with a higher ASP. We're super proud of the new ActivPanel 9 product. It comes with upgraded hardware, it comes with active-sync, security features and recording features. This is a very strong product line in the market today. And the fact that we're able to sell this product at a higher ASP really shows that. When we've launched this product, we got multiple areas of feedback from existing customers as well as new customers. What our existing customers really liked about the product is it was a seamless transition from a previous version of a Promethean product into a new version of a Promethean product, except it has much better features and functionality than prior versions, but it was a seamless transition. What new customers liked about this product is that it was super easy to setup. It was super easy to install and very intuitive to use. So, when we take a look at how this product resonated in the market, as we look back over the last six months, we're super pleased with the progress that we made.

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We also acquired a company in 2022. We acquired Explain Everything. It's an existing SaaS product and it's a whiteboard product. Whiteboards are incredibly important to our customers. Over 95% of our customers utilize the whiteboard application at least monthly. And the whiteboard function that exists within Promethean is a great user experience, but it's a very basic user experience. As technology is increased and ease of use of that technology, we saw a lot of requests from our customer base to expand our offering and specifically our whiteboard offering. We're thrilled that we're able to acquire a market leader in the whiteboard space. Product is very differentiated. It's got collaboration features. It allows you to present, record and collaborate. And it's a product that sells today in the *App Store*. We sell it directly today to end customers, and we're super excited about our ability to integrate this product into other software offerings to increase the size of a software stack that we have going to our customers. That creates a great Promethean experience that allows our customers to be able to enhance that to whatever level they see fit. We're going to build on the monetization that started with this product in 2015, and we're excited to incorporate it into our existing offerings and our future offerings.

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One of the things that we also look at is we'd like to look at customer feedback, but we also want to see where our awards are coming from. I'm thrilled to say that we've got awards across the three most important categories, teaching and learning awards for use in the classroom, edtech awards for innovation within the edtech environment, and then also IT awards for ease of use and security by the IT administrators that will set up and connect these devices. So, as we take a look back at 2022, and as Simon said it, it seems like it was so long ago, we accomplished a tremendous amount of things aside from a number of awards. We grow our market share, which is incredibly important. We had strong revenue growth. We launched our new AP9 product, which is just setting the stage for future growth. And we acquired Explain Everything, which is SaaS revenue stream, and a product that we feel really good about.

So, if we go to the next slide, I want to talk to you about what we're looking at and what's to come and what we're actually working on. So, I'm going to talk about our path to integrate AI.

So, if we go to the next slide, we mentioned last year that we had a strategic partnership to take the two market leaders, Promethean as an interactive flat panel market leader with Merlyn Mind, which is the leader in AI assistant for education. And we signed an exclusive distribution agreement between the two of us, this agreement arrangement has been great. We've had the opportunity to get more Merlyn Mind devices in the market. We've also had the opportunity to hear the phenomenal feedback that we're getting from teachers that are using the product and the ease of use that it has. And what it's really enabling us to do is to see how AI is being used in the market today, and where we can bring AI in the future across our offering. We're also seeing an opportunity in working with Merlyn to roll out an additional AI integrated panel, which I'll talk about briefly shortly.

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So, just as a quick reminder of what Merlyn Mind is. Merlyn Mind is the leader in AI powered teaching voice assistant. And really what it allows is it allows a teacher to be able to operate anywhere in the classroom using voice AI. We can tell if a product is successful or if people like using it by the amount of times that they use it. And the way that Merlyn is able to engage, or teachers are able to engage with the Merlyn product is nothing short of stellar. The average user uses this over 30 times a day in the classroom. The top 17% are using it greater than 50 times a day, and the top 6% of users are using it a hundred times a day. When you compare that to a large offering like Amazon Alexa that is not specific to a specific environment, usage is significantly higher. So, we're thrilled to see that this product designed for the classroom is being used in the classroom as intended.

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So quick recap. When you take a look at today's classroom and where we're going,

there's all sorts of technology that exists in the marketplace today. But the devices are siloed, and there isn't any integration of AI in the classroom setting on a broad basis. Merlyn's the first to really step into that. Teachers are tethered to the blackboard/panel. They have to teach from the front of the classroom. They have to teach from their laptop, which is not always ideal. And there's just too many applications that are not connected together, which really leads to teacher fatigue and burnout. Our vision of the future AI enabled classroom is devices and applications are connected with AI. Micro automations between the products and applications that are most frequently used really enable a teacher to do what they're there to do, which is to teach. We're untethering teachers and engaging students. We're allowing teachers to roam around the classroom and teach in a natural way and use their voice to share lesson plans or do searches or show additional content. And it's just a natural interaction of tech for teachers and students. This is something that they do today, but it's bringing it together in a package that makes it much easier for them in the future.

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Our roadmap on how we're going to become a category dominant leader in AI enabled classroom solutions are, we're going to focus on delivering AI with our panel, and we're going to leverage our existing channels and installed base. So, we are working to deliver an AI-enabled panel in the next panel release. We're going to introduce our installed base, which is greater than 1.9 million classrooms to AI powered technology. And we're going to leverage the 275 sales professionals in over 2,000 channel partners to accelerate penetration of our new AI solution in the market. It's important to understand that this is a new technology and a new solution. We think that we can take a bigger share of wallet when we're competing for new front of class business. But I also think it's a compelling technology that makes teachers' lives easier. And in essence, it expands our total addressable market because I think instead of a natural replacement rate, people will replace their products sooner to get to the latest and greatest technology because it will really make a difference. We then can take, you know, the base that we're building of AI powered panels and expand our offerings with generative AI solutions for education. This allows us to bring new solutions to the classroom, and then we can also focus on what we can do not only for teachers, but also for students and administrators. So, we're taking this really healthy market that is growing and we're increasing the total addressable market with people coming toward new technology. And then finally there's a lot of excitement and enthusiasm around AI, but the ability to control what teachers are using or what schools want to see the educators using is something that people can control. And we're going to make sure that we incorporate controls into the AI so people can set up the settings that they want to use, the content that they want to use and overall functionalities that's customized to the school. So, we're putting a lot of thought into the products that we're going to be bringing to market.

Next slide, please. Excellent. Thank you. I will pass the time to Simon.

Simon Leung:

Actually, let me kind of take you back on what the enthusiasm you can see in Vin's presentation about us embracing the new technology. Whether it's actually Explain Everything, or whether it's the technology that we have and some of the future that we're working on, which is actually all-around AI. I think this basically has span across both businesses. However, I do believe it will make much quicker impact in education. I just want to reiterate Vin's point about expanding the market share, what we have done by embracing AI, we basically create a new category of market for us. So instead of looking at the traditional panel market, we are looking at somebody who's looking for AI to help whether the teachers, the students, or whether they're at home or they're in the classroom. So, we were able to address all that. So, number one is that we create our TAM in both ways. One is actually we'll take share. The other one is I do believe that we will also speed up the replacement cycle because it's the overwhelming kind of benefits of using our AI panels, which can be very, very exciting. The other thing is we're going to add to our revenue stream, which is actually we monetize AI by creating SaaS opportunity for us, which again alongside with Explain Everything, we do believe education for us in 2023 is a transformative year. Go back to gaming. We are equally excited about the fact that in gaming, we're also embracing AI technology, the whole concept of metaverse because actually that's what we do well for the last many years in MMORPG games but with a lot of new technology.

In case you don't know, we have made quite a bit of investment in the Metaverse area. I think Lin Chen talked about live streaming. We are investing in a company like that. We're also looking into investing into other companies that will enable us to embrace the whole concept of metaverse. Of course, that's going to be a multi-year effort to get us to a metaverse, but we are starting like last year and we're going to continue to make progress. With that, we are cautiously optimistic about 2023. There's going to be some challenges along the way because it's actually the economy around the world, some of the geopolitical issues. But we are very confident we have the good team to support us and we'll find ways to navigate through all these challenges and continue our business. With that, I am going to stop, and I think we can open up for Q&A.

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 tele-conferencing system, you may press star one on your phone keypad and our operator will put you through. Second, if you would like to raise questions on our webcast platform, please click the question mark on the screen and type your question in the Q&A box. We welcome questions in both English and Chinese.

Simon Leung:

No questions so far?

Moderator:

There is question coming in, we are checking. Okay. So, investors are very excited about our AI path. The first question investors would like to know about our Merlyn Mind AI technology. Is it a self-developed technology or is it based on any existing platform? Are there any other future applications in pipeline?

Simon Leung:

Vin, you want to take that one?

Vin Riera:

Sure. Yes. That is Merlyn's technology that they've developed. They've been developing it over the course of the past five years. We have an exclusive distribution agreement with the Symphony Hub for that product. And it is completely focused on the classroom, which is what makes it so differentiated. It's not generalized AI, it's specific to a teaching and learning environment. It's also specific to regional applications. So, whether it's the U.S. or U.K., it can be customized.

Simon Leung:

The other thing I want to say is actually it is based on Merlyn's own technology, but that said, it doesn't stop us from working with other people like ChatGPT, right? So, we are very open in working with other people because we want to integrate all the capabilities and offer the best solutions and addressing the best use cases that we have in education.

Moderator:

Thank you, Simon. Thank you, Vin. Our next question is also for our education business: our education business revenue growth in the second half of the year decreased. What's the reason and what is the revenue outlook for 2023?

Simon Leung:

Well, first of all, we don't give guidance. But Vin maybe you can address the second half issue. And don't forget I said it at the very beginning. I mean, it's actually the economy in Europe and all these different challenges. So anyway Vin, go ahead.

Vin Riera:

Sure. I would attribute the biggest reason for the decline in the second half of the year is what we saw was buying behavior based upon Covid funding that existed. And schools could make decisions outside of typical times that they make decisions. So, one thing, if you take a look back historically at the education performance with Promethean, it's been much more seasonal and much more cyclical. It doesn't mean that the volume changes per se, it just means that time of year that the volume that customers place orders change. What we saw was as things became essentially more back to normal and more normalized in the second half of the year, it started to feel like a more normal buying behavior where people go out to bid at this time of the year in Q1 and place orders in Q2. And that's what we saw in the back half of last year.

Simon Leung:

One of the things is actually if you look at our tradition in the last many years, I think Q2 and Q3 are the buying seasons. And then the market shifts a little bit. I think the market is actually kind of going back to the Q2 and Q3, so I think we get caught in terms of the shift. And if you look at the first half of last year, our growth is actually tremendous so that I think we should kind of look at the year over year growth rather than like half year over half year or quarter over quarter because of the shifting.

Moderator:

Thank you, Simon. Thank you, Vin. Our next question is also for the education business. We would like to know more about our SaaS business at the moment. So, what would be the contribution in 2023, and what is our expectations?

Simon Leung:

Vin, you want to take a crack first or, yeah?

Vin Riera:

Sorry, I missed the first part. What's the?

Moderator:

Our SaaS business? Can you give us a brief on our current development on our SaaS model?

Vin Riera:

I'm hearing the word SARS?

Moderator:

SaaS, that's right.

Simon Leung:

SaaS model.

Vin Riera:

Oh, SaaS model.

Simon Leung:

I'm sorry, we should speak American English.

Vin Riera:

I apologize. We have been focused on building on our SaaS business and we're super excited about the Explain Everything acquisition, because the whiteboard is the cornerstone of the use case with the panel. And what it allows us to do is take an existing product that did not have a very large distribution channel, incorporate into our distribution channel as the first step, put additional focus on using distribution methods like the *App Store*. But more importantly, building that product out and starting a tiered software stack that customers can buy what they want to buy from us for an enhanced experience. And we're going to continue to bring high value, high quality software solutions that solve challenges in the classroom.

Simon Leung:

If I may add to it. So, when the integrated AI panel coming out, there's a lot of opportunities for us to add and address the use cases. So that's also a great opportunity to continue to build our SaaS revenue stream. Like I said at the very beginning, we the management team intend to separately setup a session so we can talk about all these going forward in a little bit more detail. So, stay tuned. We won't be able to address all the details at this point in time.

Moderator: [Translated from Mandarin]

Thank you, Simon, thank you Vin. Our next question is for gaming business: it seems that the overseas composition has been rising, what's our pipeline for overseas market like? Thank you.

Simon Leung:

A good question. Lin Chen.

Lin Chen: [Translated from Mandarin]

OK, I will. We will explain by two categories, the existing games and new games. For existing games, our *Conquer* IP will launch more differentiated and fusion gameplay based on MMO+ strategy. On the other hand, we will launch an enhanced version of the existing *Heroes Evolved* IP along with *Heroes Evolved 2.0*, which will surely bring the MOBA experience to the next level.

As Simon mentioned earlier, the metaverse version of Neopets is set to hit the market, while *Under Oath* in collaboration with the AAA publisher is scheduled to debut in Japan in Q4 this year, and will gradually be rolled out to more countries. Meanwhile, in the overseas segment, both our new *Code: DPS* and *Code: Xianxia* will be launched overseas. As for *Eudemons Mobile II*, which we believe has more room for optimization, will also be available to users next year in an overseas version launch. I also believe the rich pipeline of *Eudemons* will help to drive our overseas revenue. Thank you.

Moderator: [Translated from Mandarin]

Thank you, Lin Chen. We would like to welcome a question from our teleconferencing system. Operator, please put through, thank you.

We have Mr. Hu Kun from *Zhonggeng Fund,* please start.

Hu Kun: [Translated from Mandarin]

Thank you, management. I want to ask for your help about our outlook for dividend policy.

Simon Leung: [Translated from Mandarin]

We can't hear you clearly.

Moderator: [Translated from Mandarin]

Mr. Hu, would you please raise your voice a little?

Hu Kun: [Translated from Mandarin]
Apologies, now is it better?

Moderator: [Translated from Mandarin]

Very clear now, thank you.

Hu Kun: [Translated from Mandarin]

OK. Thank you, management. I want to ask the outlook for dividend policy. You have mentioned in previous earnings calls that most of our operating cash flow will be used for share buyback and dividends. But it seems our 2022 dividends figure has missed this target a bit, we are not sure what should be expected in the future?

Simon Leung: [Translated from Mandarin]

Ben, please take this question, it isn't "missed a bit", right?

Ben Yam: [Translated from Mandarin]

In regards to our dividend policy, we have announced a 40 cents dividend. In the future we will continue to maintain a stable payout ratio. We also need to maintain enough cash to capitalize on various opportunities. So, I think we will maintain a stable dividend policy in the future.

Simon Leung: [Translated from Mandarin]

Let me add to it, because we have also paid out a special dividend in 1H last year. Maybe you will consider that as a onetime thing, since it's called "special dividend". But actually, we haven't changed our dividend policy, our strategy about shareholder return hasn't changed.

Hu Kun: [Translated from Mandarin]

Understood. But you said operating cash flow before, in the future you will payout dividends according to profit, right?

Simon Leung: [Translated from Mandarin]

I am not sure if Ben has mentioned before, we've also done some share buyback. We are using various tools for shareholder return, not only dividends.

Ben Yam: [Translated from Mandarin]

We've announced before, we will return to shareholders majority of our cash that we generate annually, in a combination of buyback and dividends.

Hu Kun: [Translated from Mandarin]

Got it, thank you, management.

Moderator: [Translated from Mandarin]

Thank you, Mr. Hu, thank you, Simon, thank you, Ben. Our next question comes from *CGS-CIMB*，Ernest. The question is, dear management, thanks for the informative presentation. I understand that your plan is to significantly expand our pipeline of new games. Can investors look forward to new games to be launched in the next three months?

Simon Leung:
Do we need to answer in English or in Mandarin?

Moderator:
I think in Mandarin should be fine.

Simon Leung:
OK, LIN Chen.

Lin Chen: [Translated from Mandarin]
For the next three months, we anticipate *Code: DPS* will be tested overseas, and the open beta will be in end of this year. This is our nearest launch. Another one will be *Under Oath*, which is planned to launch in Japan in Q4, according to our publisher. *Eudemons Mobile II*, *Code DPS*, and *Under Oath* are the three games we mentioned earlier. In next year, there will be more new launches from us.

Moderator:
Thank you, Lin Chen. The next question from Ernest is that given the exciting development in our education segment, do you think it's likely to continue the trend of narrowing the segmental loss of the business, such that it may hopefully break even in 2023?

Simon Leung:
You're asking for guidance again. So, we are going to pass on that one.

Moderator: [Translated from Mandarin]
Thank you. Dear investors, if you would like to raise questions through the tele-conferencing system, you may press star one on our phone keypad and our operator will put you through. Our next question is also for our gaming business, it's from *Weighted Research*, Wee Hiang. He would like to ask by expanding *Eudemons* into so many versions, will it dilute the user experiences, or dilute the existing players too thin?

Lin Chen: [Translated from Mandarin]

This is a good question. The reason we went ahead with the IP product line planning is also intended for this purpose. In the past, the message delivered to users was relatively vague with both *Eudemons Pocket* and *Eudemons Mobile*. In our IP product line planning this year, we have clearly divided our product line into classic *Eudemons*, which is ideal for players who are particularly keen to preserve the classic settings of *Eudemons*.

With regard to quality upgrades, we will definitely make significant graphical upgrades to the existing *Eudemons* and optimize the gameplay, so that this product line will be more suitable for *Eudemons* users who are more receptive to new concepts and gameplay. At the same time, it will be compatible with a wider range of IP users and more churned users, a segment that we will differentiate in terms of promotion and strategy.

In the same time, we will launch the product evolution part for *Eudemons*, which will be geared more towards a more general and broader audience beyond the IP. In fact, in terms of product positioning and marketing strategy, we will have clear differentiation to cater to different user groups and expand the user base of *Eudemons*. In the past few launches, we have found that the new products have not greatly affected the existing products, which has also given us great confidence. We hope to continue to broaden our user base in the future through product positioning and marketing strategies, which is something we pay particular attention to in our overall game development and operation.

Simon Leung: [Translated from Mandarin]

I'd like to reiterate what Lin Chen mentioned just now, we are expanding our user base, not only just serving the current users. I think this is the most important part.

Moderator:

Thank you, Simon, thank you Lin Chen. Our next question is also from Wee Hiang. What is our current plan or schedule on the spin-off of our education business?

Simon Leung:

What do you want me to say? So, the only thing I would say is actually either no comment or stay tuned.

Moderator: [Translated from Mandarin]

Thank you, Simon. Our next question is from analyst of *Guangfa Securities*. The gross margin of education business dropped a lot in 2H, approximately from 30% to 20%.

The company said it's mainly due to forex impact. Then what's the outlook for the gross margin in 2023? Thank you.

Simon Leung:

Either Ben or Vin, maybe Ben, you can take it.

Ben Yam: [Translated from Mandarin]

Since USD was quite strong in 2022, our gross margin has been dragged down. For 2023, we need to follow closely the USD forex rate this year, if it weakens, our gross margin will better. So, I think it's quite hard to give a clear outlook. But from an ex-tariff and forex neutral basis, we will maintain a stable gross margin.

Simon Leung: [Translated from Mandarin]

Or let me add a bit to that. Frist because 1H23 we will be shipping mostly AP9, comparing to the combination of AP9 and AP7 last year. Since we have launched new products, there were some pressures to the older model. So, this is another reason apart from forex.

We will launch the AI integrated panel in 2H this year, this is a product category without any competitors, so we will be able to maintain a higher ASP. So, we are handling the situation from various angles. Another reason is we are selling in Europe in local currency, and we have set up strategy to handle this problem as well.

Last thing about gross margin, we have put some efforts to the cost control, this year the supply chain will be rather stable, which we saw some signs in 2H last year. This will also help our cost. So, in all, we are still cautiously optimistic that we will maintain a healthy gross margin.

Moderator: [Translated from Mandarin]

Thank you, Simon, thank you Ben. Our next question is from Franky from *Integrated Asset Management*. The core segmental loss of education for the year is RMB299 million, comparing to only 36 million for the 1H. would you please explain the reasons for the differences between 1H and 2H?

Simon Leung: [Translated from Mandarin]

As we have mentioned earlier, our 2H revenue was lower than 1H, as we had a considerable revenue growth in 1H. this is one of the reasons, and Ben can explain later in details why the bridge exists. From the full year perspective, as we explained many times before, there is a cycling effect to the business, and last year's cycle is quite different than normal years. This year it will resume to previous norm.

Ben Yam: [Translated from Mandarin]

On a high level, our fixed cost and opex are relatively stable in the first half compared to the second half. But our revenue is significantly higher in 1H21. So, we incurred more loss in 2H, since our cost is fixed.

Simon Leung: [Translated from Mandarin]

Ben, our 1H revenue increased quite a lot year over year, right?

Ben Yam:

Over 70%.

Simon Leung: [Translated from Mandarin]

So, you can see that 1H is different, with 70% increase.

Moderator: [Translated from Mandarin]

Thank you, Simon, thank you Ben. Next question comes from KL from *Everbright Securities*. For the gaming end, what's the recent progress of *Neopets Metaverse*, and what's the overall plan to further expand the IP?

Simon Leung: [Translated from Mandarin]

Lin Chen, do you want to take the question, or should I answer the *Neopets* question? Maybe you?

Lin Chen: [Translated from Mandarin]

You please.

Simon Leung: [Translated from Mandarin]

Sure, I'll do it.

Neopets is being developed in two areas. One of it is the older classic version. The other is on Web 3.0. We've already launched an alpha version last year and we have a major announcement coming up that we can't reveal yet. Personally, I think there are many exciting developments, whether in terms of partnerships or game development. Please be patient with us. The announcements will be made soon.

Last year is a challenging year for all blockchain games, and we're adjusting our strategy in this area to see how to proceed. Generally speaking, the company is still quite positive about Metaverse gaming and consider it to be an important part of our strategy.

Moderator: [Translated from Mandarin]

Thank you, Simon. The next question is being asked by several analysts. They hope Lin Chen can share his overall gaming sector forecast for 2023, especially in the areas of revenue and profit. They would also like to know how we will be managing the game user community now that it has expanded to a considerable scale. What are your plans for the future?

Simon Leung: [Translated from Mandarin]

I'd like to point out first that we do not give guidance. What you're asking is for guidance. As I've mentioned before, we're cautiously optimistic.

Lin Chen, go ahead and talk about the user community.

Lin Chen: [Translated from Mandarin]

In terms of community management, we are conducting it by several tiers. First is in-game. After all, ours is a gaming product, and it is our top priority to promote activity and interaction among users in the game. As I mentioned earlier, our top priority is to ensure users spend more time in our games, and as more expansion packs are released, our top priority is to keep users within the *Eudemons* ecosystem, regardless of whether they prefer a more classic version of the game or a more creative one.

The second tier involves introducing various new user reaching channels. I mentioned *Eudemons Online* just now, it also has a *Cross Platform Version* that has interoperability with mobile devices. Beyond gaming content, it also comes with desktop or wallpaper functions that have worked very well to keep users engaged.

Thirdly, we will merge the playing and paying user bases for all our current titles, to integrate marketing and operations. We will reorganize our user community management efforts through the VIP system and enhanced online services.

For the next step, many other companies in the industry will create a community app. We've tried this before but we think user retention via content is still the most important aspect, so we are more focused on creating more content. We'll also develop and publish an app in a more appropriate time. It is an integrated approach because there is seldomly one single channel that can retain a user's attention continually. We must develop and operate several closely-related channels to that end. We fully intend to do this long-term and believe that as time goes on, we'll get better and better at it. Thank you.

Moderator: [Translated from Mandarin]

Thank you, Lin Chen. Let's welcome our last two questions. The first one is about future share buyback plans.

Simon Leung:

Over to you, Ben.

Ben Yam:

Yes, I'm here. Sorry, my line was cut, I just lost the last part.

Moderator: [Translated from Mandarin]

First question is about our share buyback plan.

Ben Yam: [Translated from Mandarin]

Our share buyback plan hasn't changed, as I mentioned before, or roughly one and half years ago, we announced the plan to giving back substantially or majority of our annual free cash flow to all shareholders. We intend to maintain the cash return of our investors, by either buyback or dividends.

Simon Leung: [Translated from Mandarin]

It's important to note that we will boost shareholder return by not only share buyback, but also dividends. So, I wish you can take consideration to the combination of both.

Moderator:

Thank you, Simon, thank you Ben. Our last question is for Vin. Because our Promethean has maintained a leading position in the market for a very long time, what is your expectations for the demand in 2023 and 2024? Given the macro backdrop are quite weak in these two years.

Vin Riera:

So, I'll answer it without giving any guidance. The interactive flat panel technology we are at the stage of market adoption today where customers that were early users of the technology are now replacing the technology with new interactive devices. Customers that used to buy whiteboard technology, there's now products in the market in the interactive flat panel world that are in line with that, so the addressable market from a replacement cycle is bigger. And then there's still large portions around the globe that have not even adopted this technology yet. So overall there's a significant amount of classrooms that don't have any type of front-of-class technology which is all green space for us.

Simon Leung:

If I may, I'll basically summarize what Vin has said earlier. One is actually continue to

gain share. That's part of the growth strategy. The other one is actually he managed to expand our addressable market by introducing our value panel. I think we did talk about it may be within, I forgot, so, because we have been tallying the high-end, but we're going to introduce a value panel. So, our TAM actually has increased, this is really happening when looking at Promethean. Last but not least, is actually what Vin has spent a lot of time talking about, creating a new category which is actually AI enabled, which is actually the first one to the market. So, our TAM actually can expand even in a down market. I think that's the plan.

Moderator:

Thank you, Simon, thank you Vin.

Thank you very much, thank you Dr. Leung, Ben, Mr. Lin and Vin. 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 one-on-one meeting arrangement. Thank you. And we wish you all have a great day.