

NetDragon(0777.HK) 2020 Annual Results Conference Call and Webcast

10:00 AM, March 26, 2021 Hong Kong Time
(10:00 PM, March 25, 2021 Eastern Time)

NetDragon's Management Team

Dr. Simon Leung, Group Vice Chairman and Executive Director
Mr. Vin Riera, CEO of Promethean
Mr. Lin Chen, Group Senior Vice President
Mr. Ben Yam, Group CFO

Moderator:

Dear friends. Good morning. Thank you for joining NetDragon Websoft Holdings Limited today for our 2020 annual results presentation. Our presentation PPT will be broadcast on the live streaming platform. That 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. Well, good to be here. We have not been together for a while now, so it's great to get together once again to go through 2020 and also our quick outlook of this year, unfortunately, because of the COVID situation, we have to do it virtually. So that's why we decided to make it very formal, we're wearing a jacket. All kidding aside. So we have the team here. It's actually with technology, Vin has been in Seattle and, Lin Chen is in Fuzhou and Ben and I are in Hong Kong. So we're going to get together virtually.

Because we issued a press release last night, I'm sure you guys have a chance to kind of study it. So what I'm going to do and the team will go do is actually just to keep it at a high level and then we go into Q&A. So with that, I'm going to start with my presentation. So I talk about the team, the agenda etc. I go through the highlights and trust me, it's going to be highlights, Vin will talk about Promethean more in the sense of blended learning, Lin Chen will talk about gaming, Ben will go through the financials. I'll talk a little bit about one of the programs that we've embarked on last year, which we will continue, for a long time to come, which is actually a country rollout. And I'll do a high-level outlook for the rest of the year, and then we'll go into Q&A.

Well, I just have to bring everybody back to last year. It's a very interesting year. I've been around for a long time, but I have never kind of seen a year like that. I do remember, I think it was about February last year, I was sitting in Vancouver talking to Vin about the year and say, wow, I mean, COVID coming, blah, blah, blah, blah.

So we did a lot of work to get ourselves ready, just in case we have a down year. So the results surprised all of us in a very good way. So let me kind of go through the results and then we can talk about everything else. Yeah, we were quite happy with the result, of course we can always do better.

I mean, revenue, we hit over RMB 6 billion, almost a billion USD. Actually the one I really like is that operating profit, which is actually RMB 1.1 billion. Our net profit is actually close to a billion

RMB. One of the metrics I should have put on, actually my fault, is actually our cash generation. We can generate RMB 1.3 billion of cash last year, that brought us to a very strong cash position. So we are sitting on about RMB 4 billion of cash, which is about 700 million US dollars of net cash.

And so you know our performance in revenue and earnings. Gaming is that's kind of like repeated theme in a down year, in a sense of the economy, we continue to grow exactly for the 10th consecutive year, I've been here six years, every year we grow and we grew in a very tough year. The other thing that is really encouraging is actually we've been promoting this idea it's actually, we want to enable learning whether you're at home, whether you're in the classroom or whether you're on the go, which is at your mobile. We talk about ecosystem. We talk about a lot of things before, but at the end of the day, it's really everything about blended learning. So we see that the market is actually coming to us last year because of COVID, I think it's coming to us, we got this, but I think COVID actually fastened the pace.

So we benefited and we talked about the country rollout. We will talk about more like a case study on what we are doing with Egypt and what we are doing with some of the other countries. So, let me kind of very quickly talk about blended learning. And I did, but just to confuse you, I put up a very complicated map, just to tell you, this is actually something we have been pushing for the last five years under different names, we called it the ecosystem, but now we can officially blend it into our blended learning solutions. This will also see all our products actually coming together under one vision very clearly, including Promethean, Edmodo, those two big companies that we have. So a lot of synergy between those two companies. And then we are leveraging that to support our customer, whether you are a teacher, whether you're a student, whether you're parents and whether you're a single school whether you're district in the US or a country. So the role is actually very clear for us in terms of blended learning.

So, with that, I'm going to turn it over to my friend Vin, he's going to take you through a lot of the good things that happened with Promethean actually more with blended learning. Vin, take it away.

Vin Riera:

Great. Thank you, Simon. Good morning, everybody. My name is Vin Riera and I'm the CEO of Promethean.

2020 was definitely a dynamic year for Promethean. The traditional way that our products were bought and used in a classroom setting evolved rapidly. We saw different districts adopt hybrid learning environments where teaching and learning takes place in the classroom or remotely. We saw blended learning environments with some students in the classroom, and some students working remote. And each of these cases, we have positioned our interactive panels and lesson delivery software as an essential and adaptable tool for educators around the world. For me, being continued to be the market leader.

Promethean continued to be the market leader in 2020 with 24.6% market share. Our volume growth rate of 16.4% reflects the market acceptance for interactive flat panels in a classroom setting, as well as remote learning or hybrid learning environments. Our customers continue to purchase our products as their students returned to the classrooms. Regardless of the learning environment, our front of class device shifted to become an integral part of a hybrid learning experience for students that remained remote. Our market leadership in 2020 is a reflection on the company's ability to embrace the shifting market dynamics of remote and hybrid learning. Next slide, please. In our top 10 markets where we are either the market leader or close second, we offer at least two products in each market. Our value of Nickel offering or our premium Cobalt or Titanium offering. Having product differentiation allows Promethean to compete at the middle to high end of the market.

Our philosophy has and continues to be, to offer a product that enables us to lead the market that is designed for use in the classroom and could be sold through our global distribution channel. Our approach to market leadership is to do so thoughtfully so growth in any given market is always balanced with our ability to do so profitably. This enables us to sell our products to customers that are seeking a product designed to be used in a classroom and hybrid learning environment.

While discussing market share, there are four different markets that I want to highlight on this slide. The United States is our largest market in terms of overall size. The US is large and growing market that has significant installed base of schools using interactive whiteboards that are now transitioning to interactive flat panels. This allows Promethean numerous opportunities to upgrade our existing customers to interact with flat panels, as well as compete for share with that new customers looking for new hybrid learning solutions. Education technology and funding in the US was strong in the first half of the year. And then significantly increased when the CARES Act was announced. The CARES Act is an economic stimulus bill passed in response to the economic fallout of COVID-19 pandemic. This increase in funding will carry into 2021.

Egypt is the second largest market and represents an important part of Promethean and NetDragon's business. The business that we do in Egypt was done at the country level instead of with individual schools and it's part of a broader initiative with Egyptian Ministry of Education, Promethean and NetDragon. This is an exciting part of our business and represents an offering that we believe we can replicate and work with Ministries of Education in different countries.

The UK market is our third largest market where we have 26.1% share. The majority of the business that we do is transitioning schools from IWB to IFP, either with our legacy customers or competitive wins. The UK market was the first to adopt front of class solutions and as a region where we gain insight into replacement cycles in our more mature markets.

The last country I want to mention is Germany, where we're currently the number two provider in the market. The two market dynamics that will drive growth in Germany are "Digital Pact" funding source, which is a multi-year, multi-billion-dollar funding stream for education technologies, and a rapid adoption of the interactive flat panels. There are nearly 60% of the classrooms that do not have any type of front of class device. Our strong brand and key wins in this market will help propel our growth in 2021. Next slide, please.

This slide shows the continued growth of interactive panels over the last five years. This year-over-year growth highlights the strong demand for our products in the past. And you can see it carry on throughout 2020. Promethean embraced new and innovative ways to market and remotely demonstrate our products as well as some new ways to train our customers and share best practices on hybrid learning techniques. As Promethean worked with our customers in the early stages of the pandemic on implementing hybrid learning environments, we never stopped building pipeline, and that pipeline ultimately converted to orders in like Q3 and Q4.

Next slide please. This slide shows the strong revenue momentum in 2020, as you can see our year-over-year revenue growth rate was at 5.6%. However, our second half revenue growth rate Half-over-half was 8%. This increase in the second half speaks to the demand of our products during the year where our customers sought out new and innovative ways to educate students both in and outside the classroom.

The second half growth illustrates how the market adapted to the change in blended learning and continued to buy interactive panels as part of these newly implemented solutions.

Next slide please. Although materials drive majority of our COGS spend, we do prioritize efforts to reduce costs in several other areas of significance, including freight, warranty and warehousing. In

2020, we drove operational excellence across these categories in three ways. First, we improved our data to understand and identify spending drivers. Next, we established benchmarking to understand what good is. And third, we developed programs to specifically generate savings within these categories. For example, we strengthened our freight and warehousing procurement process to establish long-term partnerships while increasing competition and market visibility. The end results we brought in a new ocean freight partner, drove cost down on our ground freight and created a scalable cost structure for warehousing. Looking at our warranty operations. We experienced lower failure rates due to COVID-19, which in turn provided temporary improvement and warranty costs. We worked with our manufacturing partners to drive quality improvements, allowing us to optimize the cost, to provide warranty services to our customers. In other words, deciding between buying a warranty or self-warranting a product based on lowering costs over the long-term. All these efforts created operating leverage with cost growing slower than revenue. Promethean's commitments to continually enhance our operational efficiency and control costs was an important factor in our year-over-year margin improvement in 2020.

Despite the year-over-year increase in revenue and volume, Promethean recorded an overall reduction on freight, warranty and warehousing in 2020. These efficiencies helped us improve our margin from 30.1% in 2019 to 33.6% in 2020. Next slide, please. Another key differentiator for Promethean is our network of global channel partners that we've been working with for years. Recently, we added focus and resources to recruiting new resellers throughout the world. In 2020, Promethean successfully added a hundred new resellers to our network. All of the new partners added to the Promethean distribution network commit to our onboarding and training program. As our new partners are trained and their knowledge grows on the Promethean products, I expect the sales pipeline growth to follow. Promethean ended 2020 with over 1000 distributors and resellers covering 105 countries worldwide.

Next slide please. In 2020, we successfully transitioned from a company that sells interactive flat panels with lesson delivery software, to a company that's part of a blended or hybrid learning model. Our product value proposition puts us in a unique position to capitalize on the blended learning environment. Promethean shifted our resources and focused on connecting with our customers and prospects with virtual sales and marketing efforts. Our shift from being face-to-face to virtual is similar to what education segment experienced in 2020, moving from classroom instruction to hybrid learning. Many of the best practices that we developed last year will carry forward for years to come.

Let's move on to why customers buy from Promethean. Next slide, please. We're able to make the shift to hybrid learning because we have the right brand equity, the right product value, and we sell our products at the right price. I want to start with brand equity. Promethean has been in the education market for over 20 years, school administrators, teachers, and resellers know our product. And we've been part of the educators' technology journey for the past two decades. When our customers had to change the way they teach due to the pandemic, they trusted and they relied on Promethean. We designed our products to be engaging for the teachers and students, and that engagement carries forward with virtual instruction. That means we focus on how teachers use our panel and lesson delivery software when teaching their lessons. There's a real value that we deliver to our customers and every panel that they use. Finally, we honed our skills at creating an innovative, interactive panel for the education segment that has unique and intuitive features and functionality that deliver at the right price point. Creating this experience for our customers in the education market is part of Promethean's DNA.

Next slide, please. In these last few slides. I want to share with you the reasons why customers do business with us and share a powerful case study on why a large school district in the US chose Promethean as part of their hybrid learning solution.

Next slide, please. In Q4 of 2020, Promethean commissioned Forrester Research to do a total economic impact study, one of the important outputs is reflected in this slide. Not surprisingly, Promethean's interactive panels increase teacher satisfaction, which in turn has a positive impact on student attendance, retention, test scores and graduation rates. This study was beneficial for Promethean as it confirms that teachers like our products and when teachers have the tools and resources that they can depend on, they have a positive experience, in turn that positive experience resonates in their teaching and the way they engage with their students.

Next slide, please. We have numerous examples of where we've successfully implemented hybrid learning environments for our customers in 2020, the case study I want to share with you is about a large school district that we won in Q4 of last year. We're working with this top district in the US that needed to implement a hybrid learning environment across 230 schools supporting 155,000 students in a blended learning environment. Our goal is to support the teachers instructing students that were remote. The solution was having the teachers use our interactive panel with a video camera capturing the lessons, and then streaming those lessons to students on a district provided one-to-one device. In this hybrid teaching model, students in the classroom and students that were remote could have similar learning experiences. The incumbent provider was not able to find a way to configure the camera nor did their panel have the processing ability to allow the camera to function properly.

The Promethean panel's unique capabilities and our company's expertise in working with schools to implant complex applications, propel the district to shift vendors and begin placing orders with Promethean. We project nearly USD18 million in revenue from this district this year, I expect we will implement solutions like this one across the globe in 2021.

Next slide, please. In my final slide, I want to share the areas that Promethean will continue to focus on in 2021. Promethean will build on our global K-12 leadership, meaning we'll leverage our unrivaled brand recognition and trust that we've established in the market at a global scale. We will continue to grow our sales channel and enter new markets while developing new business opportunities in emerging markets, by leveraging our longstanding partnerships. Promethean will also stay on track to expand market penetration by evolving our hybrid learning applications that resonate with teachers across various learning environments. We'll also continue with our robust digital and virtual marketing efforts to maintain our market leadership. Finally, Promethean will capitalize on the accelerated trend of blended learning due to COVID-19, a trend that we expect to carry on well past after the pandemic. We will continue to align our products with funding sources and leading the pursuit of winning nationwide tenders like we do in Egypt. Thank you for your time today. I'm now going to turn the call over to Dennis.

Lin Chen:

Greetings. I'm Lin Chen and I'm happy to go through NetDragon 2020 full year results. For our gaming business, our overall strategy is centered around our IPs and genres that we are good at. We are building our core competitiveness, you can see that in the past 10 years, our gaming business maintained continuous growth, especially our flagship IP Eudemons. It has maintained 6 years growth. In the first half of 2020, there was challenge from the pandemic, real name registration and anti-addiction measures, we're happy to see that in the second half of 2020, growth of our overall gaming business revived, there's 8% year-on-year growth, so we believe that our gaming business has already restored an upward trend from last year's challenge.

Next slide. On this slide, I can share with you our core IP data. For a gaming IP, the stability and continuous development of core metrics as well as core users are the key to the gaming business' healthy development. If you look at MMO category, it is a category we are good at. We have our flagship IP Eudemons and Conquer Online. We also have Heroes Evolved and Neopets in other gaming genres like MOBA, causal and digital pet. And then if you look at IP layout, Eudemons has

big influence in China, and there are also Conquer Online and Heroes Evolved. And Neopets is a renowned IP with many users overseas, so overall speaking, our pragmatic planning for genres and accumulation of IPs have laid good foundation for our future growth and also growth in our revenue.

Next slide. First, let me talk about our Eudemons IP. For Eudemons IP, in 2020, it achieved very good results, you can see that for this MMO category, the most important thing is user base and good user ecosystem. So this is the foundation of MMO as a long-term profitable game. If you look at Eudemons, no matter whether you look at MAU, DAU, ACU and PCU, in 2020 there was big growth. If you look at Eudemons Online, in terms of MAU, and DAU, there was even more significant growth, so if you look at the revenue data, you can see that in Q4 2020, Eudemons Online in one single month, revenue achieved record high. This gave us a lot of confidence. This shows that it has very strong economic moat in this MMO category, so when we continue to invest in the IP, we will be able to enjoy good core competitiveness as well as profitability.

Next Slide. MMO is a content-based game, so you need to launch new content continuously in order to maintain users and increase revenue. In 2020, we invested more in contents with IP crossover and also cross-sector collaboration and also in the Eudemons big world vision, we have created more and more good contents and we also launched different versions and expansion packs, and these are able to create user stickiness. We're also happy to see that the spreading and fermentation of such contents have brought in some new users. They have created new talking points as well. These are good foundations for healthy development of MMO games.

Next slide. For NetDragon, in terms of gaming IP, we keep on making long term investment, so our understanding is that a gaming IP is actually a kind of expression of users' emotions proven in the market, so Eudemons, as an IP, can succeed and can grow sustainably because we are able to deliver good emotions and passionate feelings to users. If you look at Eudemons IP, our goal is to create a gaming IP with 10 billion gross billing [annually] and now we have 4 billion gross billing. And there is still a lot of room for growth. And if you look at these three different paths, we can still continue to grow this Eudemons IP. First, the original IP. We can continue to offer or launch more different versions or extensions, for example, Eudemons Mobile II, Legend of Eudemons versions. At the same time, this kind of passionate and exciting feelings have proved to be continuously favored by users. At the same time, we will use newer and also CGs well-liked by young people to continue to launch new versions. The CG upgraded in 2020 and also our next generation UE4 Eudemons allow our gaming spirit to be passed onto more new users. At the same time, MMO as a big category, is the most complicated, the most in-depth gaming category. In different gaming categories and layout, there are also some integration and innovation opportunities, so through the fusion or integration between MMO and other categories, we will offer and launch more new series of Eudemons. Next page, you can see UE4 version of Eudemons, so this shows the direction of MMO development.

In other words, there would be better CG and better immersive experience, open world and new gameplay so that our users would have better [gameplay] experience and better content experience. For Eudemons UE4 mobile game, it is also one important direction for our investment and this shows a higher standard and level in the MMO category.

Next slide. Now I would like to talk about our next gaming MMO IP and that is Conquer Online. There are many highlights. On one hand, if you look at stability of our users, the users of Conquer Online IP are very loyal, at the same time, in our overseas single market, our Conquer Online game in Egypt has already become national level game. It is not only a game, it has been developed into a gaming platform or a token platform and we have attempted many new business models which have achieved good result.

Now with respect to the Conquer Online IP, we are full of confidence in the future developments. Firstly, our successful experience in other MMO games especially Eudemons, including ways of content production and mobile strategies, can be replicated to Conquer Online IP. Conquer Online IP's successful overseas experience can be replicated to countries like Philippines, Indonesia and Malaysia apart from Egypt. In 2021, we're going to promote and expand our influence and revenue for Conquer Online IP.

Next page. Next, the IP of Heroes Evolved. In 2020, this IP continued to be popular among young players. Compared with Conquer Online and Eudemons, the biggest difference of Heroes Evolved is that its user structure is very young. It is really well-liked by young players. Most users are below 25 years old. In the past year, we continued to do crossover with tier-1 IP. As a result, there's high quality ACGN user base. And these users have given us good foundation in terms of activities and spending of our users. We also attracted a new batch of users during our IP crossover. In 2020, on Heroes Evolved IP, of course there are negative impacts from the real name registration and also anti-addiction measures. But starting in second half, this trend has become stabilized. Next page. In 2021, we will continue to launch some well-tested and successful approaches including crossover with tier-1 IP especially in competitions, so in the past few years of our exploration in terms of live streaming and competitions. Not only has it brought higher user activities, it is also a very positive business model. MOBA, as a big category, actually has a big user base and for this category, if you look at R&D expenses and also new gameplay, these can bring a lot of opportunities, for example, auto chess model is based on the MOBA gameplay. So in the future, we'll continue to do more exploration and R&D.

Next slide. Here you can see our new game pipeline. First of all, on our IP, no matter whether we're talking about Heroes Evolved, Eudemons or Neopets, we will continue to launch new games, for example, Eudemons, in 2021, our Eudemons Mobile II and Legend of Eudemons will be launched in the market. For Heroes Evolved, there will be innovation in integration of gameplay. It may be launched in the form of game add-on or app. So all these could be our possible attempts. For Neopets IP, we will launch new games with Match-3 and Island Builders. In 2021, and also 2020, we'll have increased R&D expenses in Under Oath, Xian Xia, Game-Z and Sword. These are new games that are all oriented around our core competitiveness, no matter whether we're talking about MMO and also integration with ACGN and also other new gameplay. So as a result, we may be able to come up with some blockbuster games. So this is a result of our continuous R&D input.

Next page. Now I'm going to talk about the highlights and unique characteristics of new games like Under Oath. It is an ACGN MMO game that we work in collaboration with Bilibili. We have spent a lot of time developing this game because in this ACGN category we hope to offer a very exclusive product. Bilibili has given us a lot of help on that, so we hope that this year, we'll be able to get good results and achievements when the game is launched.

Next slide. This is Eudemons Mobile II. It is unique in the sense that it is an extension of our traditional version. We are using new engine technology and CG to bring the original Eudemons experience and it will be launched within this year.

Next slide. This is Legend of Eudemons within the Eudemons series. Its unique characteristic is that it is an H5 version. It is based on typical or classic Eudemons IP. In terms of gameplay, there is some enhancement and it is more suitable for some general users and it is H5, so I think it can reach more existing users and some general users as well as some new types of users. It's an important attempt in reaching new types of users. So it will be launched in Q2 this year.

Next slide. This is the new game - Neopets Island Builders. The gameplay is very unique, it includes building of a big world and also exploration. For Neopets IP, in the past 20 years, we have accumulated the whole world vision and storyline. There is a huge user base and we believe that

it is going to deliver a very different experience and it is going to be an enhancement, a new level-up for Neopets IP.

Next slide. Overall speaking, you can see that in the overseas markets, in the past few years, we had good results. In 2021, apart from the existing four games which can be published overseas, in 2021, we will develop and launch more games in the overseas market including our Eudemons series and also our Neopets games. So in 2021, overseas revenue will continue to grow. Next slide. Here you can see that for our overseas growth strategy, we're going to have some very unique strength in category as well as regional advantage. So we're going to invest more in overseas regions. At the same time, you can see some good development of Chinese gaming companies overseas, so we can take reference from their experience and replicate it to our own games. So in 2021, we will see bigger growth for our overseas business.

Next page. In 2021, in terms of gaming IP and categories, we will continue to cultivate and spend more in R&D, so that our gaming business will be healthier and will grow more effectively. If you look at various IPs, for example, our Eudemons as well as Conquer Online, they will be launched to the market effectively and they would bring about continuous growth in revenue in 2021 and in fact, such growth is already seen in second half 2020 and also in January and February of this year. For Heroes Evolved, actually we had overcome difficulties in the past year and restored growth already. So in terms of new games and new IP, I'm sure they would bring revenue growth. And with our continuous effort, we believe that in 2021, we will see better result. Thank you.

Ben Yam:

Hello, good morning or good evening. This is Ben and I'm going to present to you our financials for the full year. So first of all, as Simon mentioned in the very beginning, 2020 has been a year of challenges and opportunities. And I think if you translate that message into the financials, while we believe the opportunities will enable us to grow in a much faster pace in the coming years. I would say that the challenges do have some impact on the revenue growth in 2020.

And as you can see here, if you can turn to the next slide, you can see on this slide, our revenue growth of gaming was 4% and education was 2%, for the year. And for the investors who have been following us for quite some years, this growth rate is lower than our typical rate. But I would like to point out that this is actually something that Vin and Lin Chen also mentioned is that our second half revenue for 2020 sequentially increased at a much higher rate. In fact, if you look at our education business, the overall revenue in the second half increased by 14.7%, compared to the first half and our gaming revenue in the second half also increased by over 8% half-over-half. So overall that's a momentum that we are pleased to see, and we do expect that momentum will continue to carry forward into the new year.

And then if you look at the cost side of the equation here on this slide, we've also continued to manage with discipline and operational excellence. And we've seen a gross margin percentage increase in Promethean as a result of robust cost management. And that translates to a higher rate of growth of gross profit growth here at 8.2% as you can see here, which is higher than our revenue growth rate. And on top of that, we have been managing our costs very effectively on the OPEX level as well as you can see the sales and marketing expense, and also the general administrative expense on this chart decreased as a percentage of revenue in 2020, and then in terms of the bottom line, the net profits increased by 18% over 2019. And then if you look at EBITDA and also non-GAAP operating profits, these also saw significant year-over-year increase. And then, cash flow continues to be strong. Our operating cash flow increased by 13% to 1.3 billion. Simon also mentioned this in the beginning, and then, we also maintain a very strong financial position, as our net cash amounted to close to 4 billion at the end of the year.

Next slide, please. So now I want to go the segmental financial highlights. Again, the highlights of the year for both businesses would be the sustained revenue growth despite the challenges and with effective cost planning and management, which enabled us to keep costs under control both on the COGS side and also on the OPEX side. And then specifically for the education segment I also wanted to highlight that as you can notice here, our core segmental loss for education increased by over 10% during the year. And a big part of that is actually due to the increased server hosting costs, that's actually related to substantially higher users for our Edmodo platform, which in turn is because of the COVID-19, and also especially in Egypt, where we have started to implement a countrywide rollout, as we have talked about before, we have seen significant increase in the MAU and DAU in various countries and especially in Egypt. So the way we look at it in terms of the segmental loss increase is that there was a bit of mismatching, right between the timing of costs and also the revenue, especially for Egypt, because while we saw a hosting costs increase last year because of higher user traffic, we actually expected to see our Edmodo revenue to come in this year, and Simon will talk more about this in the country rollout part of our presentation.

And then the other thing to note here on the core segmental loss, as you can see on the bottom left box of this slide is that our second half core segmental loss narrowed significantly to slightly above 200 million RMB compared to 377 million in the first half. And that's attributed to our continuous cost management efforts and also higher revenue, high gross profit in the second half. And as I look forward to the new year in 2021, we do expect this narrowing of core segmental loss to continue in 2021. So I think the second half, the core segmental loss as you can see here, 208 million, would be a good benchmark to forecast into the 2021. And I think that'll be the end of my part of the presentation and I will pass it back to Simon who's going to take us through the country rollout as well as the outlook.

Simon Leung:

Okay, thank you, Ben. Before I do that, I really do want to make a couple of comments on the cost side of the equation of the education business. In addition to managing the costs and everything, we also managed to cover the tariff issue because if you remember, there was a tariff imposed on all the products going into the US, so Vin and his team is actually has done a marvelous job in managing that and then continue to drive up the margin so which is such a good thing. The other point I want to make on the education businesses actually is in terms of the market share. While we continue to go after number one in the market, but we won't do it at any costs, which is actually something that Vin and his team are very good in doing is actually, while we increasing our market share, we don't allow our margin to get impacted. So that's why we see year-to-year growth in terms of margin.

And if you really take the business and separate it into two that is the developing market and the developed market is that our margin is actually very healthy while we're going after that the market share, for example, in Egypt or in Italy. So it's actually a congratulation to Vin and his team and doing a great job on that one. So, with that, I want to go into a country rollout very quickly. I'm very conscious of the time. It's actually talking about the vision, the blended learning vision for the entire country or the entire district. So basically in Egypt, we're working with them on many different projects to really help them to revamp the entire education system. I really got to talk to Dr. Tarek Shawki, who is the Minister of Education in Egypt. We took advantage of COVID. I mean, may not be a good, it doesn't sound good, but what we did is actually revamping the entire education system using basically all our platforms, both hardware and software. So here we just give you a snapshot of that in the middle of implementing it. And we're also looking at what we can help them in terms of learning after school. So that's why you see our online tutoring platform on the bottom left.

The other thing, which is quite important, we also work with partners to address the issue. You see Zoom being there. And also we're working with Microsoft Teams, by the way. I mean it's actually Office 365 so we are, we have a lot of, wonderful partners that we work with. The next page is

actually just a repeat, we have our vision, we can support a school, a district or a country. So it's actually we are quite flexible in terms of how we can support them. This is just a pictorial, kind of way to tell you, based on what we do, we can build up a very interesting SAAS and subscription and licensing model going forward. And also we work with partners to bring in a revenue opportunity for us based on the community we built. And if you look at the countries that we work with, the likes of Egypt, Thailand, Ghana, which is in Africa, and Russia, and also districts in the US, Miami, by the way, Miami is actually one of the largest, if not the largest school district in the US which we have a lot of our presence in. And so this is just talk about growth, because once you start working on countries, you start building it up. So this is actually where the SAAS revenue recurring revenue concept will be very powerful. This is different stages of what we do so we'll give you a view of we're not just working on one country.

Okay, let me go to outlook very quickly. And then we'll go into Q&A. We are very confident in 2021, both in the gaming business and also in the education business. We see a lot of funding going into education, because of blended learning, so that's why we see the market momentum is actually with us. We also see a lot of synergy between our businesses. So we have taken a look at how we can leverage our different businesses and maybe even integrating the businesses to get better synergy out of it, both from a go-to market standpoint and also from our cost standpoint, and our country strategy is actually one great example that all our companies are working together. So the last but not least is actually we'll continue with fiscal management. In this one we'll continue to focus on generating cash. Of course, the P&L is one thing, but I do want to say and tear it up. I did talk about integration. I did talk about synergy. We're going to take a look at our cost structure of our education business very closely, actually we have started that late last year. You will see some results. I'm not in a position to take you guys to it, but I think the results will be quite encouraging for our investors. With that I want to make one final comment, is actually when I look at our stock and look at our P&L, when I look at our balance sheet, I think we are very undervalued at this point. With \$700 million of net cash, with a market cap of 1.4 billion US dollars. So all good news for investors. With that, I'm going to stop and we're going to open it up for Q&A. Thank you for your patience.

Moderator:

Thank you very much Dr. Leung and the management.

Now it's time for our Q&A section. You're welcome to raise questions in the following two ways. First, if you would like to raise questions through this conferencing system, you may press star one on your keypad and our operator will bring you through. Second, if you would like to raise questions via our webcast platform, please click the question mark on the left-hand side of your screen and type in the question in the Q&A box. We also welcome questions in both English and Chinese. Let's welcome our first question.

Simon Leung:

No question?

Moderator:

The first question is this. It is about gaming. Right now, you have three flagship IPs, so at present, for these three IPs, in 2020, what is its user number, DAU, MAU, ARPU and gross billing?

Simon Leung:

I will refer to Lin Chen to take this question.

Lin Chen:

Okay. I think we can go back to our data because just now in the ppt, we already shared our core gaming data. Actually yes, in this slide, you can see that our MAU and number of registered users

are both on the rise including our revenue and gross billing, you can see that overall speaking, Eudemons' business line is mainly self-published, especially the PC game and its revenue share ratio is relatively higher. For Conquer Online, its margin is similar to that of Eudemons. We have Heroes Evolved, in overseas, we have taken over publishing from our agencies, so we have more confidence in Heroes Evolved in the overseas market. Its overseas gross billing will account for a bigger share of the total gross billing and also a bigger share of revenue. So the operating data such as our core MAU in 2020 showed good condition. Thank you.

Moderator:

Thank you. Now let's invite a question from the phone conferencing system. Thank you. The question is from Haitong. Please.

Feiya Zhao, Haitong:

Greetings. Thank you for taking my question. Congratulations on your good results. I have two questions. One is about gaming. Just now we heard that you have an Unreal Eudemons game in the pipeline and it will be built with UE4. So what is its target user group and comparing with the past Eudemons, what is the difference in terms of playing method? And what is the R&D cycle? How big a team did you use to create this game?

Another question is about education. Now looking at your education business loss ratio, in the second half of the year, it narrowed down quite well. On the year-on-year basis, it is flat. On the half and half basis, it narrowed down quite well, so is this because of a seasonal factor or is it because you have changed your strategy in marketing? If you look at 2021, for the education segment, what would be the trend of loss ratio? Thank you.

Simon Leung:

Lin Chen, please take the question about gaming first, okay?

Lin Chen:

Yes, first concerning the Unreal Eudemons game, if you look at target users, we hope that at least half of them will be our IP users, for the other half, we hope to target at the young market and young users. For the Unreal engine, it is the first time we are using it. Indeed to be honest, we are not using it for the first time. In the past, for Tiger Knight, we used UE3 engine. So in terms of the investment into this engine, our R&D team is already as big as 100 people and will continue to make more investment. So we hope that for this UE Unreal Eudemons, it can be launched to the market within one to two years of R&D cycle. For playing method, we're talking about an open world because for Eudemons, there are imaginary beasts and also the raising of beasts, big world and so on. These are some classic elements and we will incorporate other things - for example, the open world that is well-liked by young people, hoping to get the favor of young people. That's our plan. Thank you.

Simon Leung:

I will take the question about direction of education and if there are some figures, Ben can also supplement. Regarding education, regarding Promethean, usually customers purchase in Q2 and Q3. In the first half of last year, because of the pandemic, a lot of things slowed down, so the cycle or the season was deferred. Concerning loss, that's the reason why last year was different from the year before. Besides, just now in my conclusion, I already said, first of all, in relation to our education business, we have a very clear direction of blended learning. Our country rollout is also very clear. So first of all, regarding synergy, no matter whether we are talking about products because if you look at our products, there will be a lot of synergy between Edmodo and Promethean,

so we will see how we can use products synergy to help ourselves to, firstly, drive for more contracts and, secondly, we will see whether there will be new synergy in terms of cost. Besides, overall speaking, we have actually reviewed the situation, we have such a clear direction. So for some projects, we will consider whether we want to continue. So on these two fronts, in 2021, we have a lot of confidence in the revenue of education. Besides, concerning our bottom line, there will be a big progress. Ben, anything to add?

Ben Yam:

Yes, let me supplement. I think that in 2021, concerning the outlook of education business, if you look at the pipeline, which Simon has commented a lot, there would be continuous growth, and that's the core business of Promethean. Besides, our country rollout, from the cost point of view, just now in our presentation, I already said that in the second half 2020, regarding costs of education or core segmental loss, it's slightly above 200 million. It's 200 odd million RMB. So there's already a significant decrease compared to the first half. It was over 370 million in the first half, it decreased to 200 odd million in the second half. So in 2021, this trend will continue. We believe that the loss will continue to come down. And just now Simon said that apart from our top line growth, driving reduction of loss, in terms of cost, there are also moves about integration, for example, in overseas markets, there will be more integration between Promethean and Edmodo and cost reduction will become more efficient. In China, we will also do assessment of our projects. So we will do a lot more work about cost management within this year, thank you.

Moderator:

Our next question is for Promethean. Investor would like to know more about the volume and the ASP and the future trend of the Promethean products.

Simon Leung:

Vin, I think it's the one for you.

Vin Riera:

Yeah, absolutely. So let's break it into two different areas. From a volume standpoint, we did approximately 130,000 units this year in volume. One of the things that's interesting and a trend that we've seen is when customers are using our products for blended learning, they're buying our more premier product, which is our titanium product. And what we saw is a higher mix shift of titanium product this year, and then our lower end products, which is very, very encouraging. We've even seen in the market where customers have recently bought lower end panels from competitors that had to replace some of those panels with our panels as a result of that. So I guess that addresses both of your questions.

Simon Leung:

That's kind of also reflect to what I was trying to say earlier in the meeting is actually what we want to do is that it is not only a balance, it's that the ASP and the market share and also the margin, because we didn't want to go into the price war. That also goes to one of the charts that Vin has shown - our brand equity and the value and everything. So we will grow our volume, but not at the expense of our ASP nor at the expense of our gross margin.

Moderator:

The next question is about gaming. The question is regarding Under Oath. What is its overseas publishing strategy and promotion strategy? And comparing with competitors like Genshin Impact, how is the comparison? Thank you.

Simon Leung:

Lin Chen.

Lin Chen:

Ok. First, regarding the testing plan of Under Oath, first of all, we will do test in China, and then in the second stage, overseas test. For game testing where there are two areas. First, the core playing method of the game and second, CG performance of the game. And on this point, Bilibili will share with us a lot of experience because the publishing side is Bilibili. And we will listen to Bilibili in terms of its publishing experience to plan our overseas test. And based on our discussion with Bilibili, first of all, our Japanese battle RPG method can be first tested in China. And based on test data and feedback in China, we can enhance our overseas version. In this way, we believe we can get bigger success and if you consider Azur Lane and also other ACGN products like Arknights, I think we should be benchmarked to Arknights and Azur Lane, these type of ACGN games, as opposed to Genshin Impact because it is more of an MMO or ARPG category. So on this point, I believe Bilibili will give us a lot of help. Thank you.

Moderator:

Thank you, Mr Lin. Next question is about the network. The question is about blended learning solution and the progress in Egypt. When will you begin to see orders from Egypt and how will be the revenue scale? Besides, what is the implementation or rollout progress in other countries? Thank you.

Simon Leung:

Well, back to the previous slide, perhaps I explained too fast just now. First of all, you will know how much they'll be for this year. Actually, there is the issue of confidentiality regarding our contracts. But this year there will certainly be quite good revenue. Besides, on the slide you can see our progress in some countries. Of course in some cases, the scale is big, in other cases, smaller and they are different. And we are not only in these four countries. The products in different countries will be slightly different so the scale in each country is different. When there is opportunity, we will share with you the progress of each of our projects.

Moderator:

Thank you, Dr. Leung. The next question is from the phone conferencing system. Operator, please. Thank you.

Operator:

The next question is from Macquarie, Frank, please.

Frank Chen, Macquarie:

Thank you, management, for taking my question. I have two questions about education. First, regarding education, concerning the country project, what is your strategy to acquire new orders and what is the process of acquiring new orders? And we understand that you may leverage Promethean sales network to have an initial understanding of the intention of various countries. However, Promethean may focus more on developed countries. And for your country projects, the direction is mainly the developing markets. So how big will be the synergy between the two groups? The second question is about profit margin of education. In 2020, the rise in profit margin is mainly because of Promethean's margin improvement. In the future, where will be the room of margin growth for education? Will you still rely on Promethean's margin improvement or other areas? And finally, what are some factors that will drive your future break-even in education or a bigger profit? So these are my two questions. Thank you.

Simon Leung:

Let me take your first question first. Now if you look at page 48, when we enter each country, our entry point is different. So this is why our company is different from other companies because we are more flexible. We have hardware, software, tools and many partners. To give an example, in Egypt when we first went in, it is Promethean and later we brought in Edmodo. And then we have

also brought in our VOD, 101 PPT and so on. So this is an example. And then for Thailand, we used another product what we call English Galaxy. And it is an English product developed in Hong Kong and then we went in. They are very interested in this product and we used that product to also bring Edmodo and Promethean in. And for instance, Vermont, only Edmodo went in. And it is there to support their blended learning as a software platform. And then in Miami, both Promethean and Edmodo went in. When we went in, they are two separate companies because at that time we had not acquired the two companies. Later on, we acquired them and we can integrate them together and give them better support. So to answer your question, we are very flexible.

Regarding revenue, eventually, we hope to use the very good platform of Promethean, so that we can have a platform with both hardware and software. We can make use of Edmodo to build a SaaS or subscription model. So to answer your second question, in the coming few years, our good point is Promethean would definitely enjoy good growth and it will make big contribution. And why did I say that there will be synergy? Edmodo and Promethean will be integrated together and then when we enter a country, we can start to build our SaaS and recurring revenue. And Egypt is a better example to illustrate because Promethean had entered and then we placed the 22 million students on our Edmodo platform. So this year in Egypt, there will be revenue from Edmodo so we are using different products including Promethean and other software products to enter a country to build up recurring revenue. And then break-even and making profits have two different directions. One direction is revenue growth and of course, Promethean will be an important part and SaaS revenue is also very important. And if we achieve integration, we can accelerate break-even. So in terms of cost, this year we will look at cost very seriously. As I said just now, our direction is very clear and that is blended learning. So we will do a lot of work regarding integration. I believe that we will enjoy cost synergy. Besides, we will also consider whether there is the need to continue our other projects. If it is not necessary, we will make a decision. So on these two fronts, we will do something with cost.

Ben Yam:

Let me supplement, Frank, you just mentioned that Promethean may be stronger in developed markets, but there have not been too many actions in emerging markets. Actually the chart that you looked at just now shows our top 10 markets. You can see the by-revenue contribution and then it is contribution in terms of revenue. If you look at the emerging markets, Promethean is very strong in many emerging markets. We are strong in that channel and even though its revenue contribution is not as high as in developed market. However, in these markets we are still very strong. Egypt is a good example because in the past, in Egypt, the revenue was not as high. And now it's suddenly emerged. So I hope to answer your previous question.

Simon Leung:

I want to make a point. So when it comes to developing countries, actually the volume is still quite big and ASP (is lower). So if you only look at revenue, it seems that we're focused only on developed countries. And if you look at the US and Germany, because they buy our most high-end products, so the volume may not be that high but revenue is very high. So if you are interested, we can talk to you in greater detail.

Ben Yam:

Actually in many emerging developing countries, our market share is number one. In Egypt, it's 90 odd percent, 96 or 97%. Thank you.

Moderator:

Thank you, Frank. Thank you for the answers. Next, this question is from the website. It is about gaming. So regarding Eudemons, in 2020, growth in DAU and MAU was quite good. In 2021, will you be able to maintain the same growth? Next question, in 2021, what is the plan of launching some expansion packs for Eudemons?

Simon Leung:

Lin Chen.

Lin Chen:

As I said, in 2020, in terms of user base, Eudemons has achieved good results mainly because number one, we have launched excellent content. And just now the question is about content and expansion packs. We enhanced the frequency and quality. And it is the reason that MAU and DAU have grown. In 2021 there are two things. First, we'll continue to strengthen the parts that are proven or verified, that's the expansion packs as mentioned. We'll continue to maintain the same speed and quality this year. I think quality is particularly important. In 2020, in terms of growth in core users, well, we did a good job. In 2021, we hope that in terms of content marketing and reaching new types of users, we can do a better job. So we hope that in 2021 we will be able to maintain the same growth. Of course, growth in these metrics, it's definitely not easy so apart from the part we achieved last year, in 2021, there are two new Eudemons products to be launched. In terms of content marketing, there will be hopefully more breakthrough and innovation and we can achieve the same growth. Thank you.

Moderator:

Thank you, Mr. Lin Chen.

Next question is also about gaming.

Simon Leung:

So also for Mr. Lin Chen.

Moderator:

In the future, for your publishing strategy of games, and also in the future, do you have more IP licensing and collaboration plans please? Thank you.

Lin Chen:

In terms of publishing strategy, in the future, we will continue to maintain two models that is self-publishing and agency publishing. The main difference is maximization of benefits for the gaming business. If you look at ACGN categories, well, there are some leading companies with rich experience in this area. So we will continue to cooperate with Bilibili as well as Season Entertainment. And we will also invest more in self-publishing. As I said, for Heroes Evolved, we have taken over overseas publishing. In terms of self-publishing, we will invest more. We see a lot of opportunities. If you look at financial statements, our investment in publishing accounted for only a small share. And this year we want to do more in this area in order to expand the scale of our gross billing and revenue. And this is why we are confident in this year's revenue growth. Thank you.

Moderator:

Thank you. Mr. Lin. Our next question is also from our webcast platform, it will be on Promethean. Analyst would like to know what is the new product pipeline for Promethean in the next year. And also, is there any order on hand we can disclose?

Thank you.

Simon Leung:

Vin, it's over to you.

Vin Riera:

Yeah. Great question. We do have new products on the rise and we will release new products in 2022. What I should mention though is our existing product because it's a connected device and we have the ability to do over-the-air updates, we've done over 20 enhancements this past year to continually upgrade and improve the product and keep it very relevant in the market. The technology is at the point now, where, when we launch a product, we can leave it in the market for a little bit longer because we can continue to enhance it before we launch a net new product. But you will see a new product in the market from Promethean in 2022.

Simon Leung:

Actually I couldn't resist, Vin did give me a sneak preview of our new product. And I'm very excited about the one coming up, it's actually very different and you'll be excited. So, the other thing I would like to say for a minute, we could be kind of in a sense of giving guidance a little bit, but Vin is a very busy guy in Q1, so I'll leave it at that, when it comes to questions about orders, we can't go into detail, but he has not been sleeping for the last two months, so...

Moderator:

Now we will take the next question. The last question is from the phone conferencing system please.

Operator:

Thank you. The next question is from Connie, please.

Connie, BOCOM

Greetings, I'm Connie. My question is Mr. Lin, can you share with us about the gaming industry? Now in the market, competition is keener. So concerning future development trend, do you have any forecast? And regarding game projects that you are developing right now in the pipeline, will there be some change in terms of categories? Thank you.

Simon Leung:

Lin Chen.

Lin Chen:

Okay, let me take this question. Actually, concerning development of the gaming industry, I think you can see some clear trends. First, various companies are working around their own IP and categories that they are good at and they keep on cultivating. So Tencent and NetEase these are leading companies. And if you look at CP, for example Wan Mei, Youzu and G-bits, you can see that these companies focus on their own IP and categories. And in the process, based on experience that they have accumulated, they will then try to achieve breakthrough innovation and integration. And like Genshin Impact, it is based on Honkai Impact I, II, III and then there is continuous accumulation. As a result, a very popular game is introduced. For the future gaming market, I think the most important thing for any gaming company is its R&D expense. So last year, we kept on increasing our R&D expenses, that's one reason. This year and last year actually the channel profit-sharing is already better. And so in the coming period, for the gaming business, our product and R&D will be the biggest core competitiveness. And we have seen a trend.

If you look at our company's pipeline and product line, first of all, for our existing IPs and also products with stable income, we'll continue to invest, especially our Eudemons IP. So if you look at our overall gaming revenue, a growth from 3 billion to 5 billion or even 10 billion. One of the main drivers is IP, so at least half of our investment will be into existing IPs and products. This can ensure that we will have stable revenue growth for our games. At the same time, in the process, based on our IP accumulation, we will identify new opportunities and new popular game possibilities. And there may be two directions. First, content. In terms of gaming, users or players actually consume content, so high-quality content will be one direction for a game to become popular. Another direction is innovation and integration. In the industry, we can see some big categories, for example

MOBA. Why did it succeed? First, it is very entertaining and has low barrier to onboarding of users. So if you look at MMO that we are good at and also new CG enhancements and integration and innovation between MMO and other genres, well, it is based on the competitive attribute of MOBA. And if we derive a new genre from MOBA, we think there will be huge opportunities. So on one hand, we will continue to stabilize our healthy development. At the same time, in the process, we need to make attempt into other possible games that may become popular. Thank you.

Simon Leung:

Let me supplement regarding gaming. Another growth driver is overseas business. So just now Mr. Lin Chen also said that we have two new games. And basically they are for the overseas market so it is our main growth driver as well.

Moderator:

Thank you very much. Thank you Dr. Leung. Thank you Ben. Thank you Lin Chen. Thank you Vin. This is the best way to conclude...

Simon Leung:

Can I make a closing comment? First of all, thank you so much for joining the conference. So just to kind of repeat that, we are very confident about 2021, both the gaming business and also the education business. You know our gaming business quite well, that's why a lot of questions around that. On the education side, we truly believe and we are very confident that we can make progress both from our top line and the bottom line perspective. So with that I think we are very good company to invest into if you look at our balance sheet, let me repeat myself on this one. So looking forward to talking to you guys soon in the near future. Thank you.

Moderator:

Thank you Dr. Leung. Thank you Ben. Thank you Lin Chen. Thank you 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 all have a great day.