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DL - China Distance Education Holdings Ltd at Deutsche Bank Virtual Investor Conference

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## CORPORATE PARTICIPANTS

**Mark A. Marostica** *China Distance Education Holdings Limited - Co-CFO*

## PRESENTATION

### Unidentified Analyst

Hello, and welcome to the Deutsche Bank Depository Receipts Virtual Investor Conference, dbVIC. I am pleased to announce that our next presentation will be from China Distance Education from China.

(Operator Instructions) On a final note, all of today's presentations will be recorded and can be accessed via the Deutsche Bank website, [adr.db.com](http://adr.db.com).

At these -- this point, I'm very pleased to welcome Mark Marostica, Co-CFO with China Distance Education. Over to you, Mark.

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### **Mark A. Marostica** - *China Distance Education Holdings Limited - Co-CFO*

Hello. My name is Mark Marostica, Co-CFO of China Distance Education. I'm delighted to participate in Deutsche Bank's Virtual Investor Conference today.

Before we get started, please take close attention to the safe harbor statement on Slide 2 of this presentation.

Let's start off with an overview of China Distance Education on Slide 4. We are China's largest professional online education company in terms of number of paid enrollments, with fiscal 2017 revenue of \$131 million. Founded in 2000, China Distance Education has become a trusted online education brand in China with an extensive content library of audio/video course content. We're also an internet company. Our websites are among the most visited websites in China's education industry with nearly 53 million cumulative registered users as of September 30, 2017. And we have the #1 market position in our key industry verticals of Accounting, Healthcare and Engineering & Construction. Our success is rooted in our results-driven, high-quality courses and services, [passing] our students improve their passing rates on important professional certification exams and become more competitive in the job market.

Next slide, please. Aside from the 3 core industry verticals, we have a wide range of online courses across 16 industry-specific websites and related mobile apps, covering 13 industry verticals altogether. The breadth of our courses enables us to address the educational needs of our customers throughout their professional lives and even as they change careers or take on different roles in their careers.

Next slide. Our vision is to establish a lifelong and comprehensive online learning ecosystem for our students who are typically working adults aged 22 to 45. We're China's go-to-provider to help our students pass high-stakes exams to become professionals and satisfy continuing education requirements to maintain good standing. We provide professionals practical accounting training courses, which we bundle with our employment guidance services. We also serve China's college market with college-focused business start-up training and learning simulation software. And we provide value added tax advisory on accounting outsourcing services to small- and medium-sized enterprises. All in all, we've created a comprehensive ecosystem with powerful network effects serving working professionals, college students and small- and medium-sized enterprises.

Now let's review our investment highlights beginning with Slide 8. We retain the top lecturers to record our courses. Our lecturers are typically academic from leading higher education institutions in China or experienced professionals within their respective field. Courses recorded by our lecturers are put through strict quality control processes to ensure the best quality possible. Our in-house content development team works hand-in-hand with our lecturers to create our courses drawing on their experience, market intelligence and exam authorities published guidance. And importantly, we own the IP.

As you can see on Slide 9, we provide a comprehensive service package to our students. Our pool of close to 400 tutors will answer student's questions within 24 hours in writing. Plus, our customer service center is accessible by phone 24 hours a day, 7 days a week for any nonacademic

questions from our students. Each student has a personalized study account with us, where they can manage their study planning and monitor their progress. Students can also interact with their peers through an online community.

Our business is a self-reinforcing teaching learning cycle. By providing high-quality courses and services, our students can achieve superior results. And students' learning data and feedback allow us to further improve our content and services. As a result, our students achieve exam passing rates better than the nationwide average. For example, the nationwide average passing rate for China's Certified Public Accountant or CPA exams is in the 15% to 20% range, while our passing rates are 40% to 50%.

Next slide, please. Our proprietary online platform enables a large number of students simultaneously to watch lectures and perform other learning tasks and allows them to download lectures and exercises to their local devices, if they choose. Our courseware is film grade, high-definition streaming video with teachers delivering their lectures using an interactive digital blackboard to provide students a virtual classroom environment. Today, almost all of our courses are accessible on mobile devices, so students can access our courses anytime, anywhere. And for our more popular courses, we offer live streaming.

As you can see on Slide 11, our model is highly scalable. Since most of our courses are prerecorded, there are almost no limits to the number of students who can enroll in each course. We can also easily add new courses to our online learning platform as we use only one platform for all our courses and services across the different industry verticals. The highly flexible nature of our business model and platform allows us to scale our business efficiently and add or update courses with relatively low incremental cost.

Next slide. Our business model has multiple revenue streams, which not only provides us with multiple avenues for growth but lessens our dependency on any one industry vertical. When China Distance Education started operation, almost 100% of our revenue is driven by Accounting. Over the years, we successfully expanded into other key verticals, namely Healthcare and Engineering & Construction, and more recently, Legal Education. In fiscal 2017, our Accounting percentage revenue mix was approximately 42%, while Healthcare was 20%, and Engineering & Construction was 6%.

China's professional education market is large and growing. According to Goldman Sachs' estimates, China's professional education market is \$19 billion in size, growing in the mid-teens.

Looking at our market position in China's professional test preparation market, in particular on Slide 13, there are 2 key takeaways I'd like to point out. First, our online market share is very high, and you can see that on the left-hand side of the slide. In Accounting, for example, we have approximately 75% share of China's online Accounting education market. Second, our overall market share is still rather modest when you take into account all learning modalities, including online, ground-based and books and reference materials. Again, looking at Accounting, our overall market share in China's Accounting test prep market is only about 15%, leaving ample room for growth. We believe we're in a unique position to drive our overall market share higher in our core industry verticals.

First, we have willing student audience that's grown up with the web and is eager to do everything over the internet, including learning. Second, our online learning platform offers convenience with anytime, anyplace learning and no need to fight traffic to get to class, and that can be difficult in some of China's larger cities, of course. Third, our courses are affordable. Exam prep ASPs in our June quarter fiscal 2018, we're around RMB 700 or USD 100 on average, well below the cost of typical classroom learning which can be hundreds of renminbi higher. And fourth, with improvements we've made in the learning experience for online learning, such as mobile and live streaming, our learning platform continues to become more engaging for students.

Now let's take a look at our growth strategies on Slide 15. The lowest-hanging fruit from a growth strategy perspective is to add enrollments to our existing courses. This is where we enjoy the highest incremental margin. We also focus on expanding our course offerings in our existing industry verticals, such as adding longer duration VIP courses with more value-added services to students. We continue to harvest our comprehensive Accounting ecosystem, where we offer not only exam prep services but continuing ed, practical training, employment guidance services and tax advisory and accounting services, a one-stop shop in Accounting. We continue to innovate across our online learning platform to help enrich students' learning experience with technology, such as mobile and live streaming, and we've introduced the structure-led training courses or our more popular courses. By offering students a variety of learning modalities, we can appeal to different learning styles and preferences across our

student audience. In addition to organic growth, we look for select complementary acquisitions and strategic investment opportunities to enhance our offerings to students, such as our 51% acquisition of Beijing Ruida, a leading provider of exam prep services for China's national judicial examination, a.k.a. China's bar exam.

Beijing Ruida further diversifies our business model and squarely positions us in a fourth important industry vertical, that being legal. As we previously disclosed, Beijing Ruida recorded 2017 revenue of over RMB 200 million and 2017 net income of approximately RMB 50 million under PRC GAAP.

Moving to our financials on Slide 17. Before I discuss our historical financial performance, I want to point out that our fiscal year-end is September, so we've recently concluded our fiscal year 2018. Having said that, my comments today regarding our financial performance are applicable to our June quarter fiscal 2018 and prior.

Looking at our revenue growth, you can see that we recorded approximately 34% year-over-year revenue growth in the June quarter fiscal 2018, which is an acceleration in growth from prior periods. The acceleration in revenue growth is primarily due to strength in our Accounting vertical, which has produced strong revenue growth since the beginning of fiscal year 2018 through the June quarter.

Our June quarter operating income was down year-over-year, mainly due to the increase in fair value of contingent consideration with respect to our 40% equity interest in Beijing Ruida in 2017. As we previously disclosed, excluding this change in fair value impact, our adjusted operating income and adjusted net income in the June quarter fiscal 2018 was up approximately 28% and 192% year-over-year, respectively.

On Slide 18, you can see our business is seasonal, primarily due to the timing of exams. Most of the exams we offer courses for are held once a year, and the exam dates are primarily in the second half of our fiscal year in the September or October time frame. So we typically record our highest quarterly revenue and earnings in our June and September quarters.

We generated healthy free cash flow historically, as shown on Slide 19, in part due to our relatively low CapEx model and cash collection from our students in advance in most cases. This has enabled us to return value to our shareholders in the form of a special cash dividend.

Next slide, please. As of June 30, 2018, we had \$91.5 million of cash and cash equivalents, term deposits and restricted cash. The majority of our bank borrowings and restricted cash as of June 30, 2018 is related to dividend bridge loans.

Next slide. To sum up, we're China's largest online professional education company with leading brands and nationwide recognition and a lifelong and compressive online learning ecosystem. We deliver high-quality course content and partner with top lecturers from leading Chinese universities. We have multiple revenue streams, which help drive growth and diversify risk. Our growth strategy is multipronged, relying primarily on organic growth. And China's professional education market is large and growing with substantial addressable markets across China.

Thank you for your interest in China Distance Education, and please feel free to reach out to us to learn more about our company.

That's the end of our presentation today. Thank you.



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