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Earnings Call

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PRESENTATION

Operator

Good evening, and thank you for standing by for the New Oriental's FY 2020 Second Quarter and Interim Results Earnings Conference Call. (Operator Instructions) Today's conference is being recorded. If you have any objections, you may disconnect at this time.

I would now like to turn the meeting over to your host for today's conference, Ms. Sisi Zhao.

Sisi Zhao - *New Oriental Education & Technology Group Inc. - IR Director*

Thank you. Hello, everyone, and welcome to New Oriental's Second Fiscal Quarter 2020 Earnings Conference Call. Our financial results for the period were released earlier today and are available on the company's website as well as on Newswire Services. Today, you will hear from Stephen Yang, Chief Financial Officer. After his prepared remarks, Stephen will be available to answer your questions.

Before we continue, please note that the discussion today will contain forward-looking statements made under the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. Forward-looking statements involve inherent risks and uncertainties. As such, our results may be materially different from the views expressed today. A number of potential risks and uncertainties are outlined in our public filings with the SEC. New Oriental does not undertake any obligation to update any forward-looking statements except as required under applicable law.

As a reminder, this conference is being recorded. In addition, a webcast of this conference call will be available on New Oriental's Investor Relations website at investor.neworiental.org.

I will now turn the call over to Mr. Yang. Stephen, please go ahead.

Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

Thank you, Sisi. Hello, everyone, and thank you for joining us on the call. We are very pleased to report a set of solid financial results in the second fiscal quarter of this year, delivering both accelerated top line growth and continued operating margin expansion. Total net revenue growth was \$785.2 million, representing a growth of 31.5% or 34.8% if measured in RMB, exceeding the high end of our expected range. Net revenues from educational programs and services for the second quarter were \$723.3 million, representing a 33.0% increase year-over-year. The growth was mainly driven by increase in student enrollments in K-12 after-school tutoring courses, which continued its strong momentum and achieved a year-over-year revenue growth of approximately 46% in dollar terms or 49% if computed in RMB.

We continued to be guided by our Optimize the Market strategy in this quarter and carried out our capacity expansion in cities where we see potential for rapid growth and strong profitability. During this quarter, we added a net of 41 learning centers in existing cities, opened a new training school in the city of Huizhou and a dual-teacher model school in the city of Chengde. By the end of this quarter, the total square meters of classroom area increased by approximately 25% year-over-year and 6% quarter-over-quarter.

Total student enrollments in academic subjects tutoring and test prep courses in the second fiscal quarter of 2020 increased by 63.3% year-over-year to approximately 3,789,200. Please note that this higher-than-normal increase in the student enrollments is primarily due to the division of the autumn semester into 2 parts, meaning that the student enrollments are recorded separately and fall into separate quarters. At the same time, we continued our efforts in upgrading our online-merge-offline standardized classroom teaching system, while the Interactive courseware in the POP Kids program was rolled out to more cities. We are very encouraged to have received positive feedback from our customers and see sustained improvement in customer retention rate. We also continued to make strategic investments into our dual-teacher model classes as well as new initiatives in K-12 tutoring on our pure online education platform, koolearn.com, to leverage our advanced teaching resources in low-tier cities and those in remote areas.

Following last quarter's strong bottom line performance, we once again achieved year-over-year operating margin expansion in this quarter. During this quarter, we recorded non-GAAP operating income of \$36.5 million compared to a loss of \$14.9 million in the same period of last year. Non-GAAP operating margin rose by 720 basis points to 4.7% from negative 2.5% a year ago. The continued margin expansion is mainly driven by better leverage in classroom rental and related operating expenses, just as we consistently improve the utilization of facilities. In addition, supported by a standardized, modularized and systemized operating process, we achieved an outstanding improvement in operational efficiency within each key business unit. We're confident that we will be able to deliver continued margin expansion and generate sustainable long-term value to our customers and shareholders.

Per program blended ASP, which is cash revenue divided by total student enrollments, decreased by about 10% year-over-year. We'd like to note that the lower-than-normal blended ASP is primarily due to the change in the tuition fee collection schedule for our K-12 after-school tutoring courses, as explained above. The number of students we recruited and amount of fee collected during the quarter reflect the second half of the autumn semester, winter semester and the first half of the spring semester. Therefore, our blended ASP for the second quarter of 2020 appears to be lower.

Hourly blended ASP, which is GAAP revenue divided by total teaching hours, increased by approximately 6% year-over-year in RMB terms. To provide a breakdown of the hourly blended ASP, please note that U-Can program increased by 7%, and POP Kids increased by 11% and overseas test prep program increased by 7%, all year-over-year in RMB terms.

Now let's move on to the second quarter performance across our individual business lines. As mentioned earlier, our key revenue driver, K-12 all-subjects after-school tutoring business, achieved year-over-year revenue growth of 46% in dollar terms or 49% in RMB terms. Breaking down, the U-Can middle school and high school all-subjects after-school tutoring business recorded a revenue increase of 43% in dollar terms or 46% in RMB terms for the quarter. Our student enrollments grew approximately 55% year-over-year for the quarter.



Our POP Kids program delivered outstanding results with revenue up by about 51% in dollar terms or 55% in RMB terms for the quarter. Enrollment in the program went up about 87% for the quarter.

The overseas test prep recorded a revenue increase of 3% in dollar terms or 5% in RMB terms for the quarter. The consulting business recorded revenue growth of about 1% in dollar terms or 4% in the RMB terms year-over-year for the quarter.

Finally, our VIP personalized classes business recorded revenue growth of about 37% year-over-year in dollar terms or 40% in RMB terms year-over-year for the quarter.

Next, I will provide some updates on the progress we are making with our Optimize the Market strategy. Beginning with our off-line business this quarter, as mentioned earlier, we added a net of 41 learning centers in existing cities, opened a new training school in the city of Huizhou and a dual-teacher model school in the city of Chengde. Altogether, this increased the total square meters of classroom area by approximately 25% year-over-year and 6% quarter-over-quarter by the end of this quarter.

By the end of Q2 2020, the dual-teacher class model has been introduced into the POP Kids program in 48 existing cities, for U-Can program in 30 existing cities and for both POP Kids and U-Can K-12 businesses in 7 new cities. The initiative supported the increased market penetration in those markets we have tapped into. We also saw improved customer retention rate and scalability of this new model. With this program result, we will continue this strategy in the rest of the year.

On the digital technology front, we've added \$44 million in the quarter to improve and maintain our online-merge-offline, called OMO, standardized classroom teaching system. Most of the investments were recorded under G&A expenses. Furthermore, we also made a stable progress in the pure online koolearn.com business line and other supplementary online education products, which is experiencing growing market demand.

More resources are invested into executing new initiatives in pure online K-12 after-school tutoring business in fiscal year 2020. The investment includes constant development; teachers' recruiting and training; sales, marketing, R&D and other necessary costs and expenses to drive the growth for new pure online programs. With these programs, we're able to reach more students in low-tier cities in an interactive and scalable manner. We believe this will help the koolearn.com to gain new market share in the online education space and drive top line growth.

Now let me walk you through the other key financial details for the second quarter. Operating cost and expenses for the quarter were \$759.9 million, representing a 21.1% increase year-over-year. Non-GAAP operating costs and expenses for the quarter, which excludes share-based compensation expenses, were \$748.7 million, representing a 22.0% increase year-over-year.

Cost of revenue increased by 19.6% year-over-year to \$359 million, primarily due to increase in teachers' compensation for more teaching hours and higher rental costs for the increased number of schools and learning centers in operation.

Selling and marketing expenses increased by 17.7% year-over-year to \$107.8 million.

G&A expenses for the quarter increased by 24.4% year-over-year to \$293.1 million. Non-GAAP G&A expenses, which exclude share-based compensation expenses, were \$282.1 million, representing a 27.1% increase year-over-year.

Total share-based compensation expenses, which were allocated to related operating costs and expenses, decreased by 18.1% to \$11.2 million in the second fiscal quarter of 2020.

Operating income was \$25.3 million, representing a 188.6% increase year-over-year. Non-GAAP income from operations for the quarter was \$36.5 million, representing a 345.6% increase year-over-year.

Operating margin for the quarter was 3.2% compared to a negative 4.8% in the same period of prior fiscal year. Non-GAAP operating margin, which excludes the share-based compensation expenses for the quarter, was 4.7%, compared to a 2.5% in the same period of prior fiscal year.

Net income attributable to New Oriental for the quarter was \$53.4 million, representing a 306.9% increase from the same period of prior fiscal year. Basic and diluted earnings per ADS attributable to New Oriental was \$0.34 and \$0.34, respectively.

Non-GAAP net income attributable to New Oriental for the quarter was \$57 million, representing a 147.8% increase from the same period of prior fiscal year. Non-GAAP basic and diluted earnings per ADS attributable to New Oriental were \$0.36 and \$0.36, respectively.

Net operating cash flow for the second quarter of 2020 was approximately \$291.8 million. Capital expenditures for the quarter were \$52.4 million, which were primarily attributable to the opening of 78 facilities and new learning centers and renovations of the existing learning centers.

Turning to the balance sheet. As of November 30, 2019, New Oriental had cash and cash equivalents of \$1,047.6 million as compared to \$1,414.2 million at May 31, 2019. In addition, the company had \$348.3 million in term deposits and \$2,221.5 million in the short-term investments.

New Oriental's deferred revenue balance, which is cash collected from registered students for courses and recognized proportionally as revenue as the instructions are delivered, at the end of the second quarter of fiscal year 2020 was \$1,570.4 million, an increase of 25.6% as compared to \$1,250.3 million at the end of the second quarter of fiscal year 2019.

Before moving on to our outlook and guidance for the third quarter, I would like to provide some updates on the Koolearn. Koolearn Technology Holdings Limited, a subsidiary of New Oriental, which provides online extracurricular education service in China, also announced its interim results for the fiscal year 2020 earlier today. I'd like to emphasize that Koolearn is a very important platform for New Oriental, and we're optimistic about the opportunities in the online education market and confident in our investments into the platform. During the period, Koolearn has undergone a process of restructuring its college education business line, which had some negative impact on Koolearn near-term revenue growth. Koolearn also continued to invest more resources in executing new initiatives in the areas of content development, teachers' recruitment and training, sales, marketing, research and development and other necessary cost expenses to drive the growth of new online programs. For the first 6 months ended November 30, 2019, Koolearn recorded an 18.8% year-over-year increase in revenue to RMB 567.6 million or USD 81 million. Gross profit was RMB 317.1 million or \$45.2 million. Loss of the period was RMB 87.5 million or \$12.5 million compared to a profit of RMB 36.2 million in the same period of prior fiscal year.

It's encouraging that one of our K-12 business new initiatives, location-based live interactive after-school tutoring courses or Dongfang Youbiao, DFUB, have been rolled out to 128 cities in China and recorded the enrollment growth of 186.2% year-over-year. For more details, please refer to koolearn's financial results announcement in full.

Looking ahead into the next quarter and the rest of the fiscal year 2020, we will continue to be guided by our Optimize the Market strategy and further ride upon the success and momentum we have built. We're confident about capturing a wider range of the market opportunity moving forward. To provide more detail on our areas of focus for the rest of the year, first, we will continue to expand our offline business. We aim to add around 20% to 25% capacity, including new learning centers and expanding classroom area of some existing learning centers for K-12 business in existing cities. In addition, we'll continue to roll out our dual-teacher model schools to a number of new low-tier cities in certain provinces for the whole year.

Second, we'll continue to leverage our investments into digital technologies and introduce our online-merge-offline system to more offline language training and test offerings, especially for our K-12 tutoring and overseas test preparation key businesses. We will continue to make investments and we believe that total spending in absolute dollar terms in fiscal year 2020 will increase compared to the prior fiscal year. Furthermore, we will continue to invest in and execute new initiatives, including product development, teachers' recruiting and training, R&D as well as sales and marketing expenses in pure online K-12 after-school tutoring business, our koolearn.com.

Third, our top priority will remain as to focus on optimizing the utilization of facilities and controlling costs and expenses across the company to drive the continued margin expansion and increase operational efficiency.

The new facilities built in the last 2 fiscal years are being ramped up more efficiently than before. We expect our non-GAAP operating margin of the offline language training and test prep business to continue to expand in the second half of fiscal year 2020. This improvement expects to cover the margin pressure resulting from our online investments in koolearn.com.

On the whole, we expect our overall non-GAAP operating margin to continue to improve year-over-year in fiscal year 2020 compared to the year-over-year decline last 2 fiscal years.

Fourth, as of today, we have decided to move 2 days of classes in our Wuhan New Oriental school from before the Chinese New Year to after the Chinese New Year in view of the disease cases. Classes will be taught via our online live broadcasting technology if the learning centers' operations remain suspended after the Chinese New Year. Please note that classes in the cities, except Wuhan, have not been adjusted or suspended. The health and safety of our students is our top priority, and we'll continue to closely monitor the situation and cooperate with the relevant authorities. Also note, we have taken the impact from the conditions in Wuhan into consideration in our third quarter's guidance. The impact is immaterial based on our current estimation.

Finally, the recent RMB depreciation against the U.S. dollar might cause impact to our earnings in dollar terms for the third quarter of 2020.

Finally, I would like to emphasize that we have great confidence in the fundamentals of our business, which we believe will continue to remain strong. As we continue to execute our Optimize the Market strategy, we are certain that New Oriental will continue to capture the sustainable growth opportunities in the market and deliver long-term value for our shareholders.

Looking at the near-term and our expectations for the next quarter, we expect total net revenues in the third quarter of fiscal year 2020 to be in the range of \$983 million to \$1,006.4 million, representing a year-over-year growth in the range of 23% to 26%. If not taken into consideration the impact of the potential change in exchange rate between RMB and the U.S. dollars, the projected revenue growth rate in our functional currency RMB is expected to be in the range of 26% to 29% for the third quarter of fiscal year 2020.

The exchange rate used to calculate expected revenue for the third quarter of fiscal year 2020 is 6.95. The historical exchange rates used to calculate revenues for the third quarter of fiscal year 2019 was 6.81.

I must mention that these expectations reflect New Oriental's current and preliminary view, which is subject to change.

At this point, I will take your questions. Operator, please open the call for this. Thank you.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from line of Mark Li from Citi.

Mark Li - Citigroup Inc, Research Division - Director

Management, congratulations on the very strong margin performance for this quarter. We think it's beaten guidance by -- pretty nicely. May I know what are the major reasons for the non-GAAP operating margin for this quarter? And also, I would like to know our revenue guidance breakdown across different segments.

Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

Okay, Mark. Yes, we've beaten the margin guidance a lot. Our non-GAAP operating margin rose by 720 basis points in this quarter. I think it's because of the following reasons. Number one is the -- I think the continued margin expansion is mainly driven by the better utilization of the facilities. Typically, our top line growth is over 30% year-over-year in RMB terms, but the expansion in the last trailing 12 months is just 25%. And also, number two is we've built a standardized and modularized and systemized operating process. So you see the result. We achieved outstanding improvement in the operational efficiencies, and we get a lot of leverage on the selling, marketing and G&A expenses. And finally, we're seeing the revenue acceleration. Typically, we're taking market share from the small player in the market. So the revenue is very good. And I think those 3 reasons get us to the better results of the margin expansion. But yes, as I mentioned in the prepared remarks, in the rest of the year, even in the Q3 and Q2 in fiscal year '20, I think we still got more leverage going forward. So we believe we will have the margin expansion in the rest of this fiscal year. And even for the fiscal year '21, I think our margin will get the expansion as this year, okay?

So -- and the revenue breakdown, yes, in the Q3 revenue guidance, I think the K-12 business will grow by 40% in RMB terms, okay? What I'm saying is in RMB terms, year-over-year growth 40%. And overseas test prep, I think, to the low single digit growth. And the domestic test prep, it will be down by, let's say, 3% to 4%. And the overseas consulting business, the growth will be over 20%. So this is the breakdown of the Q3 guidance, okay?

Operator

Your next question comes from the line of Yuzhong Gao.

Yuzhong Gao - *China International Capital Corporation Limited, Research Division - Analyst*

Congrats on the very strong results. So we noticed that you seems to have revised up your capacity expansion target from 20% to 25%. So how should we think about the margin expand scale in the second half of fiscal year '20?

Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

Okay. Yes. This quarter, the quarter-over-quarter expansion was 6% combined with 3% in Q1. So we got 9% in the first half of this fiscal year. And typically, in terms of the seasonality, we opened more learning centers in the second half of the year. So it's more backloaded. And so I think we believe the whole year expansion plan will be somewhere around 20% to 25%. Actually, it's close to 25%. --But the top line growth will be somewhere around 30%. I think it's impossible to get over 30% top line growth in RMB terms. So in the rest of the year, as I said, I think we do have more leverage on the GP level and the SG&A level. --But typically, we don't give the detailed guidance of the margin expansion in the next quarter. But I believe we can get the margin expansion in the rest of the year and the year after.

Operator

Your next question comes from the line of Tian Hou of T.H. Capital.

Tianxiao Hou - *T.H. Capital, LLC - Founder, CEO & Senior Analyst*

The question is related to your regional expansion. So now we have more than 1,300 learning centers. So for the new learning centers you're planning to open, where are those centers going to be, in what kind of a region? And to support the additional expansion, 20% to 25%, and how do you prepare your teachers' force, the team of teachers. So that's the question related to expansion.

Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

Tian, yes, we have 1,300 learning centers in total, and we plan to open, let's say, the 20% to 25% new capacity in one year. And so most of the new learning centers we set up going forward will be happened in the existing cities. Internally, we only allow the good performing schools to open more learning centers in their cities. We have another business model called Dongfang Youbiao, belongs to the Koolearn, and we will open more -- the new business in low-tier cities, okay? There's 2 ways, okay? For a traditional offline business, we'll open more cities -- schools or learning centers in existing cities, okay? And as for teachers resource, we believe we pay the best in the market to our teachers. And also, since last year, we've built up the online teachers' training system. So that means we have the more ability to generate or produce more qualified teachers than before. So we believe we have the more qualified teachers to support the opening of the new learning centers going forward.

Operator

Your next question comes from the line of Alex Liu of China Renaissance.

Zhangxiang Liu - *China Renaissance Securities (US) Inc., Research Division - VP*

I just wanted to follow up, first, on the Tian's question. Could you share more color on, for example, how fast is the capacity growth in top cities, for example, Beijing right now? And a follow-up question. I think the overseas test business is growing. If I remember correctly, it's low-single-digit growth this quarter. And may I know what was the reason behind this seemingly a little bit unexciting growth in the past few quarters?

Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

Yes. Actually, we opened the learning centers almost everywhere. Basically, that city got better result in the last trailing 12 months. So we opened the learning centers in the top tier, Tier 1 or Tier 2 cities, and we also opened the learning centers in, like, the Tier 3, Tier 4 cities. So I think the only one indicator for us to decide whether or not to open the learning centers is the performance of that school last year, okay? And I think even for the big cities like Beijing and Shanghai, Wuhan and Guangzhou, I think there's a lot of room to open more off-line learning centers, okay? So yes and the overseas test prep, yes, this quarter, the numbers is no good, only 5% in RMB terms year-over-year growth for overseas test prep business. I think the main reason is because of the United States, China, the 2 countries' relationship change. So I think our non-United States-related businesses like the (inaudible) the United States-related businesses keep flattish this quarter. And we in Q3, I think the growth will be flattish again. So I think this is the main reason, okay?

Zhangxiang Liu - *China Renaissance Securities (US) Inc., Research Division - VP*

Okay. And just, sorry, one more follow-up. On the gross margin, there seems to be a notable jump this quarter. May I know what was the driver behind this? There's a notable improvement on the gross margin.

Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

Firstly, the revenue growth, be it in our guidance, okay, as I said, we are taking market share from the small players, and also, there are a lot of schools provide very good numbers of this quarter on top line growth. And suddenly, if you compare the top line growth with the capacity expansion, you know we have the better leverage on the rental side. And yes, I think those are the 2 key reasons to explain the GP margin expansion.

Operator

Your next question comes from the line of Lucy Yu of Bank of America.



Lucy Yu - BofA Merrill Lynch, Research Division - Research Analyst

I got one question on the cross-scheduling. So actually this year, Chinese New Year is earlier than last year. So is it fair to say that we started our spring semester a little bit earlier than last year? So thematically, in February, we are seeing more positive benefit from this kind of calendar shift, is that true? If so, can you give us a quantified impact on the cross-scheduling?

Zhihui Yang - New Oriental Education & Technology Group Inc. - CFO

I think, yes, this year, the Chinese New Year is a little bit earlier, but I think the impact from the cross-schedule is very small, very minimal, okay? But I must mention that typically in last year, the Q2, we started to do some, like, the facility movement and cross-scheduling changed in the last year Q2, which led to a postponement of some K-12 classes from Q2 to Q3 last year. So that means this year, we have an easier comparison in Q2, but a little bit harder comparison in Q3. But anyway, it's a seasonal or just tiny difference, the issue is not a big issue, okay?

Lucy Yu - BofA Merrill Lynch, Research Division - Research Analyst

Okay. And the second question is that in the first half, you have already expanded your non-GAAP operating margin by close to 5 percentage points. This is much higher than your previous expectation of 1.5% to, like, 2% for the full year. So is it fair to say the risk is on the upside to your full year guidance in terms of margin?

Zhihui Yang - New Oriental Education & Technology Group Inc. - CFO

Yes. I don't guide the second half of the year margin guidance, but we do believe we will have the margin expansion in Q3 and Q4, okay? I think for the whole year, the margin will be better than we expected several months ago.

Operator

(Operator Instructions) Your next question comes from the line of John Choi from Daiwa.

Hyungwook Choi - Daiwa Securities Co. Ltd., Research Division - Head of Hong Kong & China Internet and Regional Head of Small/Mid Cap

I have a question on your online. I know Koolearn basically on the cost said they'll step up more and open up in the lower-tier cities. Can you kind of give a sense, will the EDU and Koolearn in general will kind of step up the investment in online and, as a result, will see more in the back-end loaded for the fiscal year in terms of marketing expenses and user acquisition costs? And just quickly, after the regulation, which has been in place for more than about a year on the offline schools, are you seeing more visibility or better visibility compared -- given that the smaller players are being phased out and, as a result, you're seeing higher retention rate and better capacity growth in selected regions?

Zhihui Yang - New Oriental Education & Technology Group Inc. - CFO

Yes. As for the Koolearn investment, on Koolearn, yes, this year, we started to invest on the koolearn.com. It includes the content development or teachers' training or R&D and, yes, some marketing expenses things this fiscal year. And in the first half of the year, the margin drag from the Koolearn to EDU roughly has blended a bit, okay? This is the margin impact from the Koolearn for EDU. And in the second half of the year, we expect we still have some negative impact of the margins from the Koolearn. But we believe the margin expansion of the core business, where our school business, offline business, will cover the margin pressure from Koolearn. So we believe, on the whole, our margin will be expanded in the rest of the year, even though we spend a lot on the Koolearn.

And your #2 question is about regulation. Last year, there were several new regulations. And -- but as I said, in the last 2 earnings call, we almost met all the requirements by the new regulations in almost all the cities, and we have seen some small players disappear from the market, and we

have seen some students join our classes who are the students from small player. So I think our target even going forward is to provide the best service to the Chinese students, and we believe we can take more market share from the old players in the market.

Operator

Your next question comes from the line of Binnie Wong of HSBC.

Wai Yan Wong - HSBC, Research Division - Head of Internet Research of Asia Pacific & Analyst

So question here is that if you look at '20, like last year, right, we see a wave of a lot of online education companies, small- and middle-sized ones, compete, right. Especially, if you see, the user acquisition cost, right, has been rising up a lot. So if you look into 2020, how do you see -- I mean, calendar 2020, how do you see that will change? Do you see that our marketing strategy will be different from our players? And also, if you look at, I guess, the deceleration of growth in Koolearn, do you think that will continue or there will be some drivers to reaccelerate the online business growth?

Zhihui Yang - New Oriental Education & Technology Group Inc. - CFO

Okay. I think, firstly, Koolearn has been in transition mode in the last 2 to 3 quarters. As you know, we changed the key management members last year, and we prefer to give the new management team member more time, okay? And education is a very special business. We don't intend to do the business too fast by, like, spending the crazy dollars on the marketing activities. So even in the last year, we didn't attempt, like, burning the money to acquire the students. And going forward, I think we will allow the Koolearn to spend a little bit more on marketing expenses. But it's not a huge number, okay? We prefer to make the more or huge investments on the R&D and, like, the teachers' training or the product itself. This is our strategy.

Operator

Your next question comes from the line of Alex Xie of Crédit Suisse.

Alex Xie - Crédit Suisse AG, Research Division - Analyst

Management, congratulations on very strong results. So I would like to ask about our magnitude of utilization rate improvement. I think in the last quarter's earnings call, we mentioned it was 21% and 2% year-over-year increase.

Zhihui Yang - New Oriental Education & Technology Group Inc. - CFO

Yes, this year, I think the utilization rate for this year is somewhere around 21%, which means we got 200 bps up of the utilization rate. So that's why you see the margin expansion, okay? And so going forward, as I said, we plan to open 20% to 25% new learning centers capacity, and it brings us, like, 30% top line growth in RMB terms year-over-year. So I think you will see the higher utilization rate going forward in the rest of this fiscal year and the year after.

Operator

Your next question comes from the line of Sheng Zhong of Morgan Stanley.

Sheng Zhong - Morgan Stanley, Research Division - Associate

I wanted to ask a question about dual-teacher model because you are still adding more dual teachers in the cities. So can you share some operating data about the margin of dual-teacher model? And how -- what the current class -- what the average class a teacher can teach in the dual-teacher model? And at the same time, I noticed that you have still invest a lot in your digital technology. Wondering whether this is partly because of this dual-teacher model. And if possible, can you share more color on your -- on the spending going forward?

Zhihui Yang - New Oriental Education & Technology Group Inc. - CFO

Okay. Yes, dual-teacher model, yes, we changed our dual-teacher model strategy last year. So we focused more dual-teacher model in the Hubei and Hunan province. So now we have the 7 low-tier cities for both POP Kids and U-Can programs to buy the dual-teacher model. And now the revenue contribution from the dual-teacher model is very small. So I think the growth is very high, but revenue contribution is very small. And now I think it's too early to say the margin of the dual-teacher model because it's in the early stage. But theoretically, as I said, I think the dual-teacher model margin should be higher than the offline business, okay? And the -- yes, this quarter, the OMO investment in this quarter, we invested \$44 million on the OMO ecosystem. I think this is on track, because we started to invest on the OMO things 3, 4 years ago, and we started to bear fruits last year. And I think this is very good result. I think that means we bore fruit from the investments we made several years ago. So -- for the whole year, I think we plan to spend somewhere around \$150 million to \$160 million for the whole year. It's a little bit higher than we expected several months ago. But I think even though we spend a little bit more, but it will be covered by the offline school margin expansion. So that will be okay. You will see the overall margin expansion even though we spend a little bit more, okay?

Sheng Zhong - Morgan Stanley, Research Division - Associate

Yes, we are happy to see you spending more on the technology improvement. So can you give some color on the spending areas of our technology?

Zhihui Yang - New Oriental Education & Technology Group Inc. - CFO

Typically, we hire more IT people and the content development people in our head office to provide more better products for offline schools and the dual-teacher model schools. And also, we hired some new people work for AI department. And yes, so I think most of the investments we spent is only happened in the head office. But we do believe it will bring us the better student retention rates going forward. And we do believe this money we spend today will bring us better quality product in the future.

Operator

Your next question comes from the line of Hugo Shen of Macquarie.

Hugo Shen - Macquarie Research - Analyst

I wondered if you could give us the breakdown of enrollment growth by business in this quarter.

Zhihui Yang - New Oriental Education & Technology Group Inc. - CFO

The enrollment -- do we disclose it, the enrollment breakdown?

Sisi Zhao - New Oriental Education & Technology Group Inc. - IR Director

You can send e-mail to me, and I will send you the details, okay, after the call.

Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

Yes, because of the long question.

Operator

Your next question comes from the line of Felix Liu of UBS.

Felix Liu - *UBS Investment Bank, Research Division - Research Analyst*

Congratulations, Stephen, for the very strong quarter. So 2 quick questions from me. One is that you mentioned the ramp-up is getting faster than previously. So could you share us the latest time line to ramp up any new center? And second one is a follow-up to the previous question on OMO investment. So I understand a lot of the costs are in staff salary. So going forward, if we look at the second half of next year, do we plan to further increase the headcount? Or is it likely to stay at this level?

Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

Yes. Historically, let's say, 2 to 3 years ago, typically, we need 12 months to get the breakeven point for the new learning center, but now it's only spend 5 to 7 months to get the breakeven point. So that means we ramp up new learning centers faster than before. And I think this is one of the reasons that we decided to open more learning centers, okay, in every year, okay? And to your second question is about the OMO investments. Yes, I think we will hire more people, more qualified, more talented people work for the IT department and the content development team also for the AI department because, firstly, I think it's a good investment. We spend more money today that we get better future. But anyway, I think the total spending, it will be controlled by the management team. We don't want to waste the money, okay? So as I said, even though we spend a little bit more on the OMO investments, but we do believe we have the margin expansion going forward, for the second half of the year and the year after, okay?

Felix Liu - *UBS Investment Bank, Research Division - Research Analyst*

Okay. Great, great. Glad to see we have the budget to invest in the longer-term growth. Congratulations, again, on the strong quarter.

Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

Okay. Thank you, Felix.

Operator

Your next question comes from the line of Christine Cho of Goldman Sachs.

Hyun Jin Cho - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

Just a quick question on the revenue guidance. You mentioned that you consider the Wuhan situation in terms of coming up with the third quarter guidance. Can you give us a little bit more detail here? And also, if this situation prolongs, what are some of the alternatives you can consider to kind of mitigate the impact from the situation?



Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

Yes. Our Wuhan school actually decided today to move the 2 days courses before Chinese New Year to sometime after the Chinese New Year because of the new disease, okay? But also, we have the Plan B, let's say, if after the Chinese New Year, we cannot run the business by offline, we'll make it up by the online courses, okay? Actually, we are ready. But so far, we have not made a decision of the class adjust or suspend in the other cities except for Wuhan. So Wuhan is the only one. And yes, we have taken some impact from the business in Wuhan, but the amount is not material, okay? Wuhan's revenue contribution for New Oriental is 4%, okay? But don't forget, 45 days have passed, and also, we have the [backup] (corrected by the company after the call) plan, Plan B, to make it up. So I think the impact will be immaterial so far by the current estimation, okay?

Operator

Your next question comes from the line of Youngrin Kim of CLSA.

Youngrin Kim - *CLSA Limited, Research Division - Research Analyst*

Management, congrats on the good quarter. I have 2 questions. The first is, how much of revenue growth is actually coming from organic growth versus stealing market share from other small players? That's my first question. My second question is, I know in the past you have provided mid-to long-term margin guidance of 17% to 19%. So do you still stick by this margin guidance? Or do you see room for increase or things like that?

Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

Okay. Yes, the organic growth, I think, typically, in the first 12 months after the new learning centers opening, it will bring us, let's say, for example, we opened 20% new learning centers. But in year 1 till date, it will bring us 5% to 10% new revenues. So I think all the others are the organic growth. And we don't have the numbers of how much market share we got from the small players. We're -- okay, we just do our business to get a 30% top line growth, that's it, okay? Sisi, do you have the numbers?

Sisi Zhao - *New Oriental Education & Technology Group Inc. - IR Director*

No, it's hard to quantify, but we keep taking market share from small players every day, almost every day. And the market growth is like 10%, 15%. But our K-12 businesses are growing over 40%. So definitely, majority of the growth is from taking market share from other small players in each city.

Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

And the mid- and long-term margin guidance, we don't change the mid- and long-term actually, it's mid-term margin guidance. We keep it as 17%. And this year, the market expansion is better than we expected. And we are more optimistic on the overall margin expansion in the rest of the year and the year after, okay?

Operator

Your next question comes from the line of Joy Wei of 86Research.

Joy Wei - *86Research Limited - Analyst*

So my question is, during the quarter, we saw that U-Can and POP Kids growth accelerated. So what's driving that? Do you see more opportunities in terms of prospectives like cross offering and also product format?

Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

I think there are several reasons. Number one is if you remember clearly in the last quarter's earnings call, the summer promotion/retention rate is 5% higher of this year than last year. So this is the number one reason. Number two is, we are seeing the higher student retention rate for both U-Can and POP Kids program. Actually, the U-Can business, the retention rate is close to 80% and the POP Kids retention rate is close to 90%. So it's a couple -- it's higher than those numbers of last year. And third, we don't spend a lot on marketing expenses -- the selling and marketing expenses. In this quarter, it's just increased by, am I right, 17%, okay? But I think that we typically would rely on word-of-mouth to acquire the new student enrollments. And that means we're providing better products to the students than before. So it bring us the good result, better result than we expected, okay? Is it clear?

Joy Wei - *86Research Limited - Analyst*

Yes.

Operator

We are now approaching the end of the conference call. I will now turn the call over to New Oriental CFO, Mr. Stephen Yang, for his closing remarks.

Zhihui Yang - *New Oriental Education & Technology Group Inc. - CFO*

Again, thank you for joining us today. If you have any other further questions, please do not hesitate to contact me or any of our Investor Relations representatives. Thank you. Thank you, guys.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.

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