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PRESENTATION

Operator

Ladies and Gentlemen, thank you for standing by and welcome to the Tarena International Incorporated's Second Quarter 2016 Earnings Conference Call.

At this time, all participants are in a listen-only mode. After management's prepared remarks there will be a question-and-answer session. Today's conference is being recorded. If you have any objections you may disconnect at any time.

I would now like to turn the conference over to your host for today's conference, Ms. Helen Song, Tarena's Senior Investor Relations Manager. Please go ahead.

Helen Song - *Tarena International Incorporated - Senior Investor Relations Manager*

Thank you, operator. Hello everyone and welcome to Tarena's second quarter 2016 earnings conference call.

The Company's earnings results were released earlier today and are available on our IR website, ir.tedu.cn, as well as on Newswire services.

Today you will hear opening remarks from Tarena's Founder, Chairman and CEO, Mr. Shaoyun Han, followed by our Chief Financial Officer, Dennis Yang, who will take you through the company's operational and financial results for the second quarter 2016, and give guidance for the second quarter and full year of 2016. After their prepared remarks, Mr. Han and Mr. Yang will be available to answer your questions.

Before we continue, please note that the discussion today will contain certain forward-looking statements made under the Safe Harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. These forward-looking statements are subject to risks and uncertainties that may cause actual results to differ materially from our current expectations. Tarena does not assume any obligation to update any forward-looking statements except as required under applicable law.

Also please note that some of the information to be discussed includes non-GAAP financial measures as defined in Regulation G. The U.S. GAAP financial measures and the information reconciling these non-GAAP financial measures to Tarena's financial results prepared in accordance with U.S. GAAP are included in Tarena's earnings release which has been posted on the Company's IR website at ir.tedu.cn.

Finally as a reminder, this conference is being recorded. In addition, a webcast of this conference call is available on Tarena's Investor Relations website.



I will now turn the call over to Mr. Shaoyun Han, Tarena's Founder, Chairman and CEO. Mr. Han will speak in Mandarin and Mr. Yang will translate.

Shaoyun Han - *Tarena International Incorporated - Founder, Chairman, and CEO*

(Interpreted) Thank you, Helen, and welcome, everyone, to our second quarter 2016 earnings conference call.

I am pleased to report that we delivered another solid performance in the second quarter of 2016, with better-than-expected growth in both net revenues and profitability. Our net revenues increased by 35% to reach \$55.91 million, exceeding the high end of our previously issued guidance which is \$52.5 million in net revenues and 27% year-over-year growth rate.

As we mentioned in our first quarter earnings call, the significant growth in student enrollments in the first quarter brought us a strong course enrollment number for the second quarter, which is an operating metric that better correlates with the revenue recognized in the quarter. This is primarily reflected in our dramatic growth in net revenues this quarter. In the second quarter, our course enrollment totaled 23,694, an increase of 39% year over year, and it is the primary factor contributing to our revenue growth in the quarter.

Our student enrollment number, which is one of the leading indicators and defined as the number of new students recruited and registered in the quarter, also grew strongly at 22% year over year to reach 26,747. This marks a record-high quarterly student enrollment figure in Tarena's entire operating history. Thus, the student enrollment in the first half of 2015 totaled 49,777, increasing by 34% year over year, supported by the strengthened brand recognition, comprehensive cost offerings, as well as good track records in education quality, Tarena has been able to attract more and more students for training.

In the second quarter, the Company continued to explore the growth momentum in both IT and non-IT subjects was more an appropriate strategy to better cater to the market trend. The background and development course that we launched last year experienced a robust growth, with tremendous market demand after one year's operation. Student enrollment this quarter have exceeded 15% of total student enrollments. IT courses together continued to grow strongly with a 45% year-over-year growth and accounted for 57% of total student enrollment in the second quarter of 2016.

This quarter we have more courses with enrollments above 1,000. Diversifying course offerings and expanding into other high-growth disciplines have always been our objective priority in the past few years, which brings us a unique leading position in professional education market. Besides professional education courses, we launched key education programs under the name Tongcheng and Tongmei at the end of 2015, to target younger audience with primary to high school.

In the second quarter of 2016 we launched Tongchuang, a brand-new course on Java programming and 3D printing for keys in Beijing. The new initiative in K-12 education has shown progress towards our target. By the end of second quarter, K-12 program has been rolled out in 14 cities including Beijing and enrolled nearly 1,000 students, including almost 700 students enrolled in second quarter.

Since the first quarter of this year we've started to implement our teaching at the proper levels strategy and launched advanced-level courses in five major subjects, which we believe can help our elite students equip with better skills and make them more competitive in job market. After pilot rollout in several large cities since March this year, we successfully attracted more students and the total number of students in advanced courses reached 18%. Going forward, we will continue to execute on this initiative in delivering differentiated education services to our students, which is not only diversifying in our exceeding course offerings but also further consolidating our competitiveness by designing more appropriate course content to different students.

In terms of new learning centers, we opened six in the second quarter 2016 and closed 3, with a net addition of 3 learning centers, compared to the net addition of 6 learning centers in the same period last year. Specifically this quarter, we opened 1 learning center in each of the following six cities which are Guangzhou, Chengdu, Wenzhou, Jinan, Qingdao and Jongzhou, among which Wenzhou is a third-tier city that we newly entered. As a result, the total number of learning centers grew from 135 in the previous quarter to 138.



In addition to opening new learning centers, we also expanded leased area in a number of the existing learning centers, so that our total seat capacity increased to 47,632, up by 22.5% from same period last year and 8% from the end of previous quarter. In the meantime, we're focused to optimizing facility resources and achieve standard utilization rate of 73.1%, almost keeping the same level to the same period last year, reflecting operating efficiencies, stabilized at high level, as we continue business expansion.

As a key indicator that shows our education quality and outcome, job placement bracket is an operating metric that we are always proud of, and this quarter is no exception. I'm very pleased to report that in second quarter of 2016, the market is getting better and we continue to deliver outstanding employment results for our students. The six-month post-graduation job placement rate in this quarter was above 90%. This best-in-class result will further support our market-leading brand and overall competitive position in the industry.

Since last year the company has conducted more efforts in promoting business optimization. Reflecting from the success on margin expansion this quarter, we're pleased to see the significant year-over-year improvement in business operational efficiency. Our gross margin in second quarter increased by 1 percentage point year over year to 70.2% from 69.1% in the same period last year. Our non-GAAP operating margin expanded by 8.6 percentage points year over year to 14.9%, from 6.4% in same period last year. We kept good momentum in improving our profitability in the second quarter through the increased business scale and optimized sales and marketing workflows to drive better operational efficiency. Our CFO Dennis will elaborate on this further in their later remarks.

In the first quarter we announced the purchase of a property which was located in Beijing economic technological development area. This building is mainly for teaching purpose and serves as a multi-function learning center for those students who come to Beijing for training. The building was delivered to the Company in the second quarter and will be put into use in third quarter as renovation work is completed. The center has a capacity of more than 2,000 seats and it is expected that more than 6,000 students take their training in this center annually.

Another quick update on the progress on our online learning platform, TMOOC.CN, which was launched in March 2015. The number of registered TMOOC users have reached more than 185,000 today and our proprietary content library currently offer nearly 16,000 hours of video content. Through TMOOC we also generated 19,714 VIP users to date who have become our paying customers.

With this, I will now turn the call over to our CFO Dennis Yang to discuss second quarter financial results and outlook for the third quarter and full year.

Dennis Yang - *Tarena International Incorporated - Chief Financial Officer*

Thank you, Han-zong, and hello everyone on the call. Since you already have all the detailed numbers in the press release, I will review financial results for the second quarter of 2016 briefly, and focus on a couple of more important areas.

For the second quarter of 2016 we grew our net revenue by 35% year over year to \$56 million from \$41 million same period last year. As Han-zong explained earlier, the student enrollment is primarily a factor for our revenue growth. Total student enrollments in the second quarter of 2016 increased by 22% year over year to 26,747. With the strong student enrollment in the first quarter -- first two quarters of 2016, the total course enrollment increased by 39% year over year to 23,694 in the second quarter of 2016.

Average revenue per course enrollment in the quarter, as defined by net revenues divided by course enrollments, was \$2,360, compared to \$2,417 in the same period a year ago, a 2.4% decrease, was mainly due to the RMB depreciation against U.S. dollars since August 2015. If we exclude impact of RMB depreciation, average revenue per course enrollment in this quarter in RMB increased by 4% year over year, which resulted from increased standard tuition fees for selected courses starting from March 2016.

Now let's move to cost of revenues and operating expenses. Cost of revenues in the second quarter increased by 31% year over year to \$17 million, mainly due to higher personnel costs resulting from increased number of faculty staff, higher rental costs, and higher depreciation expenses resulting from our increased learning center resources.

Gross profit increased by 37% year over year to \$39 million. Our gross margin also increased by 104 basis points to 70% in the second quarter from 69% in the same period last year. The improvement in gross margin was mainly due to the increased standard tuition fees in RMB.

Selling and marketing expenses increased by 15% year over year to \$19 million, mainly due to high personnel costs and higher advertising and marketing expenses as we expanded our network of learning centers, and grew our student enrollments. By improving our sales and marketing functions operational efficiency, however, we can see a decrease of average advertising spending per student enrollment to \$299 in the second quarter of 2016, from \$336 in the same quarter a year ago. As previously communicated with investors, in the third quarter 2015 we have realized a benefit of Baidu account migration, further enhance our sales and marketing efficiency by restructuring our sales and marketing function and optimizing the workforce.

General and administrative expenses increased by 41% year over year to \$12 million, mainly due to higher personnel costs and higher share-based compensation expenses for increased number of general and administrative personnel to support our growing operations, and to a lesser extent, we made media bonus accruals because we achieved higher-than-expected business performance in the first half of 2016.

As communicated to investors previously, the bad expenses resulted from the legacy issue of installment payment plans extended by Tarena to our students. After having partnered with the third-party financing providers and implemented strengthened internal controls over credit granting and cash collections to reduce the size and overall risks of accounts receivable, we're turning the corner of this legacy issue and expect the bad expenses for the fiscal year 2016 will be much lower than those recorded in 2015.

Research and development expenses decreased by 13% year over year to \$1.8 million, mainly due to lower personnel costs of our instructors allocated to content development activities for our courses. As a result, operating profit was \$6.1 million for the second quarter of 2016, which was more than five times as compared with that in the same period last year. Our non-GAAP operating profit for the second quarter was \$8.3 million, which increased 217% from non-GAAP operating profit of \$2.6 million in the same quarter 2015.

Our net profit was \$6.6 million in the second quarter of 2016, compared to \$2.9 million in the same period in 2015. Non-GAAP net income increased by 84% to \$7.9 million in the second quarter of 2016 from a net profit of \$4.3 million in the same period last year.

GAAP basic and diluted net income per ADS were \$0.12 and \$0.11, respectively, in the second quarter of 2016. Non-GAAP basic and non-GAAP diluted net income per ADS was \$0.14 and \$0.13, respectively in the second quarter of 2016.

We generated \$25 million in positive operating cash flow in the second quarter of 2016, as compared to \$16 million operating cash flow generated in the same period last year. In addition, we incurred \$21 million in capital expenditures, including \$70 million we spent in purchased the office building in Beijing Economic Technology Development Area and the rest in opening new learning centers and upgrade and maintenance of our IT infrastructure.

Looking forward to the third quarter of 2016, if taken into consideration the impact of RMB depreciation against the U.S. dollar, total net revenues for the third quarter of 2016 are expected to be between \$70 million and \$72.5 million, representing an increase of 17% to 21% on a year-over-year basis. If not including the impact from the depreciation of RMB against U.S. dollars, the projected revenue growth rate is expected to be in the range of 24% to 28% on a year-over-year basis from the third quarter of 2016.

After taking into account the actual performance -- actual performance in the first two quarters and other business information available to us, we also increased our full year 2016 total net revenue expectations by \$2.5 million, to be between \$232.5 million and \$238.5 million, representing an increase of 23% to 26% on a year-over-year basis. If not including the impact from the depreciation of RMB against U.S. dollar, the projected revenue growth rate is expected to be in the range of 30% to 33% on a year-over-year basis for the fiscal year 2016.

This concludes my remarks and I now hand the phone over to the operator who will then open the line for questions. Operator, please.



QUESTIONS AND ANSWERS

Operator

Thank you, Mr. Yang. Ladies and gentlemen, we will now begin the question-and-answer session.

(Operator Instructions)

We will now take our first question from Zoe Zhao from Credit Suisse. Please go ahead.

Zoe Zhao - Credit Suisse - Analyst

Hi. Hi, management. Thank you for taking my question, and congratulations on the strong quarter. I have two questions mainly.

First of all, could you share with us your July and August enrollment run rate? And then on an apple to apple basis, excluding the enrollment time changes last quarter, what is this quarter's enrollment growth?

And the second question is, what is the current percentage of student loan taken on your own balance sheet? We understand that the Q-on-Q accounts receivable has declined. So, just a housekeeping question on the bad debt expenses booked this quarter. Thank you.

I'll translate my question myself.

(Chinese language spoken)

Shaoyun Han - Tarena International Incorporated - Founder, Chairman, and CEO

(Interpreted) So for the first question, on the enrollment towards July and August, we met our target in July on our student enrollments. For student enrollment of August, yearly we calculate in total monthly enrollment by the end of a month. So, now is only mid of August so it's hard to tell the accurate number for the student enrollment in August. But based on our observation, the student enrollment in August is also can meet our target.

Dennis Yang - Tarena International Incorporated - Chief Financial Officer

So the second question is about bad expenses. The total bad expenses we made for second quarter worth \$1.7 million. So right now the installment payment plans is only extended to our students acquired from campus channel. So the overall percentage of students can take our installment plans less than or around 10%.

Zoe?

Zoe Zhao - Credit Suisse - Analyst

Thank you.

Operator

We will now take our next question from Wendy Huang from Macquarie. Please go ahead.



Joe Yu - *Macquarie - Analyst*

Thank you management. This is Joe Yu asking question on behalf of Wendy.

So, first, I have a macro related question. So I noticed your job placement rate remained at over 90% this quarter. So, just wondering, do we expect the cooldown of China's external market impacting your student placement rate going forward? Hello?

And I have a follow-up.

Shaoyun Han - *Tarena International Incorporated - Founder, Chairman, and CEO*

(Interpreted) It is true that the China economy brings us some challenges in job placement in the first half of 2016. But our strategy on diversification of course offerings can help us to solve this issue. We deliver the diversified course offerings to our students and allow them to meet the market demand -- changes in market demand.

Let's take instance, IT courses grew probably in first half in 2016 purely because the market demand on IT positions required from in China market. So we encourage students to take -- more students to take the IT courses in the first half of, like web-front development, this very hard topic in China market. So this course enrollment -- this course take more students for their training to help them to be more competitive in job market.

Joe Yu - *Macquarie - Analyst*

Thank you. And a quick follow-up on your Baidu expense. So, did your total spending and also CPC on Baidu increased this quarter?

I will translate myself.

(Chinese language spoken)

Shaoyun Han - *Tarena International Incorporated - Founder, Chairman, and CEO*

(Chinese language spoken)

Dennis Yang - *Tarena International Incorporated - Chief Financial Officer*

Let me translate what Han-zong in response to the question.

At the very beginning, Baidu changed their policy in May and early June, we observed higher CPC for Baidu searches. Other than that, the CPC cost is back to normal. Now and going forward we believe the Baidu search CPC cost will be kept in a normal level.

Shaoyun Han - *Tarena International Incorporated - Founder, Chairman, and CEO*

(Interpreted) So you can see that our advertising spending per student enrollment kept at similar level in second quarter as compared to in the previous quarter.

Joe Yu - *Macquarie - Analyst*

So that means your total spending, just to clarify, the total spending on Baidu didn't increase, right?

Dennis Yang - *Tarena International Incorporated - Chief Financial Officer*

Actually we -- our target is to maintain a certain level of advertising spending per student. So the overall, the total student enrollment in the second quarter is greater than our first quarter, so the total spending on Baidu was getting bigger.

Joe Yu - *Macquarie - Analyst*

Okay, great. Thank you.

Operator

(Operator Instructions)

We will now take our next question from Fan Liu from Goldman Sachs. Please go ahead.

Jason Huang - *Goldman Sachs - Analyst*

Hi, this is Jason Huang asking on behalf of Fan Liu. Congratulations on a strong quarter.

Your R&D expense seems to be a bit lower than expected. Is this a one-off factor? What can we expect going forward? And also, can you update us your operating margin outlook for the full year on the back of your higher top-line guidance and your new initiatives in the K-12 and corporate level initiatives? Thanks.

Dennis Yang - *Tarena International Incorporated - Chief Financial Officer*

Let me answer your questions. In terms of R&D expenses decrease, we completed several R&D projects in middle of the year. So the last time of our instructors spend in R&D projects in second quarter. This is the reason why we saw the R&D expenses as a percentage of revenue decreased in this quarter.

On the operating margin, we're pretty sure that the operating margin will be expanded as compared to the last year. Our -- right now the estimation is about 1% to 2% expansion for the whole year 2016.

So what is the third question, can you remind me?

Jason Huang - *Goldman Sachs - Analyst*

Oh, the -

Dennis Yang - *Tarena International Incorporated - Chief Financial Officer*

K-12? What's your question about K-12? Can you repeat it?



Jason Huang - *Goldman Sachs - Analyst*

Sure. Okay. So, since like your K-12 program is on track, especially because you're launching Tongchuang, so, what can we expect going forward for the K-12 business? And especially you mentioned previously that the K-12 margin much higher than the old business as well?

Dennis Yang - *Tarena International Incorporated - Chief Financial Officer*

Yeah, actually the K-12 we expect higher margins, this is true. But for 2016, the overall percentage of revenue contributions from K-12 program will be very small, because this K-12 program just started in 2016. We saw a very strong market demand in the market for IT-related K-12 subjects in China. We launch Tongchuang robotic 3D printing program for kids in the second quarter of 2016. Together with Tongcheng and Tongmei, we expect total student enrollment for K-12 program will be around 3,000 students for the whole year.

Jason Huang - *Goldman Sachs - Analyst*

Thank you. Very helpful.

Operator

We will now take our next question from [Zhong Chen] from Industrial Securities. Please go ahead.

Zhong Chen - *Industrial Securities - Analyst*

(Chinese language spoken)

Shaoyun Han - *Tarena International Incorporated - Founder, Chairman, and CEO*

(Chinese language spoken)

Dennis Yang - *Tarena International Incorporated - Chief Financial Officer*

So let me translate the question and answer.

The first question goes to ask about the reason why the G&A expenses increased greater than the revenue growth.

The reason why the G&A expenses growth increased is because the increased number of our general and administrative personnel in software development team and finance team and work -- the workflow optimization team. We equipped those talents in our team to help us to improve our operational efficiency and we [inaudible] we believe this kind of internal system and workflow can support our bigger -- a greater business scale in the future.

And the second question is actually about the total student enrollment forecast for the whole year.

So in 2016, the student enrollment we target to increase by 25% year over year to more -- to about -- sorry, 105,000.

Operator

(Operator Instructions)



Ladies and gentlemen, that will conclude today's question-and-answer session. I will now refer the call to Helen Song, Tarena's Senior Investor Relations Manager.

Helen Song - *Tarena International Incorporated - Senior Investor Relations Manager*

Thank you, operator. If there are no further questions at present, we'd like to conclude by thanking everyone for joining us on the call. We welcome you to reach out to us directly by emailing ir@tedu.cn if you have any questions or requests for additional information. I encourage you to visit our Investor Relations site at ir.tedu.cn.

This concludes Tarena's earnings conference call. Thank you.

Operator

That does conclude today's conference call. Thank you, ladies and gentlemen. You may now disconnect.

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