

# FINAL TRANSCRIPT

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**CEDU - Q1 2010 CHINAEDU CORP Earnings Conference Call**

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## CORPORATE PARTICIPANTS

**Jimmy Xia**

*ChinaEdu Corporation - IR Manager*

**Julia Huang**

*ChinaEdu Corporation - Chairman and CEO*

**Shawn Ding**

*ChinaEdu Corporation - President and COO*

**Lily Liu**

*ChinaEdu Corporation - CFO*

## CONFERENCE CALL PARTICIPANTS

**Jeff Lee**

*Signal Hill Group - Analyst*

## PRESENTATION

**Operator**

Welcome to the ChinaEdu first quarter 2010 financial results conference call. At this time, all participants are in listen-only mode. Following management's prepared remarks, we'll hold the Q&A session. (Operator Instructions). As a reminder, this conference is being recorded, May 25, 2010.

I would now like to turn the conference over to ChinaEdu's Investor Relations Manager, Mr. Jimmy Xia. Please go ahead, sir.

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**Jimmy Xia** - *ChinaEdu Corporation - IR Manager*

Thank you. Good morning and good evening, ladies and gentlemen. Thank you for participating in today's call. Joining me today are Ms. Julia Huang, Chairman and CEO; Mr. Shawn Ding, President and COO; and Ms. Lily Liu, CFO.

After the close of the US markets on Monday, ChinaEdu issued a press release announcing its first quarter of 2010 financial results, which is available on the Company's IR web page at [ir.chinaedu.net](http://ir.chinaedu.net).

This call is also being broadcasted live over the Internet. And a copy of the presentation that will be used for today's call is also available under the quarterly results page on the Company's IR website.

Before the management's presentation, I would like to refer to the safe harbor statement in connection with today's conference call. This call may contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 including certain plans, expectations, goals and projections, which are subject to numerous assumptions, risks and uncertainties.

Forward-looking statements involve known and unknown risks, uncertainties, and contingencies, many of which are beyond our control, which may cause actual results, level of activity, performance, or achievements to differ materially from any future results, level of activity, performance, or achievement expressed, or implied by such forward-looking statements.

The Company's actual results could differ materially from those contained in the forward-looking statement due to a number of factors, including those described under the heading risk factors in the Company's annual report on Form 20F for the year-ended December 31, 2008, filed with the Securities and Exchange Commission, and in documents subsequently filed by the Company from time-to-time with the SEC.

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Unless required by law, the Company undertakes no obligation to update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

I would also like to note that the reporting currency of the Company is in RMB. But for the convenience of the reader, the amounts are presented in US dollars. All translations from RMB to US dollar were made at the rate of RMB6.8258 to \$1; the noon buying rate in effect on March 31, 2010, and the H.10 statistical release of the Federal Reserve Board.

All percentages are calculated using the numbers presented in the financial statement contained in the earnings release presented in RMB. We make no representation that RMB or US dollar amounts referred could be converted into US dollar or RMB, or any particular rate, or at all.

I would now like to turn the call over to our Chairman and CEO, Ms. Julia Huang. Following our prepared remarks, we will be happy to take your questions. Julia?

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**Julia Huang** - *ChinaEdu Corporation - Chairman and CEO*

Thank you, Jimmy. Good morning and good evening. Thank you, again, for joining us for today's call. During the first quarter of 2010, ChinaEdu's net revenue was in line with management guidance and [EPS] consensus.

Online education remains the core focus of the management team. We have made additional progress in the first quarter through the expansion of our learning center network. Our 101 Online school has continued to improve the results channel of concentration and product offerings.

Now, let's look at some of our key items for the first quarter, on slide five. Our net revenue in the first quarter of 2010 grew by 7.5% to \$12.8 million, compared with \$11.9 million in the corresponding period of 2009, which was driven by 140,000 revenue students.

Our gross profit increased 15% to \$8.2 million, compared to \$7.1 million in Q1 2009. Gross margin improved from 60% to 64%.

Operating income increased 11% to \$2.9 million from \$2.6 million in Q1 2009. And our operating margin improved slightly to 22%.

Our adjusted EBITDA increased to \$4 million in the first quarter of 2010, compared to \$3.7 million in the same period of 2009. And our adjusted EBITDA margin remained steady at 32% in the period.

And our earnings per diluted ADS was \$0.06 in the quarter, and beating analyst consensus.

Now, let's turn to Shawn Ding, our President and COO, for business and operational highlights; followed by Lily Liu, our CFO, for more financial highlights. Shawn?

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**Shawn Ding** - *ChinaEdu Corporation - President and COO*

Thank you, Julia. Ladies and gentlemen, thank you for joining us today. During the first quarter, ChinaEdu continued to progress well through organic growth, as well as the development of our online education and online degree initiatives.

Let's take a look at our slide six. As mentioned on our last call, we signed Huazhong Normal University to an exclusive technology and service contract. Huazhong is within the 68 universities that has the online degree licenses.



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We also signed an exclusive collaborative alliances contract with Jiangxi Normal University to support its adult education college prior it getting approval from the Ministry for Education for its online degree programs.

For our learning center network, by the end of the first quarter we are working with the 17 universities through our 62 learning centers; 24 proprietary and 38 franchised. We are in the process of acquiring a few independent learning centers and we should complete the process soon.

For non-degree programs, or non-degree continuous education programs, we signed a software license and professional service agreement with CTB McGraw-Hill to develop an online language proficiency exam. We hope this is the first of many partnerships between ChinaEdu and McGraw-Hill companies.

We signed a professional development program with Harvard Graduate School of Education's WIDE World online education curriculum. And we have also started to develop an online training program for K-12 teachers. In the US terms, it's teacher training.

In this quarter, we continue to invest in research and development for the long-term success of our core business.

On page seven, we continue to see great progress in our 101 Online Tutoring business. In this quarter, we have seen very good expansion of sales channels, with particular emphasis in our home market of Beijing.

We also continued the development of our tutoring products and increased the level of services. Our hybrid learning model of both online and in-person training tutoring is still in early stage, and we have seen traction for expansion in the future. Having created a separate team for 101tutor.com, this site has gained popularity with more than 300,000 daily page views.

As for our Private School business, the Anqing School has benefited from enrollment growth, as expected.

Our International Curriculum program has partnered up with foreign universities for exchange programs. Hopefully, we should see some turnaround with that program this year.

For the rest of 2010, our online education will continue to gain additional traction for the long-term growth of the Company.

Although we have not seen additional approval of online degree licenses, we're doing everything we can to prepare for the eventual approval. We're signing additional contracts for both degree and non-degree offerings to prepare for our future growth.

I would now like to turn over to Lily for a review of the key financial information for the quarter. Lily?

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**Lily Liu** - ChinaEdu Corporation - CFO

Thank you, Shawn. Let us now go through our first quarter financial results. Before I dive into the numbers, let's first take a look at our revenue mix in the first quarter compared to last year.

Our total net revenue grew by 7.5% in the first quarter to \$12.8 million compared to the first quarter of 2009. We continued to experience high growth in our learning centers, Online Tutoring, and Private School sector.

As a result, contribution from Online Tutoring grew to 6%; for Private Schools to 11%; and Online Degree programs' revenue contribution as a consequence decreased to 78%, from 81% in the first quarter of 2009.

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Our core Online Degree programs segment recorded a total net revenue of \$10 million, which represents a growth of 4.2% compared to the first quarter of 2009. The revenue is mostly a result of recognition of student tuition collected in the fall of 2009.

Our fall enrollments in 2009 recorded a healthy growth of 18.6% compared to the fall of 2008. As of end of 2009 fall semester, we are serving a total of 287,000 revenue students.

We are pleased to report that our learning centers continue to expand as planned, as mentioned by Shawn. As of quarter-end, we have a total of 62 learning centers, of which 24 were proprietary and 38 were contracted.

Now let's also take a look at our other business segments. As mentioned earlier, our 101 Online Tutoring and Private Schools continue to register strong growth. 101 Online Tutoring grew by 50% in the first quarter compared to last year, and Private Schools' net revenue grew by 49%. International Curriculum's net revenue declined by 27%, which is in line with the management's expectation.

We're very pleased with the continued execution of 101 Online Tutoring business, product development, customer service improvement, further sales penetration, and more efficient management of third party distribution are all under way.

Let's now also review this quarter's gross margins. Our total cost of revenue decreased slightly by 4% in the first quarter of 2010 compared to last year. And as a result, our gross margin expanded to 64% this quarter, compared to 60% in the first quarter of last year.

Both of our core business segments', Online Degree programs and 101 Online Tutoring, gross margins experienced improvement. Online Degree programs' cost of revenue decreased due to a decrease in special courseware development costs at selected online colleges.

Gross margins for learning centers, which is part of Online Degree programs, also experienced significant growth compared to last year, which contributed to our Online Degree programs' total gross margin expanding from 66% last year to 69% this quarter.

In this quarter, 101 Online Tutoring's cost of revenue also decreased compared to last year, resulting in gross margin expansion from 60% last year to 78% this quarter.

In addition, our Private Schools, in particular, our Anqing School, gross margin continues to improve. Gross margin was 28% this quarter, compared to 12% in the first quarter of last year.

International Curriculum's cost of revenue decreased by 37%. Gross margin remains very solid at 41%, though it is a decrease compared to 47% in the first quarter of last year.

Now let's review the operating expense line. First, our general and admin expenses remained stable, with only a 2% increase compared to the first quarter of last year. G&A expenses as a percent of net revenue were 23% this quarter compared to 24% last year.

Although G&A expenses will likely incur normal increases as the Company grows, we believe we have normalized our expense structure and G&A expense as a percent of revenue will remain relatively stable in the future.

Let's now move on to sales and marketing expenses. As we discussed at the end of last year, in 2009, our overall sales and marketing expenses, and as a percent of net revenue, decreased compared to 2008 upon streamlining our sales and marketing efforts at several subsidiaries as, well as a one-time impact from decreasing intangible amortization. This year, our sales and marketing expenses will increase compared to 2009.



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G&A expenses in this quarter increased by 58% to \$1.1 million, which represents 9% of our total net revenue and it's a comparable level to our 2008.

This year, we will also continue to increase our sales and marketing efforts at our 101 Online Tutoring, Online Degree programs, as well as the learning centers.

Lastly, let's review our R&D expenses. Research and development expenses increased by 33% in the first quarter compared to last year. R&D expenses represent 10% of our total net revenue in the first quarter.

This year, we're committed to further developments of our technology platform for the online degree programs, various non-degree programs, as well as 101 online schools. Also, as we discussed since last year, we have established teams to develop our K-12 online learning platform and adult learning community with the Internet and mobile applications.

We are confident that the Company's research and development efforts will position us to capture future growth across different areas of online education.

Now let me summarize our operating results. For the first quarter of 2010, our GAAP operating margin increased slightly from 21.6% to 22.3%. Both adjusted EBITDA margin and adjusted operating margin remained relatively stable at 32% and 26% respectively.

Online Degree programs remains our most profitable segment. And our fast growing businesses, learning centers, 101 Online Tutoring, and Private Schools' profitability will continue to experience growth.

Finally, let's take a look at our net income and EPS. Our net income decreased in the quarter compared to the first quarter last year due to an increased deferred tax expense at one of our JVs. This JV's current preferential tax rate will expire in 2011, resulting in calculation of its deferred taxes, using 25% as statutory tax rate rather than its current 12.5% preferential tax rate.

The JV is in the process of applying for the high and new tech enterprise status, which we expect to receive by the year's end. At that point, we expect a one-time tax expense reversal will occur. As a result, our net margin was 8.3% for the quarter, compared to 11.8% last year.

If we exclude the impact of increased deferred tax expense, our net margin would be on par with the first quarter net margin in the last year.

Lastly, let me also quickly summarize our balance sheet. Our balance sheet remains very strong. Our cash, term deposits, and available-for-sale investments totaled \$52 million, compared to approximately \$49.5 million as of end of last quarter.

On a per diluted ADS basis, our cash represents roughly \$3 per share. If we also consider the book value of our headquarter real estate and our portion of the book value of JVs' real estate, together with cash, it amounts to \$4.8 per diluted ADS.

Finally, before we conclude our presentation, I'd like to reiterate our net revenue guidance for the second quarter of 2010. Our current estimate is between RMB91 million and RMB97 million, or roughly translates to \$13.3 million to \$14.2 million. This forecast reflects our current view and may be subject to change.

This concludes our presentation, and we're now open for further questions. Thank you.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions). Your first question comes from the line of Jeff Lee from Signal Hill. Please proceed.

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### Jeff Lee - Signal Hill Group - Analyst

Thank you. Good evening. First question. For the last several quarters, enrolment growth has greatly exceeded online revenue growth but this quarter the gap is getting even wider; can you talk about what's driving that?

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### Lily Liu - ChinaEdu Corporation - CFO

Sure. Normally, our student enrolment growth will exceed our revenue growth, and we have explained that previously. And this quarter, the gap is even greater because there were a couple of one-time expenses at the online college level. Generally, our revenue is tuition deducting the third party learning centers' expense, as well as specific expenses at online colleges.

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### Jeff Lee - Signal Hill Group - Analyst

Okay, that's helpful. And what are your expectations then going forward for Online Degree revenue growth for the rest of the year? Should we expect the revenue growth to be [slightly] faster than in future quarters if you don't have one-time expenses?

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### Lily Liu - ChinaEdu Corporation - CFO

Going forward, we don't expect the one-time expenses will reoccur. Going forward, for this year, we do expect our Online Degree programs' revenue to be generally in the single-digit range.

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### Jeff Lee - Signal Hill Group - Analyst

Okay, great. You mentioned the 101 Online has a hybrid program. I was wondering if you could talk about what you've learned so far from that and what plans, if any plans, you have to expand it?

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### Julia Huang - ChinaEdu Corporation - Chairman and CEO

Jeff, this is Julia. This year, we are having hybrid classes in Beijing trial, and so far we have -- getting a good turnaround when we had the programs. Historically, or previously, we have a one-year program [tracked] for 2,900 per person in Beijing, so this year we are having 6,000 and 9,000 packages, which combine the online programs and offline, 101 Tutoring, and the small class -- small group classes.

So far, we have been -- in the past two or three months trial, we had small group trials. We have seen good turnaround; that students are willing to pay the higher fees given that we're providing more services to them.

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### Jeff Lee - Signal Hill Group - Analyst

Okay, great. [I was looking] also for more details on the status of the international curriculum program, so where it's at and when do you expect the declines in revenues to stop?



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**Julia Huang** - ChinaEdu Corporation - Chairman and CEO

Jeff, right now, this year, we are also starting to have another program, which is what we call the going abroad English training program for high school graduates who are [waiting] to go abroad. So, we're going to have a nine-month English program through our joint effort with China Agricultural University, one of our partners, and also China University for Law and Justice.

So, jointly, we're going to have a program which students are going to prepare for culture and exams before they go abroad to study so this year we are still going to see the decline. But next year, we're going to -- we're expecting that going abroad English training with pick up the sales instead to see the declining for this program.

**Jeff Lee** - Signal Hill Group - Analyst

Okay, great. And last question, learning centers. It looks like you've slowed down the pace of learning center openings recently; how many learning centers are you planning to open during 2010? And then, just what sort of overall contribution are you expecting your learning centers to make in 2010?

**Lily Liu** - ChinaEdu Corporation - CFO

Jeff, we are still on target to have roughly 80 to 100 learning centers by the year's end.

**Julia Huang** - ChinaEdu Corporation - Chairman and CEO

Okay, thank you.

**Operator**

(Operator Instructions). At this time, there are no further questions. I would like to turn the call over to management for closing remarks.

**Julia Huang** - ChinaEdu Corporation - Chairman and CEO

Ladies and gentlemen, thank you, again, for participating in ChinaEdu's first quarter 2010 earning call. I would like to reiterate how much we appreciate your interest and support.

Our management team feels very confident in the future of our industry and our Company in China education market. We are committed to continually grow our online education business through degree programs, training programs, and online learning initiatives.

We also increase research and development efforts of our technology platforms, Internet, and the mobile applications for the online degree and non-degree program, including our interactive online learning community for both K-12 students and adult learners in 2010, while we continue to maintain our tight control over our expenses.

We feel that ChinaEdu will be able to bring such benefit to our students, society, and ultimately our shareholders. Overall, we believe our Company is positioned strongly to capture the immense potential that online education can offer in the future.

Thank you for your time, and have a good day or good night.





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**Operator**

Ladies and gentlemen, that concludes today's conference. Thank you for your participation. You may now disconnect. Have a great day.

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