
Cloud Music Inc. First Half 2024 Earnings Conference Call

7:00 PM Hong Kong Time, August 22, 2024

Hello, everyone, and welcome to our first half of 2024 earnings conference call.

In the first half of 2024, we propelled quality development across our music-centric ecosystem by prioritising our core music business and fostering a thriving community. This strategy considerably boosted user appeal and engagement during the period, ultimately improving our monetisation capabilities in our core online music business. Our success stems from our ongoing efforts to enrich content, innovate features, enhance service experiences and foster deeper community engagement. In particular, the recent comprehensive upgrade to the NetEase Cloud Music App enhanced our unique listening experience, further intensifying our community culture and deepening user engagement. Our efforts to strengthening our music-oriented monetisation capabilities has also continued to yield positive results. As a result, we delivered solid growth in our subscription-based memberships and drove monetisation momentum in our core online music business

We continued to **inject new energy into our music-inspired community during the period**. Our DAU/MAU ratio stayed consistently above 30%. Our fast-growing online music membership subscription base demonstrated higher stickiness, spending more time on our platform with higher activity levels than non-paying users. Product-wise, our unique music-inspired community and personalised content recommendation feature stood out as our most important differentiators. Our recent app upgrade also improved users' music discovery capabilities with more personalised recommendations and innovative features for a more premium listening experience. Additionally, we continued to cultivate our community centred around our iconic Comments section, leading to more community content generation and consumption, as well as increased user interactions in a lively community atmosphere. These initiatives improved our user engagement metrics, including users' average listening time on our mobile app.

In terms of content, we have created a **differentiated content ecosystem** that encourages users' active participation and subscriptions. During the first half of the year, we continually enriched our content matrix to cater to diverse user needs. Additions to our copyrighted content library, such as Korean music labels like JYP Entertainment and Kakao Entertainment, further cement our growing body of K-pop tracks. Meanwhile, we increased support for independent musicians and enhanced our in-house music production capabilities. We strategically scaled up our catalogue in signature music genres like hip-hop through a mix of collaborations on copyrighted content and original music, consistently delighting music lovers with high-quality music works.

Meanwhile, we worked diligently to **strengthen our music-centric monetisation capabilities** and delivered solid online music revenue growth in the first half of 2024. Our online music business subscription revenue increased by approximately 25% year-over-year, mainly driven by a increase in subscription memberships. We continued to refine our premium offerings, including content optimisations and innovative features, garnering widespread acclaim from users. We also actively broadened membership privileges and joint programs with external

partners, driving user enthusiasm for subscribing to our premium content and services. Notably, membership retention rates, time spent and activity all improved.

In addition to increased subscriptions, we strengthened our advertising commercialisation capabilities during the period, harnessing our enhanced operating efficiency and optimised algorithms for performance-based ads, as well as more diverse advertising formats and initiatives, leading to an increase in advertisers' spending on our platform.

Our **profitability improvements** in the first half of the year were led by our growth and the increasing benefits of economies of scale. This was mainly the result of strong monetisation in our core online music business, where we continue to gain operating leverage .

Going forward, our strategic approach places us on course for our sustainable business development over the long term. We will remain committed to strengthening and deepening our unique music and community ecosystem. Our strategic blueprint calls for bringing more original, high-quality music to our platform, innovating products and services for our users, cultivating our music community and enhancing user experience.

With that overview, let me walk you through some of our accomplishments in the first half of the year in more detail. I'll then review our specific plans for each of our go-forward initiatives, including our content ecosystem, product innovation and community and commercialisation.

First off, our differentiated **content ecosystem**.

We continually enriched and updated our content library across both copyrighted music and self-produced music to meet the evolving needs of our users, particularly younger users who have varied tastes and a desire to discover new music. We are especially focused on promoting signature music genres, like hip-hop.

First, let's take a look at our copyright partnerships. Throughout the period, we remained dedicated to fostering partnerships and deepening our collaborations with music copyright holders, particularly by rounding out our Korean music content library.

We expanded our catalogue of music labels during the first half of 2024 via new partnerships with major Korean labels, including JYP Entertainment and Kakao Entertainment, as well as Chinese music labels such as KC DIGITAL and 果然娱乐. We added high-quality songs from a host of musicians, singers and groups. We also successfully renewed our copyright partnership agreements with Korean music labels SM, YG and CUBE.

We have also focused on signature music genres to create unique content experiences, like hip-hop, rock and Japanese ACG, which have surged in interest and popularity on our platform. We are offering users with early listening privileges to some content in our signature music genre, including selected news songs from rappers like KeyNG, VaVa, AIR and rock band Penicillin.

During the period, we also added J-Pop music from acclaimed Japanese music labels Vap Japan and B-zone, known for iconic anime OSTs like "Detective Conan," "Slam Dunk," and "Dragon Ball GT."

Our deepened collaborations with copyright holders and artists yielded impressive premium digital and physical album sales on our platform. For example, we created and launched an innovative, exclusive tab page for Taylor Swift's new album, "THE TORTURED POETS DEPARTMENT: THE ANTHOLOGY," successfully promoting its sales. The hit album achieved over 100 million streams in just 19 days after its release. For physical albums, we extended our collaborative efforts with copyright holders to optimise content distribution and commercialisation. For instance, Shi Kai's album "Counting Stars All Night" has achieved over RMB 10 million in sales on our platform.

With the revival of music-centric entertainment and the booming development of the music sector, we secured a series of copyrights for trendy music variety shows, propelling music content consumption and user activity on our platform with additions such as "The Rap of China 2024" (《中国新说唱2024》), "Singer 2024" (《我是歌手2024》) and "The Treasured Voice 5" (《天赐的声音5》). Notably, "The Rap of China 2024" accumulated over 100 million plays on our platform, delivering a strong streaming performance and receiving widespread positive feedback from hip-hop fans.

Looking at our independent artist ecosystem, as of June 2024, our platform had over 732,000 registered independent artists who contributed around 3.6 million music tracks to our library. We remain committed to supporting independent artists throughout their music industry journey, investing in initiatives that bolster musicians' productivity, improve music creation tools, expand online and offline music exposure and achieve commercialisation. These efforts ultimately strengthened our platform's original music ecosystem and unique value proposition.

In terms of *content creation*, we upgraded our content creation support by leveraging AI technology and made our all-in-one AI music creation tool, NetEase Tianyin, accessible to both independent musicians and individual users across our platform. This improved the efficiency of music production and streamlined musicians' workflow while empowering more music lovers to emerge as novel musicians. For NetEase Cloud Music X Studio, our AI-based voice synthesis software, developed in partnership with Xiaoice, we integrated top-tier IP Luo Tianyi and introduced five new natural singing voices, including ethnic and bel canto singing styles, enabling musicians to easily find the right voice for their unique projects and helping them effectively express their creative ideas. We also organised music communication and co-working camps to bring emerging music talent together for collaborative music creation. Additionally, we partnered with Mingtang Records for a recent camp and launched a joint camp with Yunshang Studio, themed "Untamed Force," where renowned musicians conducted masterclasses and offered guidance to aspiring artists, elevating the music creation process for premium music works.

Increasing the discovery and exposure of musicians and their work is another way we add value to the music industry and our artists. Through special events, targeted operations and location-based initiatives, we maximised our internal and external resources to boost the visibility of musicians and their high-quality work, adding value to the music creation industry.

In the first half of 2024, we created a host of localised events promoting local content and musicians, both online and offline, across diverse locations. These initiatives included our renowned city tour guide special planning series (城市云游指南), where we released a Northeast Special Edition and launched an online-plus-offline event in Guizhou. Additionally, we joined hands with the CCTV program "Music on the Journey" to showcase local original musicians on the CCTV stage, increasing their exposure and influence across a broader audience.

Meanwhile, we actively offered emerging musicians diverse channels to reach their audience. During the period, we officially launched Live Cover, an innovative feature within our online app's music player interface that provides musicians with a new channel for promoting their music content and their artist personas. We also continued our city flash mob activities under Project Cornerstone (石头计划) to provide musicians with more offline performance and promotion opportunities, and the first stop was in Jiaxing in May.

In addition, We actively empowered musicians with tools to make money from their work. Our platform's diverse monetisation approaches and upgraded support initiatives are designed to help musicians maximise their financial value, promoting favourable conditions that allow them to focus on music creation.

Last year, we launched "Project Cloud Ladder 2023." Under this program, more than 100,000 musicians increased their earnings through cash incentives, and over 50% of musicians grew their income. In April 2024, we rolled out the latest phase of our renowned musician support project, "Project Cloud Ladder 2024" (云梯计划 2024 第一期), which further bolsters financial backing for musician groups by offering a more attractive financial settlement mechanism. We also broadened the scope of incentives for musicians by introducing advertising revenue sharing, further diversifying the potential income streams of musicians.

Moreover, we continuously solidified our support for musicians of distinct backgrounds. To further support arrangers and other behind-the-scenes talent, we recently implemented the second phase of a revenue-sharing program for music arrangers, providing financial aid through royalties for both arrangers and BeatMakers. Meanwhile, our latest "Project Cloud Ladder 2024" added a "discretionary royalties for arranger" feature. These types of initiatives show how we are working to assist a wider variety of musicians in their music creation and career development, bolstering quality music production industry-wide.

Finally, we consistently strengthened our production capabilities. Drawing on our musical expertise and in-depth user insights, our multiple in-house studios continued to make strides in music production featuring distinct styles, creating unique music content that meets the diverse needs of various audiences.

While we are dedicated to crafting high-quality music content across a variety of genres, we particularly focus on our most signature genres. In the first half of 2024, our in-house studios successfully produced and popularised multiple hit songs, represented by 《紫荆花盛开》. We have also produced a number of popular hip-hop song tracks, including a Henan Dialect rap song, "5:20 AM" (《5:20 AM》), "Xie Tian Xie Di"(《谢天谢帝》), "Ren Shang Ren" (《人上人》) and “Hai Shi Hui Xiang Ni” (《还是会想你》). Additionally, we successfully facilitated new album releases of renowned and fresh rap talent like 谢帝、功夫胖、GALI、李大奔、王齐铭、and 沧桑.

Our in-house studio also produced the farewell-themed instrumental song, "Farewell Letter," featuring a stark contrast between upbeat melodies and melancholic tones. The song has gained popularity both within and outside the instrumental music community. We also invited mainstream artists like Joey Yung, Zhao Lusi and Amy Chen Haoyu to cover and reinterpret songs like "Tong Hua Zhen (《童话镇》)," "You Ni De Kuai Le 《有你的快乐》" and "Gu Ge Xie Mu 《骨骼谢幕》," breathing fresh new appeal into these classic works.

Moreover, our recently launched hit original track “Dehors” featured a ground-breaking cross-continental collaboration between Chinese and French artists. Performed in both Cantonese and French, it has sparked a unique and distinctive chemistry. This international crossover collaboration captured the attention of diverse audience segments, fostering deeper interaction and cultural exchange among musicians.

The quality of our in-house music is increasing, gaining exposure and popularity across offline location-based initiatives nationwide and online TV shows in China, including the CCTV 2024 Spring Festival Gala (央视春晚), Henan TV's 2024 Lantern Festival Gala (河南卫视元宵晚会), Henan TV's May 1st Gala (河南卫视五一晚会) and Beijing TV's New Year's Eve Special (北京卫视跨年之夜), as well as popular variety shows like "Singing With Legends S5 (《我们的歌5》)" and "Yi Lu Qian Xing (《一路前行》)" on Dragon TV and "Come Sing with Me (《我想和你唱》)" on Hunan TV.

We are consistently expanding our offline public broadcasting collaborations to build on this success, focusing on brands and scenarios that appeal to young users. For instance, in the first half of 2024, we partnered with commercial brands specialising in offline operations, including Wanda Plaza, Blueglass Yogurt, Manner Coffee and the Wandang micro department store. These initiatives covered a total of nearly 6,000 stores, all aimed at promoting our in-house music and increasing brand awareness among students and white-collar demographics.

Beyond music, we actively amplified our **other audio-based content offerings**, including diverse PUGC, UGC and PUGC. Our goal is to create a comprehensive listening experience for our users, ultimately increasing user engagement and tapping into more commercialisation opportunities. Our continually enriched long-form audio content effectively elevated the stickiness and spending of long-form audio users. In the first half of 2024, the average listening

time per long-form audio user on our platform increased by a significant 49% on year-over-year basis.

Podcasts are an essential part of our content ecosystem. Our podcasts focus on music-inspired content, offering music fans rich and personalised music discovery and consumption experiences. Moreover, we have been enriching our PGC library, including audiobooks and radio dramas, with a particular focus on increasing our pool of self-produced long-form audio content. This has proven to be an effective strategy in attracting new users and increasing user engagement and consumption on our platform. For instance, our original radio drama, adapted from the popular Chinese anime of the same name, "Villain Wants to Save (《恶人想要抢救一下》)," resonated with young users on our platform.

Product innovation and community ecosystem

Moving on to our products and community.

Throughout the first half of 2024, we continued innovating products, enhancing features and reinvigorating our differentiated community. These efforts resulted in strong and sustained user engagement levels. Our comprehensive NetEase Cloud Music App upgrade, which started in early 2024, marks a significant step forward in product innovation. The upgrade focuses on several key areas: enhancing personalised content recommendations, improving traffic allocation, and actively fostering our music-centric community centred around music comments.

【 Optimising user discovery and consumption experience 】 First off, we have always been committed to providing users with the best possible music discovery and consumption experience.

- Our app optimisation has had a big impact. It boasts a better framework, improves our *content distribution* methodology and brings users more optimised content recommendation features through daily recommendations, Private DJ and heartbeat mode. This has amplified the efficiency and coverage of our content recommendations, resulting in a holistically more personalised music discovery experience for our users.
- We also optimised our *classic vinyl playback experience*, which improved user stickiness. We continue to optimise music-inspired consumption with upgrades to the encyclopaedia and the lyrics consumption experience. We also released 14 new music player interface series, including full-screen cover, Forbidden City style, music comment style, Artist series, IP-themed players in collaboration with NetEase Games and designer toys. These trendy IP-themed music players offer users a fresh experience while also generating revenue through subscription memberships and individual purchases.

【Fostering community attributes】 In addition, we continuously upgrade and innovate music community-oriented products and features to enhance our users' connections with music. **Our**

product upgrades and other initiatives focus on community resonance and interpersonal connections.

During the first half of 2024, we actively nurtured our unique music-inspired community attributes by amplifying the value of our iconic Comments section across various app scenarios. These efforts led to a better community experience for both users and UGC creators, which is crucial in maintaining and improving our strong user activity and stickiness.

- *[Community consumption and interaction.]* During the reporting period, we continuously amplified the value of comments through product, operational and algorithmic optimisations. To name a few, we featured hot comments on the vinyl player, introduced a new player interface and refined our comment distribution system. Additionally, we diversified the content on our "Moments Square (动态广场)" section by enhancing the distribution of high-quality comments and by enriching diverse formats of UGC content. These efforts increased community engagement with our content and user interactions.
- *[Community content generation.]* We also initiated efforts to increase user participation in creating UGC within our community during the period. For example, we enhanced operational activities by coordinating comments with new song releases and popular topics to engage users, prompting them to share thoughts and feelings in the Comments section. Additionally, we curated various operational activities in the "Moments Square (动态广场)" section centred around specific topics and simultaneously promoted innovative UGC content coverage. These initiatives have effectively increased the number of users publishing content and updates in the music cComments and Moments section .

[Music consumption scenarios expansion] Meanwhile, we **expanded music consumption and communicative scenarios**, deepening user engagement by embedding music into daily activities.

- For instance, we recently partnered with NetEase's education arm to fuse music consumption within Youdao Dictionary, bringing music to specific English word searches and offering users an integrated music experience.
- We also continued optimising omni-device functionality. Users can now easily switch between mobile, PC, TV and in-car scenarios, effectively addressing diverse user needs and improving user experience. Regular vinyl membership subscribers can now also access content on IoT terminals. These efforts help us improve overall user activity and engagement across multiple devices and scenarios.

Finally, let's delve into **our commercialisation.**

We strengthened our music-centric monetisation capabilities throughout the first half of 2024 and delivered solid growth momentum on a year-over-year basis across both subscription memberships and advertising, verifying the sustainability and potential of our business. By continuously optimising distinctive content and product experiences, deeply cultivating active communities, and actively expanding consumption scenarios, we have laid a solid foundation for our ongoing commercialisation.

Growth in our revenue from *subscription-based memberships* accelerated during the period, rising by 25% year over year, based on an increased number of subscribers. In terms of membership expansion, we boosted user willingness to pay for premium privileges through enhanced premium content offerings, continued product innovation, broadened membership privileges, joint membership programmes and innovative marketing activities.

In terms of **membership privileges**, we introduced multiple new functions and privileges covering listening experience and interaction features, and launched a series of player interfaces.

- In terms of *product functionality innovation*, we recently launched Ear Age/Ear Pattern Sound Effects (个性化耳龄音效) and Music review/lyrics landing image (乐评/歌词启动图), and 红心动效 brought members an upgraded and personalised listening experience. Notably, our Ear Age Sound Effects automatically adjusts sound quality based on users' age to enhance audio accuracy, providing a superior experience for users of all ages. Furthermore, we introduced a new feature for members called Bestie Space (双人关系), attracting new members and enhancing user activity levels and stickiness.
- For premium users, we also released several new *themed music player interface series* and updated the Decoration Center. For instance, we entered into co-branding initiatives with the popular toy brand Farmer Bob, offering fashionable IP-themed music players that delighted young users, driving an increase in subscription memberships and individual player purchases. These trendy IP-themed music players opened up monetisation opportunities through both subscription memberships and individual purchases. We continuously innovate the player interface, such as the new player style co-branded with *Eggy Party*, encouraging users to hatch new Eggy characters by listening to music, offering them the fun of developing IP. Additionally, for artist promotional events, we have introduced a series of customisation perks for fans, including profile widgets, landing images, and player interfaces for artists like JYP and Taylor Swift.

On the collaboration front, we are actively exploring and creating a new collaboration model for our membership programme with both internal and external partners. We re-launched joint programs with NetEase Games, including *Eggy Party* during Chinese New Year, catering to music and game enthusiasts. We also expanded our external partnerships by establishing joint membership programmes. In addition to collaboration with various online video platforms, we expanded our presence into other internet service platforms and offline scenarios, such as Vipshop, Zhihu, Tongcheng, Youdao Dictionary and Atour hotels, to specifically target students and white-collar workers.

For subscription memberships, we aim to continue driving solid revenue growth by leveraging enhanced content and functions, broadening membership privileges and expanding consumption scenarios for our online music subscribers. We have made online music membership benefits more accessible by offering special promotions for student subscribers and graduation special activities. We are confident that by increasing the number of users enjoying premium privileges on our platform, especially younger generation users, we can attracting more high-quality active and paying users, driving long-term growth in scale and commercial development.

In addition to subscription memberships, we strengthened our *advertising commercialisation capabilities* during the period, supported by improved performance-based ads, as well as more diverse advertisement formats and initiatives.

Performance-based advertising has become a key driver of our ad revenue growth due to optimised audience targeting algorithms and enhanced operational efficiency. In the first half of 2024, our exploration of ad-supported models yielded promising results. Although still in its early stages, the ad-supported model has demonstrated both platform and commercial value.

For branding advertisements, we have been proactively exploring innovative ad formats that better align with our music community ecosystem. Alongside ongoing product innovation and upgrades, these efforts aim to enhance our appeal to brand advertisers. Recently, we launched our first AI-powered ad campaign, the AI Cover project, for 简醇 Yogurt, offering a distinctive advertising experience driven by our AI technology and music ecosystem.

In conclusion, we will proactively explore diversified avenues to unlock greater commercial potential. In addition to driving stable growth in our membership subscription model, we remain committed to exploring additional monetisation initiatives. We believe that continuously nurturing and deepening our music-centric community ecosystem will lay a solid foundation for our future monetisation.

Q&A

Q1: How will a macroeconomic slowdown affect subscriber net additions and ARPPU? Does this suggest that the subscription business is somewhat resistant to changes in the macroeconomy?

William Ding: So far, the macroeconomic decline has not significantly affected our business because our ARPPU is not typically high. In our industry, it works somewhat conversely. During an economic downturn, more people may choose to listen to music at home, so it is more typical for the NetEase Cloud Music platform to see rapid membership growth under those conditions.

Q2: What is the higher priority target this year – MAUs or subscriber growth?

William Ding: We need to focus on increasing MAUs first because that's key to growing subscribers. So, MAUs are still our top priority.

Q3: The paying ratio has been increasing in the online music industry, what are your primary strategies for converting users to paying customers?

William Ding: Our main pathway to convert paying users is through our dedicated focus on offering unique content.

Q4: How does management balance the subscriber base and ARPPU? Can management also share the medium- to long-term goals in this regard?

William Ding: We aren't going to share any specific targets at the moment, but we know what needs to be done and how to do it.

Q5: How is the independent musician ecosystem developing on the platform, and what is their contribution to streaming volume?

William Ding: Independent musicians are critical for us. Since our inception, our goal has been to nurture and promote independent musicians, developing and advancing original music in China. This was our primary motivation for launching the NetEase Cloud Music app. After 12 years of development, we can see a growing number of independent musicians emerging and improving their works. Independent artists' music streaming volume on our platform fluctuates based on the quality of their content, with more plays for good works and fewer for less engaging content. We are pleased to provide additional resources to support the career development of these artists.

Q6: Is there room for further price increases in the future, especially since competitors have adjusted their pricing strategies recently?

William Ding: I believe that people are willing to pay for unique content. In the current macro environment, we prefer to maintain reasonable ARPPU. We cannot run NetEase Cloud Music solely for profit, as it goes against our original intention. Therefore, we are committed to supporting original musicians and promoting original music in China. With our continuous exploration and hard work, we are confident that we can continue to cultivate high-quality

content on our platform - that is our primary goal. Any monetization model is based on unique, high-quality content rather than focusing on current ARPPU, which lacks significance.

Q7: How has 88VIP contributed to the music business's growth? Can management provide insights on recent trends and future prospects?

William Ding: We and 88VIP will continue our important strategic partnership in the coming years. We have a mutually beneficial collaboration. The co-branded membership has expanded our user base and also provided additional benefits for 88VIP users. We are very willing to engage in these kinds of partnerships and work with more companies across different industries to jointly provide users with great music-listening experiences. While 88VIP contributes financially to our business, it is certainly not the main driving force.

Q8: What is the outlook for content costs, and how will it impact profitability?

William Ding: The cost of content is directly linked to its quantity and quality. So, an increase in costs also indicates enhancements to both the quantity and quality of content on our platform. We do not foresee a significant impact from content costs in the long term. We will focus on expanding new revenue sources, together with cost optimization, to improve profits.

Q9: The gross profit margin in the first half of the year was 35%, a significant increase from the previous period. What factors contributed to this growth, and what can be expected in terms of future improvement?

William Ding: Our gross profit margin has increased for many reasons. The main reason is our internal cost optimization measures. Second, our content cost management has become more efficient. We think that our current gross profit margin is at a relatively reasonable level. In the future, our goal is to expand our revenue streams.

Q10: Marketing expenses were relatively stable in the first half of the year. What channels and strategies do you primarily use to acquire customers?

William Ding: Over the past 12 years, NetEase Cloud Music has built a large fan base. A while ago, a lack of certain content caused some users to leave. We have been working diligently to bring more music back to the NetEase Cloud Music platform, which has been well-received by users, resulting in the return of some user who had previously used NetEase Cloud Music.