[TME] - Tencent Music Entertainment Group
Fourth Quarter 2019 and Full Year Earnings Conference Call
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Presentation

Operator: Ladies and gentlemen, good evening and good morning, and thank you for standing by. Welcome to the Tencent Music Entertainment Group 2019 Fourth Quarter and Full Year Earnings Conference Call.

Today, you will hear discussions from the management team of Tencent Music Entertainment Group, followed by a question-and-answer session. Please be advised that this conference is being recorded today.

Now I will turn the conference call over to your speaker host today, Ms. Millicent T. The floor is yours, ma'am.

Millicent T.: Thank you, operator. Hello, everyone, and thank you all for joining us on today's call. Tencent Music announced its quarterly financial results today after the market close. An earnings release is now available on our IR website at ir.tencentmusic.com, as well as via newswire services.

Today, you'll hear from Mr. Kar Shun Pang, our CEO, who will start the call with an overview of our recent achievements and our growth strategies. He will be followed by

Mr. Tony Yip, our CSO, who will offer more details on our operations and business developments. Lastly, Ms. Shirley Hu, our CFO, will address our financial results before we open the call for questions.

Before we proceed, please note that this call may contain forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are based on management's current expectations and observations that involve known and unknown risks, uncertainties and other factors not under the Company's control, which may cause actual results, performance or achievements of the Company to be materially different from the results, performance or expectations implied by these forward-looking statements.

All forward-looking statements are expressly qualified in their entirety by the cautionary statements, risk factors and details of the Company's filings with the SEC. The Company does not assume any obligation to revise or update any forward-looking statements as a result of new information, future events, changes in market conditions or otherwise, except as required by law.

Please also note that the Company will discuss non-IFRS measures today, which are more thoroughly explained and reconciled to the most comparable measures reported under the International Financial Reporting Standards in the Company's earnings release and filings with the SEC. You are reminded that such non-IFRS measures should not be viewed in isolation, or as an alternative to the equivalent IFRS measure, and other non-IFRS measures are not uniformly defined by all companies, including those in the same industry.

With that, I'm now very pleased to turn over the call to Mr. Kar Shun Pang, our CEO. Cussion?

Cussion Pang: Thank you, Millicent, and hello, everyone, and thank you for joining our call today. 2019 marked an important year for TME. We made significant contribution to upholding music copyright protection, supporting original content creation and designing innovative monetization models to unlock the intrinsic value of music, all of which are beneficial to the long-term sustainable growth of the industry.

Our strategic transition to pay-for-streaming service, continuous investment in premium self-produced and licensed content, product upgrades and technological enhancements have led to better user retention, attracting more subscribers, content creators, performers and users to our vibrant ecosystem.

One of the significant highlights is the accelerating year-over-year growth of our online music subscription revenues to 48% and 60% in the third and fourth of 2019, up from 26% and 32% in the first two quarters of 2019.

Online music paying users reached 39.9 million, growing 48% year-over-year with 4.5 million net adds, the largest net increase since 2016.

The paying ratio reached 6.2% during the fourth quarter of 2019, up significantly from 4.2% and 3.2% for the same quarter of 2018 and 2017 respectively, showing a recognizable trend of acceleration. Such a great outcome was primarily driven by continuous efforts to improve paying user retention and our effective content paywall strategy, as the proportion of our music streams behind the paywall expanded further.

Looking forward into 2020, our paywall content will be further enriched, and is expected to grow at a similar pace compared with 2019 as we add more genres, including those from big three music labels.

Another important highlight is our unique fan-based economy, which connects fan-to-fan and fan-to-idol, is gathering strong momentum. We have helped many artists, whether international, domestic, established or up-and-coming, promote their music and expand their fan base.

In 2019, we recorded an impressive high-double-digit year-over-year growth in the number of users buying digital albums. As a highlight, KUN's (Speaking Foreign Language) first personal digital album, YOUNG, sold more than 12 million copies on our platform by February 2020, breaking digital albums' sales record on a single platform with an absolute dominance, and setting a new milestone in the industry.

All of these achievements would have been impossible without the dedication of every single TME staff, and their passion to bring personalized, engaging and interactive music entertainment services to over 800 million monthly active users on our platform.

Our commitment to enriching content offering has continued to strengthen our content leadership. Not only do we offer the most comprehensive music library in China, but also expand to various forms of music-centric content, including more short-form videos, long-form audio, variety shows, and high-quality user-generated content on our platform.

For 2019, to cater to user demands, particularly for the younger demographic, we added more popular genres including J-Pop, K-Pop, Chinese Ancient style and ACG music to our library. We are also seeing further penetration of the younger demographic in 2019, especially generation Z, as a percentage of total online music users.

We continued to cooperate with producers of films, videos, games, variety shows, and literature, to co-produce high-quality original soundtracks to capture user demand. As example, in 2019, the digital album of The Tamed (Speaking Foreign Language), a web drama series produced by Tencent Video, broke the sales record of the domestic OST of films and drama series.

The theme song for the hit mobile game Honor of Kings (Speaking Foreign Language) was among the top rankings of multiple music charts. Our library now covers over 90% of OST for films and drama series, and all OST copyright of the most popular variety shows launched in 2019.

Additionally, in 2019, we were committed to nurturing and promoting original music content through our indie musician program. We are glad that more independent musicians have chosen to join our musician program in recognition of our strong promotional capabilities, industry reputation, copyright protection and better financial supports. For 2019, we are proud to say that through concerted promotion efforts, the number of users listening to our musicians' original content reached almost 1 billion.

Additionally, both the number of participating musicians and original songs created more than doubled year-over-year by January 2020. And streaming of these original works, as a proportion of all streams, also nearly doubled from a year ago, with even more explosive growth for our exclusive indie musicians.

Our stepped-up effort in supporting young and talented musicians has also yielded many successful cases. Our platform served as a powerful launching pad for Hai Lun, a male grassroot singer. The streaming volume of his original new song titled Girl by the Bridge (Speaking Foreign Language), became viral quickly after release, achieving over 1.1 billion streams on our platform as of February 2020, and attracting hundreds of KOLs to perform cover versions.

Under our musician program umbrella, in August 2019, we launched a unique program targeting young talents called Produce S. By leveraging our user insights and strong promotional capabilities, it produced many popular hit songs such as Almost Lover (Speaking Foreign Language) and The Boy I Missed (Speaking Foreign Language, and promoted high-potential young artists like Yongbin Ryan.B and Uu to become super rising stars.

With such encouraging results, in 2020, we plan for a strategic upgrade to take our indie musician program to the next level of development by offering more financial and operational support to independent musicians, in order to help them realize their dreams.

Another area that we have made important strides, and will expand more proactively, is long-form audio. Last year, we added rich categories including audiobooks, talk shows, and a diverse set of topics on history, romance, and humanity, etc. And we are pleased to see the proportion of long-form audio users on our platform grew at a healthy pace. An average long-form audio user's daily time spent was more than twice of that for an average user on our platform in December 2019.

In March 2020, we signed a 5-year strategic partnership with China Literature, the leading copyright owner of online literature in China, to expand aggressively to capture huge potentials within China's massive but under-penetrated long-form audio market. China enjoys the world's largest online audio user base, and according to iMedia Research, it is expected to reach over 600 million this year.

Through this strategic cooperation, we will have access to China Literature's broad online library and license to produce certain audiobooks. These audiobooks will be made available on both TME and China Literature's platforms, thus reaching a much broader audience. This cooperation allows us to significantly expand our long-form audio content library very quickly. At the same time, we will encourage the generation of premium UGC, and attract high-quality KOLs, further enriching our content ecosystem.

Based on experience of overseas online music platforms, the penetration ratio of long-form audio users, as a percentage of total monthly active users, could reach mid-teens, suggesting strong user base advantage and growth potential for TME. If we can achieve this penetration ratio, we will have the opportunity to become the number one long-form audio platform in China.

Furthermore, we expect to realize strong synergies between long-form audio and our existing services, and to not only improve user experience and increase the overall user engagement, but also further strengthen our content leadership.

We also advanced our leading industry position by forming strategic partnership with upstream music partners. In December 2019, we announced a proposal to acquire an equity interest in UMG, or Universal Music Group, the largest recorded music company and the second-largest music publishing company globally. As the music industry in China continues marching towards digitalization, we expect our strategic collaboration with UMG to strengthen our position to capture the extraordinary growth opportunity.

We will also leverage our user insights and promotional capabilities to promote music in UMG's vast content library, and bring more of their high-quality international artists to China market.

Overall, we are very pleased with the well-rounded progress that we have achieved during the past year, and there are many new opportunities that we are excited for year 2020. Through the development of indigenous programs, broadening our content categories and formats, deepening cooperation with more partners in the music entertainment industry, we strive to make our content ecosystem more differentiated and self-sustaining.

Lastly, I would like to touch on the recent coronavirus epidemic that has been challenging our nation and now around the world. Like every other company, our thoughts are with people who have been impacted by the outbreak. We have taken effective measures to make sure that our employees are safe for their health and wellbeing.

As a corporation with strong social responsibilities, we leveraged our Tencent Musician Program to help thousands of musicians originate more than 500 songs for charity. We also offered 7-day free memberships for our online music and online karaoke services, making our platform available to people to express their thoughts and good wishes to one another.

As the leading online music entertainment platform in China, TME has been highly recognized by China's mainstream media. During the epidemic, TME was honored to be invited again to participate in the Wuhan News Agency's Sound in China program. The touching melody and lyrics of Wuhan Not Alone achieved more than 100 million times of exposure on the day of its release on our platform.

We also worked with the People's Daily to bring music to the affected areas, strengthening the bond between medical staff and patients to overcome the epidemic.

Next, Tony will discuss fourth quarter results of our social entertainment services, as well as our other focus areas. Tony, please go ahead.

Tony Yip: Thank you, Cussion. Hello, everyone. Apart from our strengthening content leadership, there are a few other areas that we have excelled in, in both our online music and social entertainment services.

For online music, to begin with, our promotional capabilities have been further strengthened. Our comprehensive promotional infrastructure not only leverages TME's online platform, but also through cooperation with external online and offline channels.

In the fourth quarter of 2019, we successfully held the first Tencent Music Entertainment Award, TMEA, in Macau and live-streamed it online on our platform, presenting a strong lineup of top domestic and international singers such as Gem Deng (Speaking Foreign Language), Westlife, and Lay Zhang (Speaking Foreign Language), etc.. This event became a national hot topic and generated tremendous media exposure both online and offline for our artists. Within 2 weeks of TMEA, the cumulative page views of the topic on the internet reached nearly 7 billion.

Second, in order to improve satisfaction of more than 600 million online music users, we constantly strive to find innovative ways to enhance our products. In the second quarter of 2019, we pioneered a product innovation by adding short videos onto Kugou Music's streaming page, to fulfill users' needs to consume music-centric short videos while listening.

By leveraging better algorithms to recommend high-quality content, the average daily streams of short videos increased almost 50% at the end of the fourth quarter of 2019 compared with the end of the third quarter. We have encouraged and attracted users to upload self-produced short videos, and by the end of 2019, over 60% of the streams of short videos were user-generated content.

As you may recall, in the second quarter of 2019, we upgraded our QQ Music app with a more distinct tab for personalized recommendation. We continue to see positive user response and achieved 30% higher streams quarter-over-quarter, driven by the personalized recommendation tab during the fourth quarter of 2019.

We significantly raised the weekly retention rate on the personalized recommendation tab to as high as 90% at the end of 2019 with added new features such as personal song list. Our upgraded features, such as daily recommendation and personalized radio stations, also yielded double-digit percentage increases in average time spent after the upgrade.

Following these, in December 2019, we launched an upgraded version of Kugou Music app with a complete revamp of our user interface, which has a younger image and highlights personalized recommendation, short videos and long-form audio. The new UI design has continued to receive positive feedback, particularly from young users. Two weeks after the added upgrade, DAU for both the personalized playlist and short videos increased by double-digit percentage.

Thirdly, on technology advancement, we recently upgraded QQ Music's song recognition to be able to continuously recognize songs embedded in short videos for various use cases, which helped increase the number of daily active users of song recognition feature by double-digits percentages in the fourth quarter compared to the third quarter of 2019. The core song recognition technology, audio fingerprint extraction, and our audio processing capability, MIDI extraction, won 2 world championships in the Music Information Retrieval Evaluation eXchange Competition in November 2019, breaking 3 world records.

Turning to our social entertainment services, overall, it achieved a nearly 33% year-over-year top line growth, as our paying user base expanded 22%, and ARPPU grew 9% year-over-year, maintaining a steady expansion rate.

One of the highlights during the fourth quarter is our annual flagship social entertainment galas, which provided performers, KOLs and music lovers with captivating and interactive experiences, attracting record high participation, and contributed to the solid paying user growth and average spend expansion, demonstrating its effectiveness to improve user engagement on our platform.

For Kugou Live, in 2019, we continued to attract a growing number of music-centric live-streaming performers onto our platform, resulting in double-digit percentage growth in the number of active performers, while increasing the number of exclusive performers by more than 300% compared to 2018.

One of our key competitive differentiators is the virtuous cycle of value creation between our social entertainment and online music services. For example, we successfully discovered Xiaoqian, a live-streaming performer on our Kugou Live platform, and helped her become an internet celebrity, with 12 of her songs advancing to top 5 on Kugou Music charts in 2019.

We also hosted more than 500 New Song Releasing Events, (Speaking Foreign Language), for emerging artists and performers in 2019, demonstrating the attractiveness and the promotional effectiveness of our integrated online music and social entertainment platforms.

Additionally, to better meet user demand, we expanded live-streaming content categories to include online games, dating, and virtual anchor live-streaming. While still at an early stage, these additional content offerings have achieved good initial user feedback.

For WeSing, during the past quarter, there were a few areas of improvement that we have started to see traction. First on short video, we improved overall conversion from recording to publishing a song by adding various short videos assisting tools. As we transform content format on the platform from audio to video, we strive to make sharing more entertaining.

Secondly, on social attributes, which are quite unique to WeSing, we substantially bolstered user interactions through the function of group messaging and private messaging, leading to a more than 40% sequential increase in the number of users adopting this feature in the fourth quarter of 2019.

Additionally, we optimized online singing room features by emphasizing user groups with similar interests and profiles, which resulted in sequential improvements on user activeness and penetration, particularly within the younger demographic.

Overall, we started to see positive results from the efforts that we have deployed to make online singing an engaging, social and fun experience to retain users, and improve their stickiness on the WeSing platform. WeSing's average user time spent, its user activities, and the penetration rate of its monthly active users for the online singing room feature all improved sequentially in the fourth quarter of 2019.

The engagement of paying users was further strengthened by our UGC reward system, resulting in solid growth of monthly retention rate of paying users throughout 2019. During the 2020 Chinese New Year holiday, we saw the average daily time spent per person increased by 30% compared to pre-holiday period, and the number of users with song recordings increased by more than 35%. We are confident that we will continue to see healthy improvements in user engagement, and further increase in the core user group activities and loyalties throughout 2020.

Looking ahead, to leverage the expertise and operational track record that we have built over the past decade, we are very excited to share with you that QQ Music will be officially launching its live-streaming services within the QQ Music app in the first half of 2020, and gradually ramping up in the course of the next few quarters. This product will focus on the discovery and cultivation of star performers and artists, as we leverage QQ Music's powerful promotional capabilities, massive organic traffic and dynamic fan-based ecosystem.

In conclusion, we ended 2019 on a strong note, and are excited that the new initiatives, including long-form audio expansion and QQ Music live-streaming, will provide new growth avenues for TME in the years to come.

With that, I would like to turn it over to our CFO, Shirley Hu, for a closer review of our financials.

Shirley Hu: Thank you, Tony. Hello, everyone. We achieved strong financial results throughout 2019. For full year 2019, our total revenues were RMB25.4 billion, up 34% year-over-year. Our non-IFRS net profit was RMB4.9 billion.

In the fourth quarter of 2019, our revenues were RMB7.3 billion, up 35% year-over-year, driven by 41% growth in online music service revenues and 33% growth in social entertainment service revenues.

Online music service revenues were RMB2.1 billion, up 41% year-over-year. The increase was mainly driven by outstanding performance from music subscriptions, supplemented by growth in advertising services and the sales of digital music albums, partially offset by decrease in sublicensing revenues.

Music subscription revenues were RMB1.1 billion, up 60% year-over-year, driven by record high growth of subscribers and improvement in ARPPU. Specifically, number of subscribers increased 48% and the subscriber ARPPU grew 8% year-over-year, reflecting success of our pay-for-streaming service strategy and premium membership offering. Consequently, we have seen continued improvement in user retention rate and increasing user willingness to pay for premium content.

Social entertainment service and other revenues were RMB5.2 billion, up 33% year-over-year, primarily driven by growth in live-streaming and online karaoke services. In the fourth quarter of 2019, our flagship annual social entertainment galas contributed solid paying user growth and user spend expansion, resulting in paying user growth of 22% and ARPPU growth of 9% on a year-over-year basis.

Cost of revenues were RMB4.8 billion, up 35% year-over-year, driven by higher revenue-sharing fees and content expenses.

Our gross margin was 34.1% in Q4 2019 and improved slightly from Q4 2018, driven by gross margin improvements in online music services as a result of revenue growth, despite ongoing margin pressure from increased revenue-sharing ratio in social entertainment services.

Total operating expenses were RMB1.4 billion, up 5% year-over-year. Total operating expenses, as a percentage of total revenue, was 19.4% in Q4 2019, down 5.7 percentage points from 25.1% in Q4 2018, part of which was due to the fact that IPO-related expenses incurred in the fourth quarter of 2018 did not recur in 2019. The decrease also reflected success of our continued efforts on operation efficiency in various areas such as user growth spending and brand and content promotion expenses.

Our effective tax rate was 12.4% in Q4 2019.

Our net profit attributable to equity holders of the Company was RMB1 billion. Non-IFRS net profit attributable to equity holders of the Company was RMB1.3 billion and non-IFRS net profit margin was 18.4%.

As of December 31, 2019, our combined balances of cash and cash equivalents, term deposits were RMB22.9 billion, representing an increase of RMB1.8 billion from RMB21.1 billion as of September 30, 2019. The increase in the balances was primarily due to cash flow generated from operations of RMB2. 0 billion in the fourth quarter of 2019.

Overall, we achieved strong growth across our online music and social entertainment businesses in both the fourth quarter and full year 2019, driven by strengths of our products and contents.

Looking forward, we will remain focused on content investments to further enhance user engagement and monetization, and continue to expand our product and service offering such as live-streaming in QQ Music and long-form audio.

This concludes our prepared remarks. Operator, we are ready to open the call for questions.

Questions and Answers

Operator: Thank you, ma'am. We will now begin the question-and-answer session. (Operator Instructions). Wendy Chen of Goldman Sachs.

Wendy Chen: So my question is about the new initiatives on the social entertainment side, and particularly adding live-streaming feature into QQ Music. I'm just wondering what magnitude of incremental revenue does management expect this new initiatives can bring to us in 2020? And for the near-term strategy, would we focus more on user adoption or monetization for this addition?

And if I may add a simple follow-up, a similar question to our long-form audio initiative, how does management see our competition landscape in this new field, and what is our near-term strategy for this new initiative in 2020?

Tony Yip: Hi, Wendy, thank you for your question. Look, we intend to launch live-streaming services for QQ Music likely in the second quarter. This product, initially we focus on the discovery and cultivation of star performance and artist. We are very strong in leveraging our experience and know-how, our massive music-centric user base, as well as our powerful promotional capabilities and dynamic fan base ecosystem to gradually scale it up. While we don't expect it to contribute to 2020 revenue in a significant manner, we do expect it to ramp up over the course of the next few quarters, with more meaningful results contributing to 2021.

Cussion Pang: I would like to add on the long-form audio part that, Wendy, you mentioned about. We are so committed and thinking that the long-form audio is a new area that we can further expand our user base and also our [offering] in the future. What we are doing is, as we mentioned before, during the last part of the second half of 2019, we actually have been already enhancing our applications and letting our users to have a better user experience on the long-form audios.

At the same time, we also partnered with many different content providers to provide more long-form audio content. One of the very exciting examples that I have just announced to everyone is we have already entered a 5-year contract with the Chinese Literature, which means that we are going to have right and very large library of long-form audios. And we are going to produce our audio books for our users, and which will help to drive the further engagement of our users on the platform. So it's going to be an exciting journey in this area for us.

Wendy Chen: Thanks very much.

Millicent T.: Next question, please.

Operator: Alex Poon of Morgan Stanley.

Alex Poon: My first question is regarding the ARPPU growth. It is showing very visible improvements in the fourth quarter. So can you give us some color on the percentage mix now of membership signing up the green diamond mix? And also what is your expectation of ARPPU growth in 2020?

And then my second question is regarding the master agreements. With the first one potentially ending in second quarter, how should we expect a change in sublicensing income and your cost structure and margin in the second half and after?

Cussion Pang: I will take the first question, regarding the ARPPU, and right now, according to I think the online music revenue is very important and healthy business model for us. And what our focus is on the paying ratio, which has been continuously improving in the past few years, and we are also seeing a pretty good acceleration on the paying ratio as well.

In terms of the ARPPU, I think that is more likely increasing. This is because more and more users also trying to subscribe to our VIP plan. And also we are seeing that the retention rate of our monthly subscribers keep improving as well. So this is growing a really healthy manner. So maybe Tony and Shirley can take the second question.

Shirley Hu: Okay. About sublicense revenues, because we expect that we will -- transmission out of which some major labels from master lessons, master agreement, so we expect that the sublicense will be increased, and such our margin will be increased because we did not put the money at front when we signed the agreement with the labels. If some third parties form did not sublicense from us, we will have some loss. So we expect our gross margin, if we don't sign the master agreement, our margin will decrease, yes.

Tony Yip: Just add to that, I think you all knew that last year, we had signed a couple of the bigger contract in the form of master licensing, where we have to pay a very chunky, high fee upfront, that covers not only our platforms usage, but also the potential revenue that we might be able to recoup by sublicensing to other platforms. But as we all know, into the second half of last year, we were not able to recoup some of that sublicensing revenue, which resulted in a loss though, in foregone revenue for us.

And therefore, going forward, we'll be evaluating the master licensing, and to the extent that we decide not to renew certain contracts on a master license basis, we'd be only doing so because it would be margin accretive to us because we would no longer have to take that risk of having to pay a high upfront licensing fee, not just for our platform usage, but also for the third-party platform usage. So we no longer need to do that if we are not extending on a master license basis. So that could potentially be a margin accretive event for us.

Alex Poon: Thank you very much.

Millicent T.: Okay. Next question, please.

Operator: John Egbert of Stifel.

John Egbert: The digital service, it seems like TME is in a much better place than many of its peers in terms of the coronavirus impact during the first half of 2020. I'm wondering if you could talk through some of the puts and takes that could impact your results during the first half of the year, both positively and negatively, between the different products in your portfolio, and in some products' usage might benefit than in others, may be spending might be a little bit tougher? But maybe you could walk us through some of those, that'd be really helpful.

Tony Yip: Sure. Well, first of all, I think before addressing the question about the outlook towards 2020, we want to reiterate that we are very pleased with the Q4 performance, with total revenue growing 35% year-over-year, which is a faster pace than Q2 or Q3. And especially, our online music subscription revenue grew 60% year-over-year, which is continuing on the accelerating growth trend, which we expect to continue into Q1. And at the same time, our social revenue grew at a very solid 33%, which is a similar pace compared to the last quarter.

And then in terms of kind of our outlook, again with the relevant disclaimers for forward looking, I'll first address the online music service and then I'll talk about social entertainment, and then I'll sum it up for overall. For online music services for Q1, we expect our overall online music services revenue year-over-year growth rate to be lower than that of Q4, primarily due to declining sublicensing revenue, as well as advertising revenues impact from the virus.

However, we expect subscription revenue, which is our core focus, to continue to see year-over-year growth rate to accelerate in Q1 compared to Q4. And similarly for the full year in 2020, we expect overall online music services revenue year-over-year growth rate to be lower than 2019 levels due to lower sublicensing revenue.

But full year subscription revenue is expected to grow at a faster pace than 2019, which is very, very excitingly, driven by growth in both subscribers and ARPPU, and not just being driven by subscriber growth. And you've already seen that our ARPPU growth has already seen 3 straight quarters of year-over-year increases, so we can expect that trend to continue.

And then for social entertainment services, we expect revenue growth to be pressured in Q1 due to short-term impact from the coronavirus, from adjustments to some of our live-streaming interactive features for compliant reasons, and the tough comparison due to the timing shift of the WeSing Annual Gala to Q4. However, we are already taking steps to mitigate these impacts, and we expect the revenue growth to improve into the second half.

In addition, we're very excited about the growth potential from the launch of live-streaming services in QQ Music in the first half, which we expect to contribute revenue more meaningfully next year in 2021, and become an additional growth engine for our social entertainment services.

I think specifically worth mentioning about the social entertainment MAU, while there is a sequential drop in fourth quarter for reasons I've outlined in Q3 earnings call, which I won't repeat again, we're very pleased to share that we expect MAU to rebound in Q1.

And we're already seeing the numbers on track to deliver that in January and February, driven by a very well-executed set of growth initiatives that I also outlined during last quarter's earnings call, just namely to improve user engagement by lowering the user usage barrier by substantially increasing short-video elements on the platform as well as by focusing on growing the social network, which is the core competitive advantage within WeSing. And as a result, we expect MAU for social entertainment to resume a healthy growth trend throughout 2020.

So in terms of overall total revenue for the Company, for reasons outlined above, we expect Q1 total revenue year-over-year growth rate to be much softer, but to accelerate over the next few quarters. And for the full year, even though total revenue growth is expected to be slower than original expectations due to the short-term impacts in the first half, we expect revenue growth to improve in the second half. And more so, we feel very confident about the long-term growth potential of TME.

You'll remember that a year ago, when we started implementing the pay-for-streaming strategy, which has proven now to be very successful, we were leading the music industry to adopt a brand new model that will build a much better future for the whole industry and for all participants involved -- platforms, content producers, musicians. And today, we feel even more confident about the prospects of the music subscription business.

If you compare it to the Western comparables where they're running at around 50% paying ratio, we're currently at 6%. And if you compare us to other online video platforms in China, where as a whole, there are between 300 million to 400 million subscribers, our platform has only 40 million. There's 8x to 10x potential that you could see by those comparisons.

And lastly, we're constantly exploring new opportunities in light of the macro backdrop. One such example is our recent launch of TME Live, a new live-streaming model that integrates offline concerts onto online live-streaming experience, given large gatherings are limited during the virus outbreak. And couple this with the launch of live-streaming and QQ Music expansion into long-form audio that Cussion mentioned, the scaling-up of advertising and the continued growth in the musician program, we're confident that all of these investments will contribute significantly to the top line growth over the years to come.

John Egbert: Great. Thank you.

Millicent T.: Thank you, Tony. Next question, please.

Operator: Binnie Wong of HSBC.

Binnie Wong: So if we look at -- I think it's encouraging to see the uplift in the paying ratio. But if we look at the MAU side, which is your fundamental driver, both the MAU in the online music and also social entertainment has also been seeing some decline, right? If you look at social entertainment, despite the shift of the Annual Gala, it's both declining on YonY and QonQ. So and then I just want to understand the reasons of the decline in the MAU here.

And then with that, also understand that if you look at the -- we understand why there's better economics of TME not choose to renew some of the master license. So how should we think about in terms of user acquisition strategy into 2020?

Tony Yip: When we talk about MAU, we're absolutely not concerned by the slight drop in the music MAU in the fourth quarter because that's just part of seasonality. Every Q4, you would see a slight drop sequentially, but we expect to recover from that into Q1.

And then for social entertainment MAU, we had alerted our shareholders and the investors in the last quarter earnings call that due to competitive pressure, we are seeing a slight decline in MAU on a sequential basis for social entertainment. But like I mentioned, we've implemented a very comprehensive and well-executed growth plan, tackling user acquisition as well as user engagement and the plan is working very well and it's showing very good traction, which is why we expect the social entertainment MAU to rebound in Q1 and to resume a healthy growth trend throughout 2020.

Cussion Pang: In terms of the master licensing that you mentioned about, I think that we are still believing that the master licensing agreements do have a very good value to the industry, which means that we will continue to have some of the master license agreement with certain kind of labels, but not all of them. We will be -- have the wisdom to decide which label are we going to adopt the master license agreement or which one we do not.

As we mentioned about especially the 3 labels, the 3 major labels, which are counting for most of the content cost, relative for the content costs of our Company, we are moving away from the master license agreement. I think that is going to let us to be enabled to achieve some cost saving, as we will no longer need to have the commitment of upfront payment for this licensing. So I think that is going to be good for us.

And also because we already have a very huge user base, over 800 million active monthly users, even though we are not going to have master licensing with the 3 major labels, if we have the license on a platform, it will meet the demands of our users, which will serve the purpose. So I think that we will be very careful in selecting our strategies in terms of the recontracting with all the [famous] labels.

Millicent T.: Next question, please.

Tony Yip: I'm sorry, just to wrap up, I think in terms of there was a question about how we would approach user acquisition from the content angle. I think as Cussion mentioned, we are very committed to enriching continuously our content offering to further strengthen our content leadership, which is already very strong, and we've added a lot of new content to cater for user demand, especially for the younger demographics, like the Chinese Asian style, like the ACG or J-pop or K-pop, which are also showing very good results in terms of allowing us to further penetrating into the younger demographics, especially the Gen-Z.

Operator: Alex Yao of JP Morgan.

Alex Yao: First question is about the progress of the ever-expanding paywall. Can you share with us, by the end of Q1, what portion of the content library will be put behind the paywall? And how do you think about by the end of 2020, what percentage will be behind the paywall?

And then secondly, regarding the sublicensing revenue, we understand the appetites or demand for sublicensing the professionally curated content from you guys is going down. Can you help us understand why is the competitor de-emphasizing such content channel? And if the consumer demand for such content is generally going down, why do you need to spend aggressively on such content?

Tony Yip: On the paywall, we will address Q1 when we report Q1 results. But what I'm happy to share is that we started embarking on the paper streaming strategy in Q1 of 2019. So effectively, we started with zero percent of our content behind the paywall based on streaming volume share. And by the end of 2019, around 9% to 10% of the content is behind the paywall. And so you could expect a similar sort of pace in terms of the pace of content that we'll put behind the paywall during 2020.

Cussion Pang: And also in terms of the content that you're talking about, what we are doing in TME is we try to provide as much content as possible to our users, which basically, because the demand of our users is very complicated, they will like to listen to the top-tier artists, the premier content. But at the same time, they will also like to listen to some long-tail content by the indie musician as well.

So I think that there's no set -- or one way to satisfy all the needs of our users. So there's a reason why we need to strike a balance and we need to provide the most content which is available to our users. And this is what we are continue doing and doing well in the past few years, and we will continue to doing this.

And in terms of the cost structures, I think that, yes, some of the premier content may be a little bit more expensive than the others, but it seems that we are also participating with many partners to co-produce some of our own content, which will help us lower some of the funding costs as well. And we are going to help in the industry, let more young, talented musicians to have the platform or the stage to help them to demonstrate their talent. So I think this is what we will continue to doing this.

And since the year of 2017, we have already put in a lot of efforts in helping the indie musicians in China, and we are achieving really good results, especially on our musician program. So I think that our current strategies are very clear, and I'm sure that the direction is correct and we will achieve even further success in the in the years to come.

Millicent T.: Next question, please.

Operator: Alex Ziyang of Macquarie.

Alex Ziyang: Just a really quick follow-up on the master license. I guess could you give us some color on the main negotiation points when we're talking to music labels, both from the domestic or more independent labels and the international ones? Thank you.

Tony Yip: Well, I think in terms -- obviously, we won't be able to share a lot of details in terms of the negotiation points, given the highly sensitive nature. But I'd like to remind you that price is not the only discussion point. In the past, we've often won contracts without having to pay the highest price because our content partners really see us as a partner of choice. Given that, we help them with copyright protection in China, we are the biggest platform, that account for a vast majority percentage of the market share.

We are by far the most successful in terms of helping them monetize the music online. And our promotional capability not only is strong on our own platform, but we also extend our promotional capability beyond our online platform into external channels through our partnerships, as well as through offline channels, such as live events, etc.

So all of these are very important factors that our content partners take into consideration, which is why we are able to have the confidence that will keep renewing the important content that matters to us.

Operator: Hans Chung of KeyBanc Capital Markets.

Hans Chung: So my first question regarding the social entertainment business, and there seems to be the regulatory issues in live-streaming platform in whole sector in early of this year. And then also I think of the negative impact for Q1 guidance, and just wonder what's our view on this? And then how should we overcome the regulatory issue? And then how are we confident with just getting back to the normalized course in the second half?

And then a follow-up question is regarding the gross margin, and can management team just give some puts and takes about the gross margin for the whole year, given that we have a different moving parts going on this year, that faster growth for music, the renewal of the sublicensing deal and also the softer social entertainment business in the first half and so on. So just kind of a general sense about our gross margin for the year compared to last year.

Cussion Pang: Okay. I'll take the first part of the question and maybe Tony and Shirley talk about the margin. When we're talking about the social entertainments ideas, I think overall, we have done a really good growth rate in the year 2019. And the growth rate is very healthy, but the recent interactive features adjustments and also the coronavirus had some short-term financial impacts to us, especially on the social entertainment business in the first half of 2020.

But since we have already got many years of experience in winning our social entertainment business and build a strong foundation. So therefore, we are confident to achieve a healthy and long-term sustainable goal of our social entertainment services in the future.

And as we also mentioned during the early part of this conference call, we mentioned that we are targeting to launch the QQ Music live-streaming services in the second quarter of this year. So once again, it is going to be another driver for us in the social entertainment revenue in the future.

And also during the coronavirus period, we're also seeing that we are having some good result on the leasing platform as well. More people started to have more interaction with their friends through the social networks, and we are also seeing a strong comeback on the user base actively participating in our social entertainment platform. So we are expecting that recovery and a good growing trend in the second half of this year.

Shirley Hu: Okay. About the gross margin, we think the margin is a complex picture in 2019, 2020. First on the music side, we think our gross margin will be improved because our sublicense revenue will be increased. And when we jump out from the master agreement, the cost of that will be have benefit from it. So overall, we expect that the gross margin will be improving on the online music side.

Second, because of competition, we need to invest more on the revenue-sharing ratio on the social entertainment, that will impact our gross margin. The third, we need to invest more on the content, especially in long-form audio, so that will also impact our gross margin. And fourth, because the gross margin will be also impacted by the revenue structure because in 2020, we expect that the online music service revenue will be a growth factor in social entertainment. So overall, we think that into 2020, the gross margin will be a little decreased, yes.

Millicent T.: Next question, please.

Operator: Thomas Chong of Jefferies.

Thomas Chong: I have a question regarding the cooperation of Literature. Can management comment about how the business model works in terms of the revenue-sharing ratio or the cost that we need to pay to China Literature?

And a follow on that, are we seeing there will be more synergies with other part of Tencent ecosystem like gaming, the video? Any thoughts on more synergies of our music business?

Tony Yip: Yes, I'll first talk a little bit about the strategic angle with our cooperation with China, and then I'll let Shirley talk a little bit about the financial impact. I think it is very clear to us from our testing, that there are a lot of complementary behavior between our music users and long-term audio users.

And for based on our experience, we are already seeing that for users who listen to online, listen to long-form audio, the time spent that they spend on our platform is even longer than the time spent for our overall user base. And so it's very effective in terms of being able to improve the user stickiness, as well as allowing us to meet a broader set of user demands.

At the same time, from a long-form audio perspective, audiobooks is the number-one biggest category of content consumption. And within audiobooks, China Literature is by far the biggest provider, the biggest owner of this IP. And so through our strategic cooperation with China Literature, we are able to immediately get access to all the most important audiobook licensing that allow us to create these audiobook content, so that we could ramp up the user penetration.

And like we mentioned earlier, if you look at our Western peers, we're within a short period of 1 year or maybe less than 2 years, 1 to 2 years, they're able to achieve around a 16% penetration of their online music users that are also listening to long-form audio. And if we are able to achieve a similar set of penetration ratio, given our very sizable online music user base, there is an opportunity for us to become the number one long-form audio platform in China.

And the mid-teens penetration doesn't stop there; there is actually more room for that to grow to the 600 million target that's mentioned by the industry report. So there's very strong strategic synergies of why this corporation is very beneficial to both parties.

And I'll let Shirley talk a little bit about the financial impact.

Shirley Hu: About financial impact, because in 2020, we needed to invest in the long-form audio (corrected by company representative), we will give literature a reasonable minimum guarantee for it. And we are very excited because we have a very strong subscriber user base. So in long-form audio, we will focus on the subscriber increment. We believe in following years after 2020, we can get benefit from this business.

Millicent T.: Operator, we take the last question from the queue, please.

Operator: Zhijing Liu of UBS.

Zhijing Liu: Congratulations on the strong results. I have two questions. First one is will QQ Music's new initiative of live-streaming have cannibalization with our existing live-streaming business for Kugou?

And second question is regarding advertising-supported music, similar to Spotify, do you think it is achievable for TME in next 1 to 2 years? And how should we balance this new growth points with competition?

Cussion Pang: Okay. I'll take the first question. Thank you for talking about the QQ Music, the live broadcasting, which is an exciting project we're working on. First of all, both of the Kugou platform and QQ Music platform and Kuwo platform, they are already huge in size by themselves. And also the overlapping of users of them is very minimal, which means that they are serving its own user base really well. And when we are going to launch the live broadcasting services in QQ Music, it will even serve the QQ Music users even better. And there is not going to have any cannibalizations among the platform itself. So, yes, Tony, can you take the question?

Tony Yip: I think also in terms of QQ Music live-streaming, we have a lot of experience in user segmentation across our 3, 4 major apps; even similar to the music side, even though we are 3 music platforms, there's very minimal user cannibalization. In fact, having multi-brand, it allows us to cover a bigger user base as a whole and so we are adopting a similar know-how and expertise onto our live-streaming whereby, even though we have multi-platform, multi-brand on live-streaming. But it will target slightly different user segments that allow us to broaden our reach.

And then in terms of audio, we are certainly very committed to investing in this growth initiative. We see huge potential; there's a lot of synergies between music and long-form audio. And we view -- obviously, we take reference to the Western peers' experience and we target, we strive to achieve that. We won't set a timeframe on it because it's early days, but through our cooperation with China Literature, we are laying a very strong solid foundation, very strong foundation, that puts us in a very advantageous position in the starting gate.

Operator: I'm sorry, sir. It looks like we may have lost that question. Well, we have approached the end of the conference call. I will now turn the call over to the speaker host today, Ms. Millicent T. for closing remarks. Ma'am?

Millicent T.: Thank you. Thank you, everyone, for joining us today. If you have any further questions, please feel free to contact TME's IR team. This concludes today's call and we look forward to speaking to you again next quarter.

Cussion Pang: Okay. So listen, I just want to add quick conclusions. I think I would like to say thank you to every one of you joining the call today, especially for the support to TME. I think the year of 2019 is a very special year for TME since it's the first completed financial year after we officially launched it and listed on the New York Stock Exchange back in December 2018.

I think for this year, we are delivering a very good result and we are 120% committed to continue to create values for our users, partners and also our shareholders.

I think during the period of the coronavirus epidemic, I think that I wish you and also your family with good health, and all survivors -- and understanding that the virus has brought some negative impact to our society or even the global economy. But I'm sure that all the bad time is gone, and the future is bright. So we're together and I wish you and your family all the best, and God bless you all.

Okay. Thank you so much for (inaudible).

Tony Yip: Thank you. Okay. Thank you.

Shirley Hu: Thank you.

Operator: And we thank you, everyone, for joining us today. If you have further questions, please feel free to contact TME's Investor Relations team through the contact information provided on our website, or the Piacente Group, the Company's Investor

Relations partner.

This concludes today's call and we look forward to speaking with you again next quarter. Thank you again, everyone. Take care. Goodbye. Have a great day.