阅文集团
CHINA LITERATURE

China Literature Announces 2020 Interim Results

Hong Kong, August 11, 2020 – China Literature Limited ("China Literature" or "the Company", stock code: 0772), a leading online literature platform in China, today announced the unaudited consolidated results for the six months ended June 30, 2020.

Results Highlights [1]

- Total revenues increased 9.7% year-over-year to RMB3,260.2 million (USD460.5 million).
- Gross profit increased 6.8% year-over-year to RMB1,731.3 million (USD244.6 million).
- Operating loss was RMB3,555.6 million (USD502.2 million), as compared to an operating profit of RMB527.7 million in the prior corresponding period.
- Loss attributable to equity holders of the Company was RMB3,295.9 million (USD465.6 million), as compared to a profit attributable to equity holders of the Company of RMB392.7 million in the prior corresponding period.
- Basic loss per share was RMB3.30. Diluted loss per share was RMB3.31.
- On a non-IFRS basis:
  - Operating loss was RMB56.7 million (USD8.0 million), as compared to an operating profit of RMB517.1 million in the prior corresponding period.
  - Profit attributable to equity holders of the Company was RMB21.7 million (USD3.1 million), as compared to RMB390.0 million in the prior corresponding period.
  - Basic earnings per share were RMB0.02. Diluted earnings per share were RMB0.02.

Mr. Cheng Wu, Chief Executive Officer of China Literature stated, "The first half of 2020 presented tremendous challenges for China Literature. The sudden outbreak of the COVID-19 pandemic and a complex and changing macro-environment had a negative impact on our business. The Company recorded a loss for the first time in many years. The disappointing results made us realize that the lack of resilience of our underlying business model and our structural issues that have piled up over the recent years. We will take actions to actively deal with these challenges and have already quickly responded to address some of the most urgent issues affecting the cornerstones of our business. Going forward, we will focus on upgrading our content, platform and ecosystem to unlock the core values of the Company and to achieve a turnaround. In the long run, we are prepared to adopt a new culture and creative ideas from a more strategic and multi-dimensional perspective. We will also work with our strategic partners including Tencent to develop the industry together, with a more open and positive attitude, and invest in our future with greater courage and patience."

Financial Review [2]

Revenues increased 9.7% year-over-year to RMB3,260.2 million (USD460.5 million).

Revenues from online business increased 50.1% year-over-year to RMB2,495.4 million (USD352.5 million). Online business revenues from our self-owned platform products increased 101.9% year-over-year to RMB1,989.7 million (USD281.1 million), primarily driven by the expansion of distribution channels and users' growing willingness to pay for our reading content during the first half of 2020. Online business revenues from our self-operated channels on

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1. Figures stated in USD are based on USD1 to RMB7.0795.
2. Certain figures included in this press release have been subject to rounding adjustments. Accordingly, figures shown as totals may not be an arithmetic aggregation of the figures shown in the breakdown items.

Tencent products decreased 24.8% year-over-year to RMB324.3 million (USD45.8 million), primarily due to the continued decline in paid reading revenues from our self-operated channels on certain Tencent products. Online business revenues from third-party platforms decreased 26.2% year-over-year to RMB181.4 million (USD25.6 million), primarily due to the decrease in revenues from certain third-party platform partners.

Revenues from intellectual property ("IP") operations and others decreased 41.5% year-over-year to RMB764.8 million (USD108.0 million). Revenues from IP operations decreased 40.8% year-over-year to RMB719.2 million (USD101.6 million), primarily due to the decrease in revenues from New Classics Media ("NCM") during the first half of 2020. Revenues from others decreased 51.1% year-over-year to RMB45.7 million (USD6.4 million), primarily due to the decrease in revenues from the sales of physical books as impacted by the COVID-19 pandemic. In addition, we continued to adjust our physical book business and distribution channels in tandem with our business development strategy.

Cost of revenues increased 13.3% year-over-year to RMB1,528.9 million (USD216.0 million), mainly due to greater platform distribution costs resulting from expansion of online reading channels and our self-operated online game, which led to an increase in revenues. The increase in cost of revenues was partially offset by a decline in the production costs of TV, web and animated series and films along with a decrease in revenues.

Gross profit increased 6.8% year-over-year to RMB1,731.3 million (USD244.6 million). Gross margin was 53.1%, as compared to 54.6% in the prior corresponding period.

Interest income decreased 27.5% to RMB62.0 million (USD8.8 million), reflecting lower interest income from bank deposits.

Other losses, net were RMB3,529.7 million (USD498.6 million), as compared to net other gains of RMB269.6 million in the prior corresponding period. The other losses in the first half of 2020 consisted mainly of i) the impairment provision of goodwill and trademark rights related to the acquisition of NCM of RMB4,405.7 million (USD622.3 million), ii) a fair value gain on consideration liabilities of RMB1,240.3 million (USD175.2 million) due to an expected saving of earn-out consideration under the earn-out mechanism set upon the acquisition of NCM, and iii) the impairment provision of the Company's long-term investments related to certain investee companies of RMB252.0 million (USD35.6 million).

Selling and marketing expenses increased 30.1% year-over-year to RMB1,270.3 million (USD179.4 million), primarily driven by greater marketing expenses to promote our online reading content during the first half of 2020. As a percentage of revenues, our selling and marketing expenses increased to 39.0% in the first half of 2020 from 32.9% in the first half of 2019.

General and administrative expenses decreased 25.9% year-over-year to RMB350.7 million (USD49.5 million), primarily attributable to the reversal of compensation costs of RMB116.7 million (USD16.5 million) related to the service expense of certain employees and former owners of NCM as the Company expects that the performance of NCM in 2020 will be below expectation. As a percentage of revenues, general and administrative expenses decreased to 10.8% in the first half of 2020 from 15.9% in the first half of 2019.

Net provision for impairment losses on financial assets reflected the provision for doubtful receivables. In the first half of 2020, the provision for doubtful receivables was RMB198.3 million (USD28.0 million), mainly related to TV and film projects.

Operating loss was RMB3,555.6 million (USD502.2 million), as compared to an operating profit of RMB527.7 million in the prior corresponding period.

Income tax benefit was RMB201.3 million (USD28.4 million), as compared to an income tax expense of RMB123.5 million for the same period last year. In the first half of 2020, the recognition of deferred income tax assets and the reversal of deferred income tax liabilities from the accrual of asset impairment losses exceeded the income tax expenses that incurred during the first half of 2020, resulting in a net gain from income taxes.

Loss attributable to equity holders of the Company was RMB3,295.9 million (USD465.6 million), as compared to a profit attributable to equity holders of the Company of RMB392.7 million in the prior corresponding period.

Key Operating Information

- Average MAUs on our self-owned platform products and self-operated channels increased 7.5% year-over-year from 217.1 million to 233.4 million in the first half of 2020, among which i) MAUs on our self-owned platform products increased 16.1% year-over-year from 115.6 million to 134.2 million, primarily due to the expansion of distribution channels for our reading content; and ii) MAUs on our self-operated channels on Tencent products decreased 2.3% year-over-year from 101.5 million to 99.2 million, primarily due to the decline of users for paid reading content for certain Tencent products, partially offset by the increase in users brought by free-to-read content.
- Average MPUs on our self-owned platform products and self-operated channels increased 9.3% year-over-year from 9.7 million to 10.6 million in the first half of 2020, driven by the growing number of paying users on our self-owned platform products, partially offset by a decrease in paying users from our self-operated channels on certain Tencent products as more users were allocated to read free-to-read content on these Tencent products in the first half of 2020.
- Monthly ARPU increased 51.6% year-over-year from RMB22.5 to RMB34.1 in the first half of 2020, mainly because we enhanced the depth of our content operations, optimized our recommendation system and expanded content distribution channels during the period.

Other Key Information

- EBITDA was RMB59.6 million (USD8.4 million) in the first half of 2020. Adjusted EBITDA was RMB17.1 million (USD2.4 million) in the first half of 2020.
- As of June 30, 2020, the Company had net cash of RMB4,530.4 million (USD639.9 million).
- On October 31, 2018, the Company acquired 100% of the equity interest in NCM which is primarily engaged in TV series, web series and film production and distribution in China. NCM, on a standalone basis, recorded RMB129.9 million (USD18.3 million) in revenues and RMB97.1 million (USD13.7 million) in net loss in the first half of 2020. Due to the fluid and changing macro-environment and the outbreak of the COVID-19 epidemic, NCM's production cycle for film and television projects has elongated and becomes less predictable. The Company carried out an assessment of goodwill and trademark rights attributable to NCM as of June 30, 2020

based on impairment indicators. In the Board’s view, the recoverable amount of goodwill and trademark rights related to the acquisition of NCM was lower than their carrying amount, and the impairment provision was recorded of RMB4,405.7 million (USD622.3 million) in goodwill and trademark rights. At the same time, the Company recognized a fair value gain on consideration liabilities of RMB1,240.3 million (USD175.2 million) and reversed compensation costs of RMB116.7 million (USD16.5 million) related to the service expense of certain employees and former owners of NCM, as the Company expects that the performance of NCM in 2020 will be below expectation and will trigger a reduction in the earn-out consideration to the management team of NCM as sellers under the terms of the acquisition agreement.

Business Review and Outlook

Overview

The year 2020 started with a global COVID-19 pandemic unexpectedly. The pandemic has drastically changed the world over the past few months and has lasting implications for the macro-economy and film and TV industry in particular. Offline consumer demand shrank dramatically, streets were almost empty and theater chains were locked and closed. On the supply side, numerous projects, including TV and film productions, were delayed. The release dates are still uncertain for many projects.

The pandemic together with the fluid and changing macro-environment have had a negative impact on our business performance. The experience has made us realize that China Literature has structural issues that have piled up in recent years, which have gradually degraded the Company’s market share and neutralized its competitive edge. These are the fundamental reasons for our disappointing results.

Business Review

Our core online reading business has been facing challenges. The robustness of the China Literature platform depends on our talented writers and their creative drive. In the past, we failed to take full care of our writer’s feelings and support our writers adequately through our incentive program, and some of our writers expressed concern about previous versions of the writer's contract. Writers are the cornerstone of the China Literature platform, and we need to do more to enhance their trust.

Meanwhile, the free-to-read business failed to meet our expectations. Last year, we launched our free reading App Feidu as a supplement to our paid reading products. The free-to-read reading product has strong influence in certain markets and over certain user groups, but Feidu’s overall performance failed to match the leading position the Company enjoys in China’s online literature sector.

For IP business, consolidation with New Classics Media failed to produce full synergy. NCM is one of the best TV and film production houses in China. After the NCM acquisition, we tried to systematically convert our leading IP into TV series and films. The results were encouraging, as witnessed by the popularity of *Joy of Life (庆余年)* but far from an overall success, and our integration with NCM fell behind schedule, largely because we lacked a team with sufficient knowledge of both online literature and drama production to drive progress.

In addition, we lacked a structure, a top-down design to create an IP-centric content and operational strategy, which could maximize the life-time value of IP by promoting cross-media production. Our past efforts had resulted in some success stories but the real issue is how to scale. We need a detailed, systematic set of guidelines to turn our valuable IP into various entertainment content such as comics, animations, TV series, film and games. We need to carefully manage the value of each IP over its life cycle, and apply a common methodology to the entire IP portfolio in order to maximize portfolio returns.

Furthermore, we have many business partners that have not yet successfully been converted into participants in our ecosystem. With business partners, we negotiate deals by focusing on give and take, a typical zero-sum game mindset. With ecosystem participants, the central question is how to create a long-term, win-win relationship.

Initial Action and Results

We will take actions to deal with these challenges. The Company has already responded quickly to some of the most urgent concerns.

For example, regarding the complaints the writers have about our previous contracts, we initiated a candid dialogue with writer candidates to hear their concerns and promised to tackle deep-rooted issues in the industry. Within one month, we launched several new contract templates for writers to choose from, and stepped up our efforts to fight piracy to better protect writers' rights. These actions helped us regain the trust of the writer community, strengthened our core business, and attracted favorable attention from the market.

Outlook

Looking ahead, we will use the same critical thinking and responsive attitude as key tools to address issues in the Company's other business lines. We will take major steps to improve our content, platform and ecosystem. First, we will strengthen our core business through enhancing IP incubation capability, strengthening fundamentals, and speeding up cross-sector development to accelerate our IP development. Second, we will improve the social and community features of the platform and establish a stronger connection between China Literature's products and the Tencent portfolio. Finally, we will introduce enhancements to our IP-centric ecosystem, leveraging our high-quality IP to build business partnerships and networks in content segments including comics, animation, TV series, film, and games. We will capture new opportunities arising from our innovative technology, segment business models and partnership networks.

About China Literature Limited

China Literature Limited is a pioneer in the online literature market and operates China's leading online literature platform. The Company owns nine major branded products. Among these, QQ Reading, a unified mobile content aggregation and distribution platform, is the flagship product. Other branded products focus on individual genres and their respective fan bases. China Literature's shareholder and strategic partner, Tencent, provides the Company with exclusive content distribution access via its suite of leading mobile and Internet products, including Mobile QQ, QQ Browser, Tencent News, Weixin Reading and Tencent Video. The Company also has distribution beyond the Tencent platforms by pre-installing Apps on handsets partners such as OPPO, Huawei and VIVO, as well as licensing content to third-party partners such as Baidu, Sogou, JD.com and Xiaomi Duokan. China Literature monetizes its vast and proprietary content library mainly through online paid reading and content adaptations for a variety of entertainment formats. China Literature's diverse and high-quality content library is a significant competitive advantage that lies at the core of its business model. In 2018, China Literature further expanded its content capabilities downstream by acquiring New Classics Media, a renowned TV series, web series and film production company in China. For more information, please visit http://ir.yuewen.com/.

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Non-IFRS Financial Measures

To supplement the consolidated financial statements of the Company prepared in accordance with IFRS, certain non-IFRS financial measures, namely non-IFRS operating (loss)/profit, non-IFRS operating margin, non-IFRS profit for the period, non-IFRS net margin, non-IFRS profit attributable to equity holders of the Company, non-IFRS basic EPS and non-IFRS diluted EPS as additional financial measures, have been presented in this press release for the convenience of readers. These unaudited non-IFRS financial measures should be considered in addition to, and not as a substitute for, measures of the Company's financial performance prepared in accordance with IFRS. These non-IFRS financial measures may be defined differently from similar terms used by other companies. In addition, non-IFRS adjustments include relevant non-IFRS adjustments for the Company's material associates based on available published financials of the relevant material associates, or estimates made by the Company's management based on available information, certain expectations, assumptions and premises.

Our management believes that the presentation of these non-IFRS financial measures, when shown in conjunction with the corresponding IFRS measures, provides useful information to investors and management regarding the financial and business trends relating to the Company's financial condition and results of operations. Our management also believes that the non-IFRS financial measures are useful in evaluating the Company's operating performances. From time to time, there may be other items that our Company may include or exclude in reviewing its financial results.

Forward-Looking Statements

This press release contains forward-looking statements relating to the industry and business outlook, forecast business plans and growth strategies of the Company. These forward-looking statements are based on information currently available to the Company and are stated herein on the basis of the outlook at the time of this press release. They are based on certain expectations, assumptions and premises, some of which are subjective or beyond our control. These forward-looking statements may prove to be incorrect and may not be realized in future. Underlying the forward-looking statements is a large number of risks and uncertainties. Further information regarding these risks and uncertainties is included in our other public disclosure documents on our corporate website.

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CONSOLIDATED INCOME STATEMENT

	Six months ended June 30,	
	2020	**2019**
	(RMB in million, unless specified)	
Revenues		
Online business[1]	2,495.4	1,662.5
Intellectual property operations and others[2]	764.8	1,308.5
	3,260.2	**2,971.0**
Cost of revenues	(1,528.9)	(1,349.8)
Gross profit	**1,731.3**	**1,621.2**
Gross margin	***53.1%***	***54.6%***
Interest income	62.0	85.6
Other (losses)/gains, net	(3,529.7)	269.6
Selling and marketing expenses	(1,270.3)	(976.7)
General and administrative expenses	(350.7)	(473.4)
Net (provision for)/reversal of impairment losses on financial assets	(198.3)	1.5
Operating (loss)/profit	**(3,555.6)**	**527.7**
Operating margin	***(109.1%)***	***17.8%***
Finance costs	(38.1)	(93.5)
Share of net profit of associates and joint ventures	81.8	82.5
(Loss)/profit before income tax	**(3,511.8)**	**516.7**
Income tax benefit/(expense)	201.3	(123.5)
(Loss)/profit for the period	**(3,310.5)**	**393.2**
Net margin	***(101.5%)***	***13.2%***
(Loss)/profit attributable to:		
Equity holders of the Company	(3,295.9)	392.7
Non-controlling interests	(14.7)	0.5
	(3,310.5)	**393.2**
(Loss)/earnings per share		
(in RMB per share)		
- Basic (loss)/earnings per share	(3.30)	0.39
- Diluted (loss)/earnings per share	(3.31)	0.39

Notes:

(1) Revenues from online business primarily reflect revenues from online paid reading, online advertising and distribution of third-party online games on our platform.

(2) Revenues from intellectual property operations and others primarily reflect revenues from production and distribution of TV, web and animated series, films, licensing of IP rights for adaptation, operation of self-operated online games and sales of physical books.

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CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Six months ended June 30,	
	2020	**2019**
	(RMB in million)	
(Loss)/profit for the period	**(3,310.5)**	**393.2**
Other comprehensive (loss)/income:		
Items that may be subsequently reclassified to profit or loss		
Share of other comprehensive loss of associates and joint ventures	(0.1)	(0.4)
Currency translation differences	77.6	(18.1)
Total comprehensive (loss)/income for the period	**(3,233.0)**	**374.7**
Total comprehensive (loss)/income attributable to:		
Equity holders of the Company	(3,218.4)	374.2
Non-controlling interests	(14.7)	0.5
	(3,233.0)	**374.7**

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SEGMENT INFORMATION

	Six months ended June 30,	
	2020	**2019**
	(RMB in million, except percentages)	
Revenues		
Online business	2,495.4	1,662.5
Intellectual property operations and others	764.8	1,308.5
Total revenues	**3,260.2**	**2,971.0**
Cost of revenues		
Online business	(1,146.2)	(703.3)
Intellectual property operations and others	(382.6)	(646.5)
Total cost of revenues	**(1,528.9)**	**(1,349.8)**
Gross profit		
Online business	1,349.2	959.2
Intellectual property operations and others	382.2	662.0
Total gross profit	**1,731.3**	**1,621.2**
Gross margin		
Online business	54.1%	57.7%
Intellectual property operations and others	50.0%	50.6%
Total gross margin	**53.1%**	**54.6%**

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CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	As of	
	June 30, 2020	**December 31, 2019**
	(RMB in million)	
ASSETS		
Non-current assets		
Property, plant and equipment	36.1	41.5
Right-of-use assets	71.6	92.6
Intangible assets	7,655.5	12,168.8
Investments in associates and joint ventures	796.0	963.6
Financial assets at fair value through profit or loss	451.1	457.2
Deferred income tax assets	311.2	190.8
Prepayments, deposits and other assets	109.0	145.0
	9,430.5	**14,059.5**
Current assets		
Inventories	551.1	606.0
Television series and film rights	1,198.5	1,107.7
Financial assets at fair value through profit or loss	724.0	-
Trade and notes receivables	2,362.0	3,366.1
Prepayments, deposits and other assets	799.8	668.4
Restricted bank deposits	74.7	94.8
Term deposits	2,804.9	415.8
Cash and cash equivalents	3,515.0	5,931.8
	12,029.9	**12,190.5**
Total assets	**21,460.4**	**26,250.0**
EQUITY		
Capital and reserves attributable to the equity holders of the Company		
Share capital	0.6	0.6
Shares held for RSU scheme	(0.0)	(0.0)
Share premium	16,364.5	16,161.8
Other reserves	1,265.0	1,135.4
(Accumulated losses)/retained earnings	(1,197.1)	2,098.7
	16,433.1	**19,396.6**
Non-controlling interests	**(0.4)**	**14.2**
Total equity	**16,432.7**	**19,410.8**

	As of	
	June 30, 2020	December 31, 2019
	(RMB in million)	
LIABILITIES		
Non-current liabilities		
Borrowings	624.8	-
Lease liabilities	29.8	34.4
Long-term payables	22.3	-
Deferred income tax liabilities	194.6	322.6
Deferred revenue	32.5	33.5
Financial liabilities at fair value through profit or loss	-	535.1
	904.0	**925.5**
Current liabilities		
Borrowings	1,239.4	1,303.1
Lease liabilities	41.0	55.6
Trade payables	906.3	1,020.7
Other payables and accruals	927.7	1,489.7
Deferred revenue	829.3	717.7
Current income tax liabilities	180.0	205.4
Financial liabilities at fair value through profit or loss	-	1,121.5
	4,123.8	**5,913.6**
Total liabilities	**5,027.8**	**6,839.2**
Total equity and liabilities	**21,460.4**	**26,250.0**

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RECONCILIATION OF OPERATING (LOSS)/PROFIT TO EBITDA AND ADJUSTED EBITDA

	Six months ended June 30,	
	2020	2019
	(RMB in million)	
Reconciliation of operating (loss)/profit to EBITDA and adjusted EBITDA:		
Operating (loss)/profit	(3,555.6)	527.7
Adjustments:		
Interest income	(62.0)	(85.6)
Other losses/(gains), net	3,529.7	(269.6)
Depreciation of property, plant and equipment	11.5	11.0
Depreciation of right-of-use assets	32.6	31.3
Amortization of intangible assets	103.4	83.3
EBITDA	**59.6**	**298.2**
Adjustments:		
Share-based compensation	52.2	71.6
Expenditure related to acquisition	(94.6)	89.4
Adjusted EBITDA	**17.1**	**459.2**

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RECONCILIATIONS OF IFRS TO NON-IFRS RESULTS

	Six months ended June 30, 2020					
		Adjustments				
	As reported	Share-based compensation	Net loss from investments and acquisition[1]	Amortization of intangible assets[2]	Tax effects	Non-IFRS
	(RMB in million, unless specified)					
Operating (loss)	(3,555.6)	52.2	3,401.0	45.8	-	(56.7)
(Loss)/profit for the period	(3,310.5)	52.2	3,394.3	45.8	(174.7)	7.0
(Loss)/profit attributable to equity holders of the Company	(3,295.9)	52.2	3,394.3	45.8	(174.7)	21.7
EPS (RMB per share)						
- basic	(3.30)					0.02
- diluted	(3.31)					0.02
Operating margin	(109.1%)					(1.7%)
Net margin	(101.5%)					0.2%

	Six months ended June 30, 2019					
		Adjustments				
	As reported	Share-based compensation	Net (gain) from investments and acquisition[1]	Amortization of intangible assets[2]	Tax effects	Non-IFRS
	(RMB in million, unless specified)					
Operating profit	527.7	71.6	(146.0)	63.7	-	517.1
Profit for the period	393.2	71.6	(125.1)	63.7	(13.0)	390.5
Profit attributable to equity holders of the Company	392.7	71.6	(125.1)	63.7	(13.0)	390.0
EPS (RMB per share)						
- basic	0.39					0.39
- diluted	0.39					0.39
Operating margin	17.8%					17.4%
Net margin	13.2%					13.1%

Notes:

(1) Including impairment provision of goodwill, trademark rights and long-term investments related to certain investee companies, fair value changes arising from investee companies, fair value gains on consideration liabilities related to the acquisition of NCM and the reversal of compensation costs related to the service expense of certain employees and former owners of NCM.

(2) Represents amortization of intangible assets and TV series and film rights resulting from acquisitions.