



**ATA Creativity Global 2020 Second Quarter Financial Results Conference Call
TRANSCRIPT**

August 12, 2020 at 9 p.m. ET

SPEAKERS

Carolyne Sohn – Vice President, The Equity Group

Kevin Ma – Chairman and Chief Executive Officer, ATA

Jun Zhang – President, ATA

Amy Tung – Chief Financial Officer, ATA

Operator:

Good day and welcome everyone to the ATA Creativity Global 2020 Second Quarter and Six Months Financial Results Conference Call hosted by Carolyne Sohn. My name is Matthew and I'm your event manager. During the presentation, your lines will remain on listen-only. [Operator Instructions]

And with that, I'd like to hand it over to your host, Carolyne. Please proceed.

Ms. Carolyne Sohn:

Thank you, Matthew, and hello, everyone. Thank you for joining us.

The press release announcing ATA Creativity Global's, or ACG's, results for the three and six months ended June 30, 2020, is available at the IR Section of the Company's website at www.atai.net.cn.

As part of this conference call, the Company has an accompanying slide presentation available on its website. A replay of this broadcast will also be made available at ACG's website for the next 90 days.

Before we get started, I would like to remind everyone that this conference call and any accompanying information discussed herein contains certain forward-looking statements within the meaning of the

safe harbor provision of the Private Securities Litigation Reform Act of 1995. These forward-looking statements can be identified by terms such as “anticipate”, “believe”, “expect”, “future”, “plan”, “outlook”, and “will” and include, among other things, statements regarding ACG’s future growth and results of operations; ACG’s strategy of becoming a leading international education service provider; ACG’s plans for mergers and acquisitions generally; the benefits of the Huanqiuyimeng Acquisition; ACG’s ability to operate efficiently and maintain continued financial strength under unusual circumstances; ACG’s growth strategy and subsequent business activities; market demand for ACG’s portfolio training programs and other education services; the impact of the COVID-19 outbreak on ACG and its operations; and ACG’s plan and anticipated benefits of the measures implemented in response to the COVID-19 outbreak.

Although the Company believes that the expectations reflected in its forward-looking statements are reasonable as of today, those statements are subject to risks and uncertainties that could cause the actual results to differ dramatically from those projected. There can be no assurance that those expectations will prove to be correct. Information about the risks associated with investing in ACG is included in its filings with the Securities and Exchange Commission, which we encourage you to review before making an investment decision.

The Company does not assume any obligation to update any forward-looking statements as a result of new information, future events, changes in market conditions, or otherwise, except as required by law. Regarding the disclaimer language, I would also like to refer you to slide 2 of the conference call presentation for further information.

All U.S. dollar amounts in this conference call, relating to financial results for the three and six months ended June 30, 2020, are converted from RMB using an exchange rate of 7.0651 RMB: 1.00 USD, the noon buying rate as of June 30, 2020. All historical conversions are accurate as of the time reported, unless otherwise noted. The Company reports its financial results under U.S. GAAP in RMB, and all percentages calculated in the presentation are based on RMB unless otherwise noted.

For those of you following along with the accompanying PowerPoint presentation, there is an overview of the Company on slide 3. And management will be referring back to this deck throughout the prepared remarks. In addition, we are more than happy to take investor questions through our webcast portal or via email to the Company.

On today’s call, the Company’s CFO Ms. Amy Tung will provide a brief overview of operating and financial highlights for the second quarter and first half of 2020 and then ACG’s Chairman and CEO

Mr. Kevin Ma and President Mr. Jun Zhang will conclude the remarks with a discussion of the Company's outlook as well as its long-term growth strategy before opening the floor for questions.

With that, I'll turn the call over to ACG's CFO, Ms. Amy Tung. Please go ahead, Amy.

Ms. Amy Tung:

Thank you, Carolyne, and welcome everyone. Good evening to those in America. We appreciate everyone's time.

During the second quarter of 2020, we continued to deliver the majority of coursework to our students via online method, which we have done since February 1st. It was encouraging to see some local governments authorize the offline delivery of certain trainings late in the second quarter. And while we understand many students still prefer face time with their teachers and peers, we feel it is very important that we put the health and safety of our students, faculty, staff and employees first under these unprecedented conditions.

As with Q1, we continued to see several portfolio training students pursue their studies during Q2, while others decided to postpone their coursework. Our educational travel services business continued to be impacted in Q2 as almost all tours were cancelled, but we are pleased to be partnering with a few select prestigious overseas art institutions in offering some short-term online summer school and master training bootcamp programs, which generated RMB1.3 million in Q2 with increased contributions expected in Q3.

Our results for the second quarter of 2020 were impacted by the ongoing pandemic environment as in-person teaching remains unavailable in certain areas. We are encouraging students to continue pursuing their studies remotely, and we are also pleased that, since we last spoke in late May, the public health situation in China has improved to where nearly all of our employees are able to report to work in the office. With our sales team being able to operate at capacity, our business pipeline is seeing a resurgence, which bodes well for future periods.

For the second quarter of 2020, we reported a 7.4% year-over-year decrease in credit hours delivered for our portfolio training programs, from approximately 30,200 credit hours in Q2 2019 to approximately 27,900 in Q2 2020. This decrease was primarily a reflection of the continuing COVID-19 environment. We provide a breakdown of these credit hours and additional operating metrics on the next slide. Later in the presentation, Kevin and Jun will provide an update on current operations and where they stand.

As an overview, a credit hour is the standard unit measuring educational credit for our Portfolio Training Program and translates into roughly one hour of time committed. When it comes to enrollment headcount, a student may be counted twice in enrollment if he or she enrolls in both portfolio training and educational travel services in any given period.

Student enrollment for the period was 772, out of which 444 were enrolled in the Portfolio Training Program.

The Portfolio Training Program consists of time-based programs and project-based programs, and we provide a breakout of the credit hours delivered during the period compared to the prior-year comparable period in our presentation.

Revenue is recognized proportionately per credit hour delivered. However, as the total credit hours of project-based programs are not predetermined, the progress of a project-based program, which is measured by credit hours delivered compared against the total credit hours expected to be delivered, is re-evaluated at each quarterly and annual financial reporting date.

As in previous quarters, we saw a year-over-year increase in students opting for the project-based program versus the time-based program. As previously discussed, each program has its benefits depending on the particular student's needs. A student that already possesses some basic skills and wishes to only complete a portfolio will tend to favor the project-based program as it appears to be the less expensive option for completing a portfolio with a defined cost. Meanwhile, the time-based program caters to students that may want additional guidance and opportunity to work with teachers for some basic foundational skills before beginning on their portfolio.

With that, let's move to financials for the quarter.

I wanted to remind everyone that for the results shown for this period, we have applied acquisition accounting and made purchase price allocation adjustments (PPA) to various assets acquired and liabilities assumed from the Huanqiuyimeng Acquisition. As a result, certain line items will include adjustments from amortization of the difference between the carrying value in Huanqiuyimeng's book and the fair value assessed from the PPA process applied to the Huanqiuyimeng Acquisition. I will highlight where we saw some impact on our financials due to this PPA adjustment for the 2020 second quarter.

Total net revenues for the second quarter of 2020 increased to RMB26.4 million, compared to RMB1.4 million in the second quarter of 2019 as a result of revenue contributions from Huanqiuyimeng, which

consisted primarily of revenues from Portfolio Training Programs. Net revenues for this quarter include a PPA adjustment decrease of RMB6.0 million. I'd also like to note the sequential decrease in total net revenues, from RMB32.7 million in Q1 to RMB26.4 million in Q2, which is mainly a result of an RMB6.1 million decrease in revenue contributions from overseas study counseling services. Q1 is the quarter during which students receive the majority of their overseas study offers, which results in higher revenues from overseas study counseling services.

Gross margin was 25.1% during the 2020 second quarter, compared to gross margin of negative 1.8% in the prior-year period when the Company did not have substantive operations. Excluding the PPA adjustment to net revenues, gross margin for the 2020 second quarter would have been 39.0%.

Net loss from continuing operations attributable to ACG was RMB32.1 million for the period, compared to a net loss of RMB18.2 million in the prior-year period, as a result of increased operating expenses incurred related to the day-to-day operations of the Huanqiuyimeng business.

Moving to financial highlights for the first half of 2020... total net revenues for the year-to-date (YTD) period increased to RMB59.1 million, compared to RMB3.0 million in the prior-year period. Total net revenues for the period include a PPA adjustment decrease of RMB12.0 million.

Gross margin was 31.1% for the first half of 2020, compared to 12.9% in the prior-year period. Excluding the PPA adjustment to net revenues, gross margin for the first half of 2020 would have been 42.7%.

And net loss from continuing operations attributable to ACG was RMB52.5 million in the first half of 2020, compared to net loss of RMB31.1 million in the prior-year period, primarily due to increased operating expenses related to the Huanqiuyimeng operations as mentioned earlier.

Finally, we continue to be in a solid financial position with US\$16.9 million in cash and cash equivalents on the balance sheet. Working capital deficit was US\$16.9 million, and total shareholders' equity was US\$35.0 million at June 30, 2020, compared to working capital deficit of US\$11.7 million and shareholders' equity of US\$43.9 million, respectively, at December 31, 2019.

This past May, our Board of Directors authorized the repurchase of up to US\$1.0 million of the Company's issued and outstanding ADSs from time to time in open market and privately negotiated transactions. By August 1, 2020, the Company had repurchased 450,337 ADSs at an average stock price of \$1.2631. This share repurchase plan is in effect until December 31, 2020.

With that, I'd now like to turn it over to Kevin who will expand upon our outlook and growth strategy. Kevin?

Mr. Kevin Ma:

Thank you, Amy.

2020 has forced many of us in education to re-evaluate how we provide accessible learning to the various types of students in China. While the public health situation in China has improved dramatically over the course of the past few weeks, in-person teaching remains unavailable in many areas as the pandemic continues to impact several countries around the world.

ACG is known for its one-on-one portfolio training programs and the individualized attention our students receive as highlighted in recent reviews on Dianping, which is essentially like Yelp in China. Although the majority of our teachers are unable to interact with students face to face, we continue to strive to deliver the quality instruction and personal support for which we have gained recognition over these past several years.

I am pleased to see that many of our students have continued to pursue their studies in one form or another and have been happy with the level of attentiveness they have been receiving. With traveling abroad no longer being a viable option given the pandemic environment, students are choosing to pursue language studies or other types of foundational education to better prepare themselves for when that opportunity presents itself again. And many are even finding these types of courses to be quite well suited to being taught online.

ACG continues to be in a solid financial position as we continue to navigate the challenges presented by the global pandemic whether that means leveraging our operating flexibility or providing students with alternatives to our regular summer study abroad programs.

We continue to put the health and safety of our students and employees first and will continue providing students with the support they need to succeed via online platform, phone, email, WeChat, etc. as we monitor how the ongoing situation unfolds globally.

I'd now like to hand the floor over to Jun Zhang, ACG's president, to provide an update on our current growth initiatives. Jun will make his remarks in Mandarin, which will be followed by an English translation.

Mr. Jun Zhang:

Thank you, Kevin。

就像 Kevin 和 Amy 提到的，ACG 在努力应对全球疫情带来的影响。我们很高兴看到从第一季度到第二季度，作品集新签约人数和结转课时都有所增长，并且也在继续鼓励我们的学生通过远程线上平台进行课程学习。

我们的销售渠道持续改善是因为北京办公室差不多所有的销售和市场人员已经返岗可以更好地投入营销工作。此外，我们已开始使用多样化的在线平台，比如抖音（中国的 Tik Tok）作为其中一种营销工具，让潜在的学生可以在决定去哪里报名之前，亲身体验我们的艺术和创意教育。

即使已可以再次进行面对面的授课，我们相信疫情的影响仍然存在。它重申了科技在教育中的关键作用以及在传输方法的整体效能。虽然我们相信没有什么能够取代面授课程，但很多学生同时也喜欢灵活、有效率的在线课程。因此，我们在继续提供传统的作品集线下培训课程之余，也在计划将部分线下课程转为线上课程，尤其是一些侧重于基础知识的入门课程往往具有更标准化的课程内容，它们更适合进行在线教育。

至于游学，我们很高兴能与一些海外知名的艺术院校和机构合作，提供一些短期在线夏校以及大师集训营的课程，以替代我们之前的游学课程和项目。大部分在线夏校以及部分大师集训营合作项目会在 7 月和 8 月进行，将对我们第三季度的收入有正面影响。

更重要的是，我们一直关心着我们的学生，对于那些在疫情前已经报名的学生，我们在为他们提供创意艺术教育的同时，也在确保他们和我们授课老师的安全。

下面将交回给 Kevin。

Ms. Carolyn Sohn [translation]:

Thank you, Kevin.

As both Kevin and Amy mentioned, ACG has worked to adapt to the situation we've been presented with the global pandemic. We were pleased to see incremental improvement in portfolio training enrollment and credit hours from Q1 to Q2 and continue to encourage students to pursue their coursework via remote learning platform.

Our sales pipeline continues to improve as nearly all our sales and marketing personnel in Beijing have returned to the office and are able to operate at optimal productivity. Additionally, we have begun utilizing diversified online platforms, such as Douyin (also known as TikTok in the States), as a marketing tool enabling potential students to experience first-hand what our art and creative education offerings are like before making a decision on where to enroll.

Even after in-person classes can be conducted once again, we believe the effects of the pandemic will remain. It has reaffirmed the crucial role technology plays in education as well as the overall efficacy of the delivery method. While we believe nothing quite replaces meeting in person, many students are enjoying the flexibility and added efficiency of being able to take certain courses online. As a result, we are planning to convert some offline classes for portfolio training, particularly those at the introductory level that tend to have a more standardized curriculum, to online, but will still make traditional offline delivery an option.

With regards to educational travel, we are pleased to be offering some alternatives to our usual travel tours and programs. Working closely with a few well-known overseas art schools and institutions, we have been offering some short-term online summer school programs, which offer certifications upon the completion of the programs, as well as bootcamps led by teachers from these overseas institutions whom we have invited to cooperate with ACG's own teachers. Most of the summer school program offerings and certain master bootcamps will have taken place in July and August, which will have a positive impact on our top line in Q3.

Most importantly, we are focused on our students and providing them with the creative education they signed up to receive before the pandemic began while ensuring their and our staff's safety.

With that I'll turn it back to Kevin.

Mr. Kevin Ma:

Thanks, Jun and Carolyne.

To conclude, ACG continues to be well positioned financially and operationally.

We have worked tirelessly to adapt to the evolving situation and continue to do so while moving forward with our strategic growth initiatives. I believe ACG has risen to the challenge, and while our business has certainly felt the impact of these unusual circumstances, it has proven resilient, and we are optimistic about the future growth potential of our company.

There is a great deal of uncertainty in the world today. But we remain focused on continuing to serve our students and prioritizing the well-being of all our stakeholders. I would like to thank all of our employees, associates, family, and friends for their ongoing support, and I hope everyone continues to stay safe and healthy.

With that, operator, let's open it up for questions.

Question-and-Answer Session

There were no questions on the call.

Mr. Kevin Ma:

Thanks again to all of you for joining us. If anyone has questions for us, please feel free to reach out directly to us or our investor relations firm The Equity Group. We are always available to speak to investors and look forward to speaking with you all during our next quarterly call. Thank you.

Operator:

Thank you very much, everyone. This concludes your conference call for today. You may now disconnect. Thank you for joining and enjoy the rest of your day.