



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

May 14, 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 First Quarter Conference Call hosted by Carolyne Sohn. My name is Greg and I'm the event manager for today's call. During your presentation, your lines will remain on listen-only. [Operator Instructions]

Now, I'd like to hand over to Carolyne. Please proceed.

Ms. Carolyne Sohn:

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

The press release announcing ATA Creativity Global's, or ACG's, results for the first quarter ended March 31, 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 first quarter ended March 31, 2020, are converted from RMB using an exchange rate of 7.0808 RMB: 1.00 USD, the noon buying rate as of March 31, 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 first quarter 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.

Our results for the first quarter of 2020 were impacted by seasonality as a result of the Spring Festival holiday as well as the effects of COVID-19. When we last spoke to investors at the end of March, businesses in China were beginning to open and, while cautious, were returning to normal operations following the impact of the pandemic.

We made a conscious decision to transition all Huanqiyimeng coursework to a completely online format beginning February 1st as a measure of prioritizing the health and safety of our students, faculty, staff and employees during these times. At that time, we provided all of our students the option to fulfill their classes online.

On the portfolio training side, several students did opt to continue with their studies, but some decided to postpone their coursework. Our educational travel services business was also impacted during the period as the majority of tours were cancelled.

As a result of these headwinds, we reported an 8.7% year-over-year decrease in credit hours delivered for our portfolio training programs, from approximately 28,900 credit hours in Q1 2019 to approximately 26,400 in Q1 2020. 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 681, out of which 404 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 partial Q3 and Q4 2019, we continued to observe the same trend of students increasingly opting for the project-based program versus the time-based program. We noted on the last earnings call that each program has its benefits depending on the particular students' 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 first quarter.

Total net revenues for the first quarter of 2020 increased to RMB32.7 million, compared to RMB1.6 million in the first 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.

Gross margin was 35.8% during the 2020 first quarter, compared to gross margin of 25.3% 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 first quarter would have been 45.8%.

Net loss attributable to ACG was RMB20.5 million for the period, compared to a net loss of RMB12.9 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.

Finally, we continue to be in a solid financial position with US\$21.6 million in cash and cash equivalents on the balance sheet.

Working capital deficit was US\$13.3 million, and total shareholders' equity was US\$40.0 million at March 31, 2020, compared to working capital deficit of US\$11.7 million and shareholders' equity of US\$43.9 million, respectively, at December 31, 2019.

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. These are unprecedented times. As Amy noted, we continue to operate our business in this new environment and are focused on continuing to provide quality art and creative instruction to our students, enabling them to continue working toward their goals even while much of the world remains under "shelter in place".

We are fortunate to be in a solid financial position that will allow us to navigate the challenges businesses all over the world are facing as a result of COVID-19 for the amount of time it will take for circumstances to return to a new normal.

ACG has a great deal of operating flexibility as our infrastructure allows us to scale to meet changes in demand from our student base. We have been taking advantage of this operating flexibility to streamline costs when it comes to teaching availability and associated teaching costs arrangements. At the same time, we are able to almost immediately ramp up to satisfy an increase in demand when students that had decided to postpone their studies resume their programs once again.

With regards to educational travel, we do know that many of our partner institutions will not be holding their regular summer programs, which will have an impact on our business. We regret that our students will not be able to take advantage of our tours and programs this summer, but we want to emphasize that the public health and safety of our students and employees is of the utmost importance. We are in close contact with all our partners and will keep an eye on the global situation in the coming weeks and months.

We are prepared to continue supporting our students via online platform and are looking into ways in which we can maximize the potential of online technologies to grow our business and better serve students.

Additionally, we announced today that our Board of Directors approved a share repurchase program, which will allow the Company to repurchase up to US\$1 million of its issued and outstanding ADSs from time to time in the open market and privately negotiated transactions. The plan is effective now through the end of the year. We are pleased that the Board shares our confidence in the long-term growth potential of ACG's business and our commitment to building value for shareholders.

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

Mr. Jun Zhang:

谢谢 Kevin。

正如各位可预见的，受新型冠状病毒的影响，我们近期的目标有一些调整。改进我们的技术已成为一项优先任务，因为我们看到许多学生仍然希望继续他们在艺术和创作领域的学习。我们的目标是通过远程学习平台，为我们的学生提供可接触到全国最好讲师的可靠渠道，同时为他们取得成功提供必要的学术和良好的沟通支持。

此外，我们已经开始研究如何在服务提供之外利用线上的优势。例如，我们计划提供线上体验课程，让学生可以对环球艺盟的产品更直观的感受，从而促进销售。

我们计划继续为作品集提供传统的线下培训模式，但也正在探讨将一些线下课程转换为线上课程的可能性。对于内容比较标准化的基础知识入门课程，更适合进行线上教授，这样可以使我们在为学生提供更多灵活性的同时，也降低成本。

在线授课还提供了扩展学术产品和访问国际知名教师的途径，这些老教无需亲自来到现场即可进行远程授课。

关于游学，我们之前提到大多数的合作院校都取消了常规的暑期课程。因此，我们正在尝试为学生在今年夏天提供其他的选择，包括与某些知名海外学校和机构合作的在线云夏校的项目计划以及一些新开发的国内艺术主题游学项目。

现在，我们所有在北京的销售和市场人员几乎都已返回到办公室办公，而我们的销售也开始逐步恢复。北京之外的其他校区尚未完全开放，但我们预计这些校区在未来几周内也将陆续开放。

在全球各地企业均面临挑战的情况下，我们在财务和运营上仍然在良好的位置并平稳地过渡。我们将继续推进具有积极意义的发展目标 -- 建立合作伙伴关系，改善技术和提高入学人数。通过这样做，我们相信我们将成为中国最大的优质艺术、创造力教育和海外留学服务的提供商之一。

下面将交回给 Kevin。

Ms. Carlyne Sohn [translation]:

Thank you, Kevin.

As you might imagine, our immediate goals have changed somewhat in light of the COVID-19 pandemic. Improving our technologies has become a major priority as we are seeing that many students still wish to pursue their studies in art and creativity. We aim to provide reliable access to our best instructors around the country via remote learning platform while also providing the necessary academic and emotional support our students need to succeed.

In addition, we have begun looking at how we can take advantage of “online” beyond a service delivery method. For example, we plan to offer online classes as “trials” that will allow students to get a first-hand sense of Huanqiuyimeng’s offerings to generate sales.

We plan to continue offering the traditional offline mode for portfolio training but are exploring the possibility of converting some offline classes to online delivery. Introductory classes that focus on the fundamentals tend to have a more standardized curriculum, which lends itself to online delivery. Doing so will offer students added flexibility while lowering costs.

Online delivery also offers the potential for expanded academic offerings and access to internationally acclaimed instructors who can conduct classes remotely without the need for travel.

With regards to educational travel, we mentioned earlier that most of our partner institutions have cancelled their regular summer programs. We are working to develop alternative options for students this summer, including online summer school programs partnering with certain well-known overseas art schools and institutions and the newly developed art-themed domestic travel programs.

Our sales pipeline has begun to regain momentum now that nearly all of our sales and marketing personnel in Beijing are able to return to the office. Some of our local offices have not yet fully reopened, but we expect they will in the next couple of weeks.

We are well positioned financially and operationally to weather the challenges businesses all over the world have been presented. We continue to push forward on our growth initiatives where it makes the most sense—forging partnerships, improving our technology, and growing enrollments. In doing so, we believe we will emerge as one of the largest providers of quality art and creativity education and study abroad experiences in China.

With that I'll turn it back to Kevin.

Mr. Kevin Ma:

Thanks, Jun and Carolyne.

To conclude, ACG has the strong foundation needed to survive the current situation.

We continue to explore M&A opportunities, but it is a slow process in the current environment. We have a regimented strategy when it comes to evaluating potential opportunities internationally, which is somewhat challenged when site visits and in-person meetings are prohibited.

Above all, we remain focused on serving students to the best of our ability and prioritizing the well-being of all our stakeholders. I would once again like to extend my gratitude to all of our employees, associates, family, and friends for their support during these times. ACG wouldn't be what it is today without you. 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. Everyone, that concludes your conference call for today, you may now disconnect. Thank you for joining and enjoy the rest of your day.