

Hong Kong Exchanges and Clearing Limited and The Stock Exchange of Hong Kong Limited take no responsibility for the contents of this announcement, make no representation as to its accuracy or completeness and expressly disclaim any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this announcement.



CATHAY MEDIA AND EDUCATION GROUP INC.

華夏視聽教育集團

(incorporated in the Cayman Islands with limited liability)

(Stock Code: 1981)

Supplemental Announcement – Discloseable Transaction

Reference is made to the announcement of Cathay Media and Education Group Inc. (the “**Company**”) dated 20 December 2020 (the “**Announcement**”) in respect of the acquisition of the Target Company. Capitalised terms used herein shall have the same meanings as those defined in the Announcement unless the context requires otherwise. The Company would like to provide additional information in respect of the Acquisition in this announcement.

As set out in the Announcement, the RMB300 million consideration was determined with reference to and considering, among others, past academic results, geographic location, brand reputation, number of students, course offered and tuition level of the Target Company. These considerations included:

- Past academic results: Shuimuyuan is a leading art entrance exam training institution in China with past academic results among the top tiers in China and a good reputation for its high-quality education standards. For example, in the 2019-2020 academic year, Shuimuyuan students obtained a total of 1,312 arts entrance certificates from China’s nine arts academies. In the same academic year, 124 students and 393 students received arts entrance certificates from Academy of Arts & Design, Tsinghua University and Central Academy of Fine Arts, respectively. Shuimuyuan ranked first by the number of arts entrance certificates for students entering Academy of Arts & Design, Tsinghua University and Central Academy of Fine Arts for nine consecutive years. Such track record of academic excellence contributed to student enrollment growth in past years and is an invaluable intangible asset for future recruiting activities, which also contributes to Shuimuyuan’s enterprise value.
- Geographic location: As of November 2020, Shuimuyuan has five campuses and learning centers in Beijing, Jinan, Hangzhou, Shenzhen and Dalian, with approximately 3,100 trainees each year. This is the result of Shuimuyuan’s continued expansion of its geographical coverage in the past few years, and has not only fuelled the growth in student enrolments, but also reflects the ability of Shuimuyuan, its brand and its management to grow and conduct operations across different geographic areas. This scale has helped Shuimuyuan build a presence across multiple regions, with an established brand spanning the north, east and south of China. As the Company aims to operate its media and arts education business across China and grow organically in addition to its current operation of Nanjing Chuanmei Xueyuan, Shuimuyuan’s ability to expand across geographic locations is a key success factor for training companies and of particular value to the Company. Moreover, with the more recent growth in geographical locations and student numbers, and the expected continued expansion of Shuimuyuan’s business, we do not consider the historical financial results to entirely reflect the growth potential and likely future performance of the Shuimuyuan business.

- Brand reputation: As set out above, Shuimuyuan has achieved excellent academic results, creating a brand and reputation that itself would contribute to student enrolment growth and potential increases in revenue. Shuimuyuan has received many awards from professional institutions and industry newspapers and periodicals, including “Most Influential Education Group” (by xinhuanet.com), “Reputable Education Group” (by xinhuanet.com) and “Well-known Art Education Brand” (at the Education Ceremony of www.cnr.cn). This stellar industry reputation is in itself an intangible asset and contributes to Shuimuyuan’s enterprise value.
- Number of students: In the past few years, Shuimuyuan’s students’ number has been growing along with increases in its geographic locations. As November 2020, Shuimuyuan has approximately 3,100 trainees, which is among top tiers in industry. Shuimuyuan also has a track record of high-quality education, with more than 3,000 students admitted to the nine Chinese art academies since inception. While the successes of the past years and existing student numbers demonstrate Shuimuyuan’s academic level and brand reputation, we anticipate there is continued room for further growth. There is a market shortage of artistic talent, driven in recent years by significant demand for UI design and visual design capabilities due to the growth of the Internet. This is reflected in increases in enrolment of art majors, for which entrance examinations are an essential pre-requisite. Indeed, in 2019, approximately 600,000 students took the national college art entrance exams, with further growth expected. Against this wider trend, we believe that there is considerable opportunity for the number of students served by Shuimuyuan to continuously grow, particularly leveraging the Company’s existing resources in media and arts higher education and experience in film and TV production.
- Course offered and tuition level: Shuimuyuan’s course offerings primarily involve art entrance exam training for secondary-school students, including multiple courses offerings tailored to students seeking entry to Academy of Arts & Design, Tsinghua University and Central Academy of Fine Arts, among others. The secondary-school student population nicely complements the Company’s existing strength in media and arts higher education, through its operation of Nanjing Chuanmei Xueyuan, expanding the range and scope of services that the Group provides and covering a wider range of potential customers. The current tuition fee per student in Shuimuyuan ranges from RMB50,000 to RMB100,000, reflecting not only its academic quality and specialised course offerings, but also its ongoing profitability. Holistically, the Acquisition allows the Group’s media and arts training business to expand both in scale and scope as well as diversifying the range of students served and geographical coverage.

Considering the factors numerated above, the Directors are of the view that the consideration of RMB300 million is fair and reasonable, reflecting both the strength of Shuimuyuan’s historical performance and most importantly its considerable potential for future growth.

The consideration of RMB300 million was itself arrived at after arms length negotiations with the Founder and with reference to, and after taking into account of, (i) the Company's valuation of Shuimuyuan based on a consideration of comparable market valuations (including the P/E ratios of a number of comparable training-focused companies listed on the Stock Exchange), (ii) projected future revenue in light of the business plan and historical financial information of the Target Company and the Affiliated Entities, (iii) assessment of the staggered consideration and provision of Profit Guarantee for 2021, 2022 and 2023, and (iv) results of legal and financial due diligence. For example, the Company selected four companies listed on the Stock Exchange, each of which also had a primary or exclusive business focus on education training services. The average and median price-to-earnings ratio for FY2019 of such companies provided a benchmark maximum value of the consideration for the acquisition of the Target Company (after applying a private company valuation discount). Conversely, the projected Profit Guarantee set a minimum value for the Target Company (being a conservative minimum assessment of the expected financial performance of the Target Company). During commercial negotiations with the Founder, the risks identified in legal and financial due diligence were also sought to be mitigated and reflected by downward adjustment of the consideration. Additionally, it was agreed that RMB135 million (representing approximately 45% of the RMB300 million consideration), would be withheld and subject to achievement of an aggregate RMB83.45 million in total net profit being attributable to owners of the Target Company for 2021, 2022 and 2023. This earn-out provision better ensures that the actual consideration paid is more reflective of the true value of the Target Company to the Group and better protects the Company and its Shareholders.

The Company would like to clarify that the agreed formula to be applied at the end of year 2023, originally stated on page 6 under the heading "Profit guarantee", should be:

$$\left(1 - \frac{\text{Accumulated Audited Net Profit of the three Performance Guarantee Years}}{\text{Total Guaranteed Net Profit of the three Performance Guarantee Years}}\right) * \text{Total consideration of RMB300 million}$$

On page 7 under the heading "Profit guarantee" it was stated that the parties had agreed that in any Performance Guaranteed Year, if the Audited Net Profit is not less than ninety-five percent (95%) of the Guaranteed Net Profit, the Target Company shall be deemed to have achieved the guaranteed profit. The Company supplements that this provision is in recognition of the potential ordinary course variability in the Target Company's financial performance in the coming years, including due to potential unforeseen circumstances, force majeure events or COVID-19. We consider this arrangement to be commercially reasonable and in the best interests of the Company as the agreed level of Guaranteed Net Profit remains the commercial expectation and it is important and more beneficial for the Company to keep a higher benchmark for the purposes of business evaluation and personnel performance evaluation.

On page 7 under the heading “Profit guarantee” it was stated that if Beijing Company cannot carry out its Principal Business for the year ending 31 December 2021 due to a force majeure event (including COVID-19), each Performance Guaranteed Year may be postponed for one year at the request of the Founder. The Company would like to clarify that in such an event, the Guaranteed Net Profit amounts and corresponding compensation arrangements will instead apply to 2022, 2023 and 2024, respectively. Such flexibility was agreed to after extensive commercial negotiations as, given the uncertain long-tail impact of COVID-19, it was difficult to anticipate the precise impact on operations for 2021. If the Beijing Company were unable to carry out its’ Principal Business in 2021, it is expected that the net profit of the Target Company would be significantly less than Guaranteed Net Profit of RMB24 million. Nevertheless, it was commercially agreed that in such worst case scenario, it is in our interest to delay the Performance Guaranteed Years rather than to forego the investment and expansion opportunity presented by the Acquisition. Moreover, as this would also delay payment of the consideration, for which satisfaction of the profit guarantee is a condition precedent, any such postponement has limited impact on the Company financially.

By order of the Board
Cathay Media and Education Group Inc.
Pu Shulin
Chairman and executive Director

Hong Kong, 28 January 2021

As at the date of this announcement, the executive Directors are Mr. Pu Shulin, Mr. Sun Haitao, Mr. Wu Ye and Mr. Yan Xiang, and the independent non-executive Directors are Mr. Zhang Jizhong, Mr. Lee Cheuk Yin Dannis and Mr. Huang Yu.