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## INDUSTRY OVERVIEW

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*The information that appears in this section has been prepared by Frost & Sullivan and reflects estimates of market conditions based on publicly available sources and is prepared primarily as a market research tool. References to Frost & Sullivan Report should not be considered as the opinion of Frost & Sullivan as to the value of any security or the advisability of investing in us. Our Directors believe that the sources of information contained in this section are appropriate sources for such information and have taken reasonable care in reproducing such information. Our Directors have no reason to believe that such information is false or misleading or that any material fact has been omitted that would render such information false or misleading. The information prepared by Frost & Sullivan and set out in this section has not been independently verified by us, the Sole Sponsor, the [REDACTED], the [REDACTED], the [REDACTED], the [REDACTED](s) or any other party or affiliate involved in the [REDACTED] and neither they give any representations as to its accuracy and the information should not be relied upon in making, or refraining from making, any investment decision.*

### SOURCE OF INFORMATION

We have commissioned Frost & Sullivan, an Independent Third Party, to conduct a study of, and to produce a report on, the Japanese animation content distribution market and the entertainment and character IP licensing market in the PRC (“**Frost & Sullivan Report**”). Entertainment and character IP licensing refers to the licensing of IP properties of five major categories, namely animation, comics, films, TV shows and other online entertainment IP. We agreed to pay Frost & Sullivan a fee of HK\$488,000 for the preparation of the Frost & Sullivan Report, and our Directors consider that such fee reflects market rates.

The methodology used by Frost & Sullivan in gathering the relevant market data in compiling the Frost & Sullivan Report included secondary research and primary interviews. Secondary research involves information integration of data and publication from publicly available resources, including official data and announcements from PRC government departments, market research on industry, and enterprise player information issued by our chief competitors. Primary interviews are conducted with relevant institutions to obtain objective and factual data and prospective predictions. Frost & Sullivan considers the source of information as reliable because (i) it is general market practice to adopt official data and announcements from various PRC government departments; and (ii) the information obtained from interviews is for reference only and the findings in the Frost & Sullivan Report are not just based on the results of these interviews. Frost & Sullivan has proven track records in providing market research studies for government departments/agencies and private clients in the regions where the Frost & Sullivan Report covers.

Frost & Sullivan is a global consulting company founded in 1961 in New York and has over 40 global offices with more than 1,800 industry consultants, market research analysts, technology analysts and economists. Frost & Sullivan’s services include technology research, independent market research, economic research, corporate best practices advising, training, customer research, competitive intelligence and corporate strategy. Frost & Sullivan has three offices in the PRC and direct access to the most knowledgeable experts and market participants in the Japanese animation content distribution and entertainment and character IP licensing industry.

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Frost & Sullivan conducts research on market size, share and segmentation analyses, competitor tracking and corporate intelligence, etc. Some of the information extracted from the Frost & Sullivan Report are also referred to in the sections headed "Summary," "Business" and "Financial information" in this document. Our Directors confirm that, to the best of their knowledge, there is no adverse change in the market information since the date of the Frost & Sullivan Report which may qualify, contradict or have an impact on the information in this section.

Except as otherwise noted, all of the data and forecasts contained in this section are derived from the Frost & Sullivan Report, various official government publications and other publications.

### **ASSUMPTIONS USED IN THE FROST & SULLIVAN REPORT**

In compiling and preparing the Frost & Sullivan Report, Frost & Sullivan has adopted the following assumptions: (i) the economy of the PRC is assumed to maintain steady growth across the forecast period; (ii) the social, economic and political environments of the PRC are likely to remain stable in the forecast period, which ensure the stable and healthy development of the Japanese animation content distribution market and the entertainment and character IP licensing market; and (iii) there is no war or large scale disaster in the regions where our Group operates its business during the forecast period.

### **RELIABILITY OF INFORMATION IN THE FROST & SULLIVAN REPORT**

Our Directors, after making reasonable enquiries, are of the view that the sources of information used in this section are reliable as the information was extracted from the Frost & Sullivan Report. Our Directors believe that the Frost & Sullivan Report is reliable and not misleading as Frost & Sullivan is an independent professional research agency with extensive experience in its profession.

### **ANALYSIS ON THE JAPANESE ANIMATION CONTENT DISTRIBUTION MARKET IN THE PRC**

Animation content refers to all forms of animated media including traditional animation, live-action TV and live-action movie based on animations or comics.

Japan leads the market of animation content. The earliest commercial Japanese animation dates to 1917. Since then the market has steadily developed. Since 1980s, animation became increasingly accepted in the mainstream in Japan. The market witnessed a boom and became more influential in overseas markets.

The market of Japanese animation in the PRC boomed in 1990s. However, the market shrank in 2000s due to the limitation of distribution of overseas animation imposed by the State Administration of Radio Film and Television. The renaissance of Japanese animation started since 2015, mainly credited to the development of online broadcasting and the booming of the distribution of foreign films.

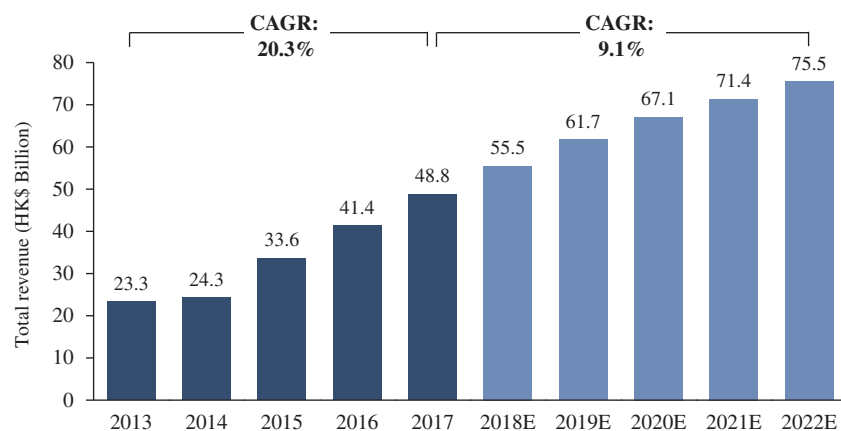
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### MARKET SIZE OF THE JAPANESE ANIMATION CONTENT DISTRIBUTION MARKET

The revenue of Japanese animation content distribution in the global market increased in the past several years, mainly due to the development of theatrical animation market and the growing popularity of Japanese animation in the PRC and overseas markets. The global market increased from HK\$23.3 billion in 2013 to HK\$48.8 billion in 2017, showing a CAGR of 20.3% during the period.

Going forward, the global market is expected to keep growing at a CAGR of 9.1%, reaching HK\$75.5 billion in 2022. The global market is forecast to be driven by the fast developing overseas markets.

**Total revenue of the Japanese animation content distribution global market  
2013 – 2022E**



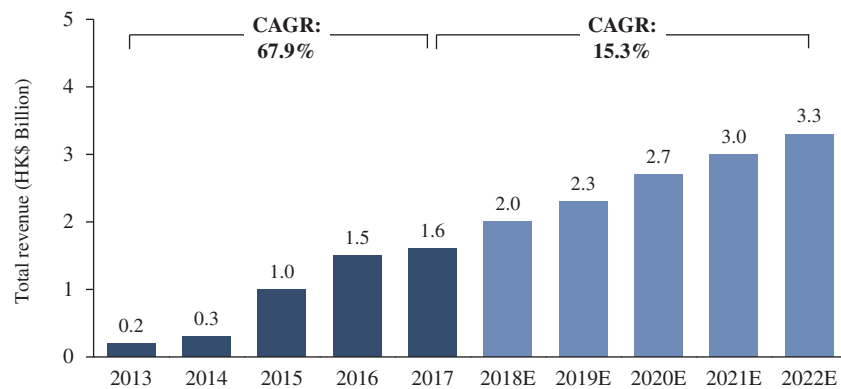
Source: Frost & Sullivan

The distribution market of Japanese animation content in the PRC witnessed a sharp growth from 2013 to 2017, mainly due to the growing awareness of IP protection in the PRC. Foreign content including animation content could not be broadcasted neither on TV nor online without the relevant TV drama distribution licence. In recent years, content without licences of broadcasting were forced to be removed from the online video sites. An increasing number of online video sites started to purchase licences and paid content are more widely accepted among audiences in the PRC. Also, the licensing fee kept an growing trend in recent years and is likely to continue growing in the following several years.

On the other hand, the growth of the market in the PRC is forecast to slow down in the coming several years due to the standardization of the market. The total revenue of the market is expected to grow from HK\$1.6 billion in 2017 to HK\$3.3 billion in 2022 at a CAGR of 15.3%.

## INDUSTRY OVERVIEW

### Total revenue of the Japanese animation content distribution market in the PRC, 2013 – 2022E



Source: Frost & Sullivan

### MARKET DRIVERS OF THE JAPANESE ANIMATION CONTENT DISTRIBUTION MARKET

**Boosting anime, comic and games (ACG) market:** the ACG market in the PRC witnessed a fast growth during the past several years. The total revenue of the PRC’s ACG industry grew from approximately HK\$105 billion in 2013 to HK\$180 billion in 2017 with a CAGR of 14.5%. The developing ACG market has widened the access to animation content for a larger audience base. With constantly enlarging audience and user base, the growth of animation content distribution market is also expected to be well supported.

**Emerging media channels:** the economic development is expected to continue bringing about media development, which supports expanded distribution of animation content. The explosion of new media channels, such as Internet and mobile phones, has significantly reformed the whole ACG industry in the PRC. The main streaming platform of animation is transferring from traditional TV to the Internet. The growing number of online video websites and the prevalence of mobile devices like smartphones, tablet PC and e-book enable wider, further, and more efficiently spread of animation content.

**Increasing interest in Japanese animation:** Japanese culture has gained its popularity in the PRC. The number of Chinese tourists visiting Japan increased from 2.1 million in 2013 to 9.6 million in 2017 with a CAGR of 46.9% during the period, showing a growing interest of Chinese people towards Japanese culture. Also, being the origin of animation culture, Japanese animation plays an important role in world’s animation industry. In line with the growing interest towards Japanese culture, the popularity of Japanese animation is expected to increase in the PRC.

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### ENTRY BARRIERS TO THE JAPANESE ANIMATION CONTENT DISTRIBUTION MARKET

**Capital support:** a large amount of initial capital is necessary for purchasing licences of content and marketing when entering the market of animation content distribution. This kind of investment is durative rather than one-time since the companies need to purchase licences for new content constantly in order to be competitive in the market. Minimum guarantee is needed when obtaining licence, and this kind of minimum guarantee is generally set at a high level. Some of the minimum guarantee is higher than the interest of the content. Minimum guarantee is usually paid in cash and hence a large amount of cash is needed for companies in the market. Therefore, it is difficult for new entrants without strong and continual capital support to enter and survive in the market.

**Stable relationship with producers:** existing distributors generally have established stable relationship with content producers or owners, which ensure the stability of supply chain. For the market of Japanese animation content distribution, it is not easy for new entrants to compete with existing brands with high reputation to establish network with overseas upstream players and obtain licences or distributorships from them.

**Business network:** established business network and customer relationship can be regarded as a barrier for new entrants in Japanese animation distribution market in the PRC since the downstream market is relatively concentrated as the number of major players is less than 10. Mutual reliance has been developed between distributors with high brand recognition and reputation and their customers. Existing players have already set up stable business networks with key customers based on years of accumulation of trust and good working relationship. Customers also tend to engage distributors who have good track records and more variety of content licence. Thus it is relatively difficult for new entrants to challenge incumbent players and develop their business networks in the initial development stage.

**Industry knowhow:** leading players in the market have gained a deep industry knowhow through years of operation. With the experience gained in the market, the players are able to follow the latest market trend and select high quality content and thus ensure the distribution of the content. It would not be easy for new entrants without such industry knowhow to deal with the process from selecting content to final distribution.

### OPPORTUNITIES AND THREATS OF THE JAPANESE ANIMATION CONTENT DISTRIBUTION MARKET

#### Opportunities

**Developing Japanese animation movie market:** compared with the market of TV animation series, the market of theatrical animation is still underdeveloped in the PRC. The market of Japanese theatrical animation witnessed a sharp growth in recent years. Unlike the TV animation series, whose production minutes stayed at a relatively stable level, the production of Japanese animation movie continued to grow in recent years. The growing production and the increasing popularity of Japanese animation movie is expected to drive the Japanese animation content distribution market in the PRC.

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**Standardisation of the market:** The market of Japanese animation content broadcasting in the PRC faced a transformation in recent years. An increasing number of video sites purchase licences to enrich content offer at their sites. As the market is getting more standardised in the coming future, the distribution of content licences will gain its importance in the PRC.

### Threats

**Development of domestic animation content:** during the past several years, domestic animation witnessed a growth in the PRC due to the favorable policy environment. With the support from the PRC government, investment in the industry of domestic animation increased and the production significantly grew during the period. The development of domestic animation content may have an impact on the distribution of foreign content including Japanese animation content.

## ANALYSIS ON THE ENTERTAINMENT AND CHARACTER IP LICENSING MARKET IN THE PRC

IP licensing refers to process of licensing a trademark or copyrighted property to extend the use in association with products, services and promotions. The properties could contain various IP types in different nature such as an animated character, a company logo, a song, a fashion brand, etc. Based on IP type, entertainments and character IP licensing can be divided into five major categories: animation, comics, films, TV shows and other online entertainment IP.

IP licensing usually involves two business entities in a contractual licensing agreement: (1) IP licensor or IP licensing agent; and (2) the licensee. The prospective licensee basically pays royalty, fixed at a rate against sales, recoupable against minimum guarantee paid upon the entering the licensing agreement, to IP licensor or IP licensing agent in exchange of the right to use the IP in its products, services or promotions during an agreed time period in a defined geographical area.

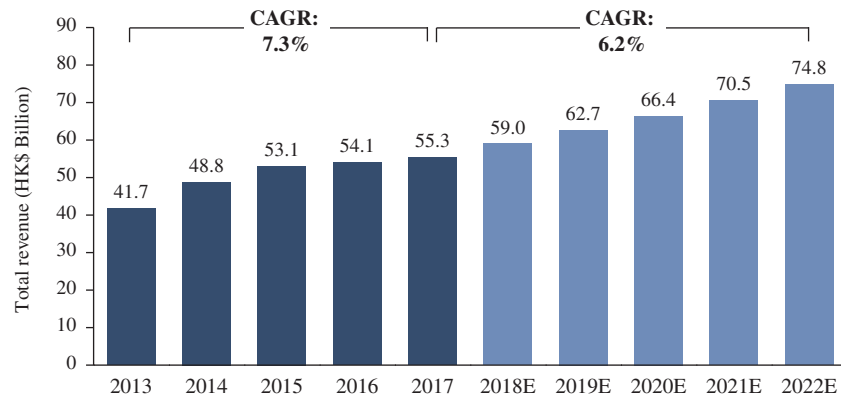
## MARKET SIZE OF THE ENTERTAINMENT AND CHARACTER IP LICENSING MARKET

The global market of entertainment and character IP licensing has grew steadily over the past five years. The total revenue generated by the entertainment and character IP licensing business has increased from HK\$41.7 billion in 2013 to HK\$55.3 billion in 2017, representing a CAGR of approximately 7.3%. The U.S. is the world’s largest entertainment and character IP licensing market, taking over 50% of market share.

Going forward, the market is expected to keep stable growth pace at a CAGR around 6.2%, reaching HK\$74.8 billion in 2022. The U.S. is most likely to remain the largest market of entertainment and character IP licensing market in a long time period.

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### Total revenue of the entertainment and character IP licensing global market, 2013 – 2022E

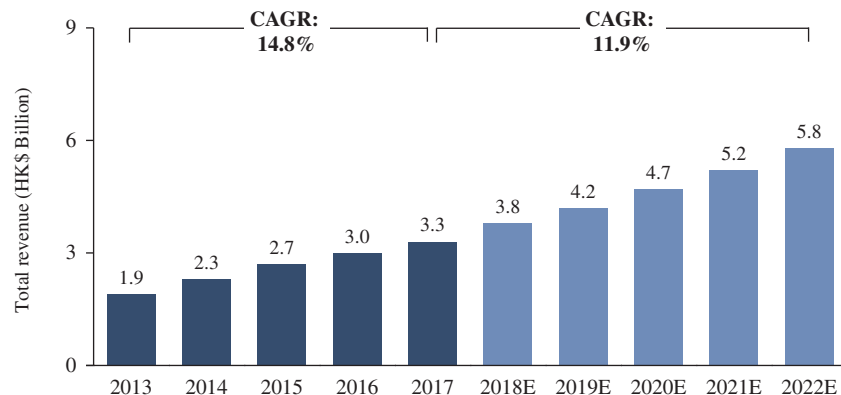


Source: Frost & Sullivan

In 2017, the PRC was the fourth largest market in the entertainment and character IP licensing market and had approximately 3.3% market share in the world. Driven by the increasing consumption ability of consumers in the PRC, the entertainment and character IP licensing market in the PRC has witnessed rapid development in the past five years. The total revenue generated from the entertainment and character IP licensing business has increased from HK\$1.9 billion in 2013 to HK\$3.3 billion in 2017 with a CAGR of 14.8%.

Going forward, the increasing awareness of the importance of IP merchandising to licensors and licensees will also promote the development of the PRC market. The total revenue of the entertainment and character IP licensing market is likely to grow at a CAGR of 11.9% from HK\$3.3 billion in 2017 and to reach HK\$5.8 billion in 2022.

### Total revenue of the entertainment and character IP licensing market in the PRC, 2013 – 2022E



Source: Frost & Sullivan



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### MARKET DRIVERS OF THE ENTERTAINMENT AND CHARACTER IP LICENSING MARKET

**Consumption upgrade:** along with the steady development of macro economy, the per capita annual disposal income of PRC urban households has increased from RMB26,955 in 2013 to RMB36,396 in 2017, representing a CAGR of 7.8%. Benefiting from the increasing disposal income, both the consumption level and consuming concept had evolved. Consumers are increasingly paying attention to the consumption in more value-added products, such as IP licensing products. Consumption upgrade has become a key driver for the development of the entertainment and character IP licensing market in the PRC.

**Large number of IP fans:** over the past years, the prevalence of fan economy in the PRC has further driven the development of the entertainment and character IP licensing market. Particular IPs including animation characters, music and sports team can easily accumulated large number of fans, which had become the main consumption power of IP derivative products or services. IP licensed products in the form of apparels, toys, fashion accessories and games are increasingly market preferred by the large number of IP fans.

**Increasing demand from downstream licensees:** IP licensing is a high value-added practice for downstream licensees, especially in the animation and comics industry. By licensing the IP rights for use in conjunction with their products or services, the licensees are more likely to sell more of their products or attach their products to their emotion generated by the IP. The increasing demand from downstream licensees is expected to further drive the entertainment and character IP licensing market.

### ENTRY BARRIERS TO THE ENTERTAINMENT AND CHARACTER IP LICENSING MARKET

**Capital barriers:** since an IP usually has a high value, a licensing distributor needs to invest large amount of money to acquire the trademark or copyright licence from the IP owner. As the business scale expands, a licensing distributor requires more capital to acquire more IP licence types. New entrants to the market have invest vast amount of money to be competitive in the entertainment and character IP licensing market.

**Upstream IP resources:** the amount of IP resources determines the core competitiveness of market players in the entertainment and character IP licensing market. The IP image, IP influence and IP quality are the determining factors on the marketing effects for the downstream licensees. Licensees are more likely to enter contractual agreement with those licensing distributors who have high quality IP resources.

**Brand recognition:** market players have established a well-known brand names through long-term cooperation with licensors. IP owners are increasingly willing to license their IPs to licensing distributors with good brand names, which are also recognized by downstream licensees.

**Professional expertise:** a qualified licensing distributor should not only be able to integrate both upstream and downstream resources in the industry, but also has deep know-how in the IP derivative market to maximise the value-added services through IP licensing.



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### OPPORTUNITIES AND THREATS OF THE ENTERTAINMENT AND CHARACTER IP LICENSING MARKET

#### Opportunities

***Increasing concentration level:*** at the moment, the Hong Kong entertainment and character IP licensing market is rather fragmented with many medium-to-small licensing distributors. With the increasing awareness of intellectual properties, the entertainment and character IP licensing market is expected to become more concentrated through merge and acquisition activities. The concentration level of the entertainment and character IP licensing market in the PRC is likely to increase in the coming years.

***E-commerce:*** the rapid development of e-commerce has presented new growth opportunities for the entertainment and character IP licensing market. IP licensed products are no longer limited to traditional offline sales channel, but are increasingly sold through e-commerce platforms. As young people are more used to e-commerce and popular IPs such as animation usually attract more young fans, e-commerce is likely to be the major sales channel and it will gain more market shares in retailers.

#### Threats

***Lower respect of IP rights:*** although the entertainment and character IP licensing market in the PRC has witnessed rapid growth over the past years, the relatively lower respect of IP rights threatened the healthy development of the market. Low priced copycat commodities greatly affected the economic benefits of licensees, licensing distributors and licensors.

***Lack of professional talents:*** professional talents are the key success factors to the licensing market. Except for the well-known brand name of IP, the accurate match between the licensors and licensees determines the effectiveness of IP licensing. An experienced professional is the link between licensors and licensees. However, there is a lack of such professional talents in the entertainment and character IP licensing market.

### COMPETITIVE LANDSCAPE

#### Japanese animation content distribution market

In terms of revenue, the top three players in the PRC together accounted for approximately 34.9% of the Japanese animation content distribution market in the PRC in 2017. The Company led the market and ranked number one among Japanese animation distributors in the PRC in terms of revenue in 2017 accounting for approximately 14.1% of the total market in the PRC.

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### Top three players of Japanese animation content distribution market by revenue in the PRC, 2017

Ranking	Company name	Market share (%)
1	Our Company	14.1
2	Company A	12.7
3	Company B	8.1
Top three		34.9
Others		65.1
Total		100.0

Source: Frost & Sullivan

- Notes:
1. Company A is a company established in Taiwan. Company A focuses on the distribution of animation content and also the IP licensing service.
  2. Company B is a company established in the PRC. Company B mainly provides services in the animation content distribution market, the entertainment and character IP licensing and digital business.

### Entertainment and character IP licensing market

At the end of 2017, there were approximately over 300 active IP licensors in the entertainment and character IP licensing market in the PRC. However, the number of licensing distributors was less than 100 due to shorter development history. At the moment, entertainment/character is the major IP type in the PRC's entertainment and character IP licensing, among which animation and comics characters are the most popular licensed category for licensing distributors in the PRC.

Company C, an American diversified multinational mass media and entertainment conglomerate, is the largest player in the entertainment and character IP licensing market in the PRC as of 2017. Company C directly licenses its own IP characters to downstream licensees without involving any distributors. The rest of the market is highly fragmented and our Company occupied nearly 0.2% market share in 2017 in terms of revenue in the PRC market.