*This announcement and the listing document referred herein is for informational purposes only as required by the Rules Governing the Listing of Securities on the Stock Exchange and do not constitute an offer to sell or acquire or the solicitation of an offer to buy any securities. Neither this announcement nor anything referred to herein (including the listing document) forms the basis for any contract or commitment whatsoever. For the avoidance of doubt, the publication of this announcement and the listing document referred to herein shall not be deemed to be an offer of securities made pursuant to a prospectus issued by or on behalf of the issuer for the purposes of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) of Hong Kong nor shall it constitute an advertisement, invitation or document containing an invitation to the public to enter into or offer to enter into an agreement to acquire, dispose of, subscribe for or underwrite securities for the purposes of the Securities and Futures Ordinance (Cap.571) of Hong Kong.*

*This announcement does not constitute an offer to sell or the solicitation of an offer to acquire, purchase or subscribe for any securities in the United States or in any other jurisdiction in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such jurisdiction.*

*Neither this announcement nor anything herein forms the basis for any contract or commitment whatsoever. Neither this announcement nor any copy hereof may be taken into or distributed in the United States or other jurisdiction in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such jurisdiction. The securities referred to herein have not been and will not be registered under the United States Securities Act of 1933, as amended, or with any securities regulatory authority of any state of the United States or other jurisdiction and may not be offered or sold in the United States, except pursuant to an applicable exemption from, or in a transaction not subject to, the registration requirements of the United States Securities Act of 1933, as amended, and applicable state or local securities laws. Any public offering of securities to be made in the United States will be made by means of a prospectus. Such prospectus will contain detailed information about the company making the offer and its management and financial statements. The Company does not intend to make any public offering of securities in the United States.*

# Xiaomi Best Time International Limited

*(incorporated in Hong Kong with limited liability)*

# US$855 MILLION ZERO COUPON CONVERTIBLE BONDS DUE 2027
# (the "Bonds")

**(Bond Stock Code: 40511)**

## unconditionally and irrevocably guaranteed by

**XIAOMI CORPORATION**
**小米集团**

*(A company controlled through weighted voting rights and incorporated in the Cayman Islands with limited liability)*

**(Stock Code: 1810)**

# PUBLICATION OF OFFERING CIRCULAR

This announcement is issued pursuant to Rule 37.39A of the Rules Governing the Listing of Securities (the "**Listing Rules**") on The Stock Exchange of Hong Kong Limited (the "**Stock Exchange**").

Please refer to the offering circular dated December 15, 2020 (the "**Offering Circular**") appended herein in relation to the issuance of the Notes. The Offering Circular is published in English only. No Chinese version of the Offering Circular has been published.

**Notice to Hong Kong investors:** Xiaomi Corporation (the "**Company**") and Xiaomi Best Time International Limited (the "**Issuer**") confirm that the Bonds are intended for purchase by professional investors only (as defined in Chapter 37 of the Listing Rules) and have been listed on the Stock Exchange on that basis. Accordingly, the Company and the Issuer confirm that the Bonds are not appropriate as an investment for retail investors in Hong Kong or elsewhere. Investors should carefully consider the risks involved.

The Offering Circular does not constitute a prospectus, notice, circular, brochure or advertisement offering to sell any securities to the public in any jurisdiction, nor is it an invitation to the public to make offers to subscribe for or purchase any securities, nor is it circulated to invite offers by the public to subscribe for or purchase any securities.

The Offering Circular must not be regarded as an inducement to subscribe for or purchase any securities of the Company, and no such inducement is intended. No investment decision should be made based on the information contained in the Offering Circular.

By order of the Board
**Xiaomi Corporation**
**Lei Jun**
*Chairman*

Hong Kong, December 18, 2020

*As at the date of this announcement, the directors of Xiaomi Best Time International Limited are Mr. Lin Bin and Mr. Chew Shou Zi.*

*As at the date of this announcement, the Board comprises Mr. Lei Jun as Chairman and Executive Director, Mr. Lin Bin as Vice-Chairman and Executive Director, Mr. Chew Shou Zi as Executive Director, Mr. Liu Qin as Non-executive Director, and Dr. Chen Dongsheng, Prof. Tong Wai Cheung Timothy and Mr. Wong Shun Tak as Independent Non-executive Directors*

# IMPORTANT NOTICE

**THIS OFFERING IS AVAILABLE ONLY TO INVESTORS WHO ARE PERSONS OUTSIDE OF THE UNITED STATES.**

**IMPORTANT: You must read the following disclaimer before continuing.** The following disclaimer applies to the attached offering circular (the "**Offering Circular**"). You are therefore advised to read this disclaimer carefully before accessing, reading or making any other use of the attached Offering Circular. In accessing the attached Offering Circular, you agree to be bound by the following terms and conditions, including any modifications to them from time to time, each time you receive any information from us as a result of such access. In order to review this Offering Circular or make an investment decision with respect to the securities, you must not be located in the United States.

**Confirmation of Your Representation:** The attached Offering Circular is being sent to you at your request and by accepting the e-mail and accessing the attached Offering Circular, you shall be deemed to represent to Credit Suisse (Hong Kong) Limited, Goldman Sachs (Asia) L.L.C., J.P. Morgan Securities plc and Morgan Stanley & Co. International plc (collectively, the "**Managers**") that (1) you are not in the United States and, to the extent you purchase the securities described in the attached Offering Circular, you will be doing so pursuant to Regulation S under the U.S. Securities Act of 1993, as amended (the "**Securities Act**") (2) the e-mail address that you gave us and to which this e-mail has been delivered is not located in the United States, its territories or possessions, (3) you consent to delivery of the attached Offering Circular and any amendments or supplements thereto by electronic transmission, (4) you (and any nominee and any person on whose behalf you are subscribing for the securities to which the attached Offering Circular relates) are not a "connected person" (as defined in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "**Listing Rules**")) of the issuer or the guarantor, which includes but is not limited to any director, chief executive or substantial shareholder of the issuer or the guarantor or any of their respective subsidiaries or any associate of any of them within the meaning of the Listing Rules, and (5) you (and any nominee and any person on whose behalf you are subscribing for the securities to which the attached Offering Circular relates) are, and will immediately after completion of the offering of such securities be, independent of and not acting in concert with, any of such connected persons in relation to the control of the issuer and the guarantor.

The attached Offering Circular has been made available to you in electronic form. You are reminded that documents transmitted via this medium may be altered or changed during the process of transmission and consequently none of the Managers, the Trustee (as defined in the attached Offering Circular) or the Agents (as defined in the attached Offering Circular) or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them accepts any liability or responsibility whatsoever in respect of any discrepancies between the document distributed to you in electronic format and the hard copy version. We will provide a hard copy version to you upon request.

**Restrictions:** The attached document is an Offering Circular and is being furnished in connection with an offering exempt from registration under the Securities Act solely for the purpose of enabling a prospective investor to consider the purchase of the securities described herein. You are reminded that the information in the attached Offering Circular is not complete and may be changed.

**THE SECURITIES HAVE NOT BEEN, AND WILL NOT BE, REGISTERED UNDER THE SECURITIES ACT, OR THE SECURITIES LAWS OF ANY STATE OF THE UNITED STATES OR OTHER JURISDICTION AND THE SECURITIES MAY NOT BE OFFERED OR SOLD WITHIN THE UNITED STATES, EXCEPT PURSUANT TO AN EXEMPTION FROM, OR IN A TRANSACTION NOT SUBJECT TO, THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT AND APPLICABLE STATE OR LOCAL SECURITIES LAWS. THIS OFFERING IS MADE SOLELY IN OFFSHORE TRANSACTIONS PURSUANT THE SECURITIES ACT. NOTHING IN THIS ELECTRONIC TRANSMISSION CONSTITUTES AN OFFER OF SECURITIES FOR SALE IN ANY JURISDICTION WHERE IT IS UNLAWFUL TO DO SO.**

Nothing in this electronic transmission constitutes an offer or an invitation by or on behalf of the issuer or guarantor of the securities or the Managers, the Trustee or the Agents to subscribe for or purchase any of the securities described therein, and access has been limited so that it shall not constitute in the United States or elsewhere a general solicitation or general advertising (as those terms are used in Regulation D under the Securities Act) or directed selling efforts (within the meaning of Regulation S under the Securities Act). If a jurisdiction requires that the offering be made by a licensed broker or dealer and the Managers or any affiliate of the Managers is a licensed broker or dealer in that jurisdiction, the offering shall be deemed to be made by the Managers or such affiliate on behalf of the issuer in such jurisdiction.

You are reminded that you have accessed the attached Offering Circular on the basis that you are a person into whose possession the attached Offering Circular may be lawfully delivered in accordance with the laws of the jurisdiction in which you are located and you may not nor are you authorized to deliver the attached, electronically or otherwise, to any other person. If you have gained access to this transmission contrary to the foregoing restrictions, you are not allowed to purchase any of the securities described in the attached Offering Circular.

**Actions that You May Not Take:** If you receive the attached document by e-mail, you should not reply by e-mail to this announcement, and you may not purchase any securities by doing so. Any reply e-mail communications, including those you generate by using the "**Reply**" function on your e-mail software, will be ignored or rejected.

**YOU ARE NOT AUTHORIZED TO AND YOU MAY NOT FORWARD OR DELIVER THE ATTACHED OFFERING CIRCULAR, ELECTRONICALLY OR OTHERWISE, TO ANY OTHER PERSON OR REPRODUCE SUCH OFFERING CIRCULAR IN ANY MANNER WHATSOEVER. ANY FORWARDING, DISTRIBUTION OR REPRODUCTION OF THE ATTACHED OFFERING CIRCULAR IN WHOLE OR IN PART IS UNAUTHORIZED. FAILURE TO COMPLY WITH THIS DIRECTIVE MAY RESULT IN A VIOLATION OF THE SECURITIES ACT OR THE APPLICABLE LAWS OF OTHER JURISDICTIONS.**

**You are responsible for protecting against viruses and other destructive items.** If you receive this document by e-mail, your use of this e-mail is at your own risk and it is your responsibility to take precautions to ensure that it is free from viruses and other items of a destructive nature.

**OFFERING CIRCULAR** **CONFIDENTIAL**

# Xiaomi Best Time International Limited

*(incorporated in Hong Kong with limited liability)*

## U.S.$855,000,000 Zero Coupon Guaranteed Convertible Bonds due 2027
## unconditionally and irrevocably guaranteed by

# XIAOMI CORPORATION
# 小米集团

*(A company controlled through weighted voting rights and incorporated in the Cayman Islands with limited liability)*
*(Stock Code: 1810)*

**Issue Price: 105.25 per cent.**

The U.S.$855,000,000 in an aggregate principal amount of zero coupon guaranteed convertible bonds due 2027 (the "**Bonds**", which term shall include, unless the context requires otherwise, any further bonds issued in accordance with the terms and conditions of the Bonds set out in "*Terms and Conditions of the Bonds*" (the "**Conditions**" and each of the Conditions, a "**Condition**"), will be issued by Xiaomi Best Time International Limited (the "**Issuer**"), a direct wholly-owned subsidiary of Xiaomi Corporation 小米集团 (the "**Guarantor**" or the "**Company**"). The due payment of all sums expressed to be payable by the Issuer under the Trust Deed (as defined in the Conditions) and the Bonds have been unconditionally and irrevocably guaranteed (the "**Guarantee**") by the Guarantor. The issue price of the Bonds shall be 105.25 per cent. of the aggregate principal amount of the Bonds and the denomination of each Bond shall be U.S.$200,000 and integral multiples of U.S.$100,000 in excess thereof.

The Bonds will, upon issue, constitute direct, unconditional, unsubordinated and (subject to Condition 4(a) of the Conditions) unsecured obligations of the Issuer and shall at all times rank *pari passu* and without any preference or priority among themselves. The payment obligations of the Issuer under the Bonds and the obligations of the Guarantor under the Guarantee shall, save for such exceptions as may be provided by mandatory provisions of applicable legislation and subject to Condition 4(a) of the Conditions, at all times rank at least equally with all of their respective other present and future unsecured and unsubordinated obligations.

Each Bond will, at the option of the holder, be convertible (unless previously redeemed, converted or purchased and canceled) on or after January 27, 2021 up to the close of business on the date falling 10 days prior to the Maturity Date (as defined below) (both days inclusive) (but, except as provided in the Conditions, in no event thereafter) into class B ordinary shares in the share capital of the Guarantor with a par value of U.S.$0.0000025 each, conferring a holder of a class B share one vote per share on any resolution tabled at the Guarantor's general meetings (the "**Class B Shares**") credited as fully paid at an initial conversion price of HK$36.74 per Class B Share (the "**Conversion Price**"). The Conversion Price is subject to adjustment in the circumstances described under "*Terms and Conditions of the Bonds – Conversion – Adjustment to Conversion Price*". The Closing Price (as defined in the Conditions) of the Class B Shares on The Stock Exchange of Hong Kong Limited (the "**Hong Kong Stock Exchange**") on December 1, 2020 was HK$26.15 per Class B Share.

Unless previously redeemed, converted or purchased and canceled as provided in the Conditions, the Issuer will redeem each Bond at its principal amount on December 17, 2027 (the "**Maturity Date**"). The Bonds may be redeemed, at the option of the Issuer, in whole, but not in part, at any time, on the date specified in the Tax Redemption Notice (as defined in the Conditions) for redemption at their principal amount, in the event of certain changes to the laws and regulations of Hong Kong, the Cayman Islands or the PRC or, in any such case, any political subdivision or any authority thereof or therein having power of tax, subject to the non-redemption option of each Bondholder after the exercise by the Issuer of its tax redemption option as described in the Conditions. The Bonds may be redeemed by the Issuer, in whole, but not in part, on the date specified in the Optional Redemption Notice (as defined in the Conditions) at their principal amount (i) at any time after December 17, 2025 provided that the Closing Price of a Class B Share (translated into U.S. dollars at the Prevailing Rate (as defined in the Conditions)) for 20 out of 30 consecutive Trading Days (as defined in the Conditions), the last of which occurs not more than five Trading Days prior to the date of the relevant Optional Redemption Notice, was at least 130 percent. of the Conversion Price (translated to U.S. dollars at the Fixed Exchange Rate (as defined in the Conditions)) then in effect immediately prior to the date upon which notice of such redemption is given; or (ii) at any time if, immediately prior to the date the relevant Optional Redemption Notice is given, 90 per cent. or more in principal amount of the Bonds originally issued (which shall for this purpose include any further bonds issued in connection with Condition 17 of the Conditions) has already been converted, redeemed or purchased and canceled. The holder of each Bond will also have the right at such holder's option to require the Issuer to redeem all or some only of such holder's Bonds on the Relevant Event Put Date (as defined in the Conditions) at their principal amount, following the occurrence of (i) the Class B Shares ceasing to be listed or admitted to trading or being suspended from trading for a period equal to or exceeding 30 consecutive Trading Days on the Relevant Stock Exchange (as defined in the Conditions); (ii) a Change of Control (as defined in the Conditions); or (iii) (a) any Change in Law (as defined in the Conditions) that results in (x) the Group (as defined in the Conditions) (as in existence immediately subsequent to such Change in Law), as a whole, being legally prohibited from operating substantially all of the business operations conducted by the Group (as in existence immediately prior to such Change in Law) as of the last date of the period described in the Guarantor's consolidated financial statements for the most recent fiscal quarter and (y) the Guarantor being unable to continue to derive substantially all of the economic benefits from the business operations conducted by the Group (as in existence immediately prior to such Change in Law) in the same manner as reflected in the Guarantor's consolidated financial statements for the most recent fiscal quarter and (b) the Guarantor not having furnished to the Trustee, prior to the date that is 12 months after the date of the Change in Law, an opinion from an independent financial adviser or external legal counsel stating either (x) that the Guarantor is able to continue to derive substantially all of the economic benefits from the business operations conducted by the Group (as in existence immediately prior to such Change in Law), taken as a whole, as reflected in the Guarantor's consolidated financial statements for the most recent fiscal quarter (including after giving effect to any corporate restructuring or reorganization plan of the Guarantor) or (y) that such Change in Law would not materially adversely affect the Issuer's and the Guarantor's ability to make principal and premium (if any) payments on the Bonds when due or to convert the Bonds in accordance with the Conditions. See "*Terms and Conditions of the Bonds – Redemption, Purchase and Cancelation*".

For a detailed description of the Bonds, see "*Terms and Conditions of the Bonds*".

**PRIIPs REGULATION / PROHIBITION OF SALES TO EEA AND UK RETAIL INVESTORS** – The Bonds are not intended to be offered, sold or otherwise made available to and should not be offered, sold or otherwise made available to any retail investor in the European Economic Area ("**EEA**") or in the United Kingdom (the "**UK**"). For these purposes, a retail investor means a person who is one (or more) of: (i) a retail client as defined in point (11) of Article 4(1) of Directive 2014/65/EU (as amended, "**MiFID II**"); (ii) a customer within the meaning of Directive (EU) 2016/97 (the "**Insurance Distribution Directive**"), where that customer would not qualify as a professional client as defined in point (10) of Article 4(1) of MiFID II. Consequently no key information document required by Regulation (EU) No 1286/2014 (as amended, the "**PRIIPs Regulation**") for offering or selling the Bonds or otherwise making them available to retail investors in the EEA or in the UK has been prepared and therefore offering or selling the Bonds or otherwise making them available to any retail investor in the EEA or in the UK may be unlawful under the PRIIPS Regulation.

Application will be made to the Hong Kong Stock Exchange for (i) the listing of, and permission to deal in, the Bonds on the Hong Kong Stock Exchange by way of debt issues to professional investors (as defined in Chapter 37 of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (the "**Listing Rules**") ("**Professional Investors**") only; and (ii) the listing of, and permission to deal in, the Class B Shares issuable on conversion, and such permissions are expected to become effective on December 18, 2020 and when such Class B Shares are issued, respectively. This document is for distribution to Professional Investors only.

**Notice to Hong Kong investors: The Issuer and the Guarantor confirm that the Bonds are intended for purchase by Professional Investors only and will be listed on the Hong Kong Stock Exchange on that basis. Accordingly, the Issuer and the Guarantor confirm that the Bonds are not appropriate as an investment for retail investors in Hong Kong.**

**The Hong Kong Stock Exchange has not reviewed the contents of this Offering Circular, other than to ensure that the prescribed form disclaimer and responsibility statements, and a statement limiting distribution of this Offering Circular to Professional Investors only have been reproduced in this Offering Circular. Listing of the Bonds on the Hong Kong Stock Exchange in not to be taken as an indication of the commercial merits or credit quality of the Bonds or the Issuer or the Guarantor, or quality of disclosure in this Offering Circular. Hong Kong Exchanges and Clearing Limited and the Hong Kong Stock Exchange take no responsibility for the contents of this Offering Circular, 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 Offering Circular.**

The Guarantor has been assigned a rating of "Baa2" by Moody's Investors Services, Inc. ("Moody's"), "BBB-" by S&P Global Ratings ("S&P") and "BBB" by Fitch Ratings Inc. ("Fitch") and the Issuer has been assigned a rating of "Baa2" by Moody's. The Bonds are expected to be rated "Baa2" by Moody's. A credit rating is not a recommendation to buy, sell or hold securities and may be subject to revision, qualification, suspension, reduction or withdrawal at any time by the assigning rating agency.

**Investors should be aware that investing in the Bonds and the Guarantor's Class B Shares to be issued upon conversion of the Bonds involves certain risks. Further, investors should be aware that they will have limited anti-dilution protection and no rights as holders of the Class B Shares prior to the conversion of the Bonds, and that there are various other risks relating to the Bonds, the Issuer and its subsidiaries, the Guarantor and its subsidiaries, their business and their jurisdictions of operations which investors should familiarize themselves with before making an investment in the Bonds. See "*Risk Factors*" beginning on page 13 for a discussion of certain factors to be considered in connection with an investment in the Bonds. Investors should carefully consider the risks involved.**

**The Bonds, the Guarantee and the Class B Shares to be issued upon conversion of the Bonds have not been and will not be registered under the United States Securities Act of 1933, as amended (the "Securities Act") and, or other securities laws and, subject to certain exceptions, may not be offered or sold within the United States. The Bonds are being offered and sold only outside the United States in reliance on Regulation S under the Securities Act ("Regulation S"). For a description of these and certain further restrictions on offers and sales of the Bonds and the Class B Shares to be issued upon conversion of the Bonds and the distribution of this Offering Circular, see "*Subscription and Sale*".**

The Bonds will be represented by beneficial interests in a global certificate (the "**Global Certificate**") in registered form, which will be registered in the name of a nominee of, and shall be deposited on or about December 17, 2020 (the "**Issue Date**"), with a common depositary for, Euroclear Bank SA/NV ("**Euroclear**") and Clearstream Banking S.A.("**Clearstream**"). Beneficial interests in the Global Certificate will be shown on, and transfers thereof will be effected only through, records maintained by Euroclear and Clearstream. Except as described in the Global Certificate, certificates for Bonds will not be issued in exchange for interests in the Global Certificate.

*Managers*

**Credit Suisse** **Goldman Sachs (Asia) L.L.C.** **J.P. Morgan** **Morgan Stanley**

*(in alphabetical order)*

The date of this Offering Circular is December 15, 2020

## NOTICE TO INVESTORS

**This Offering Circular does not constitute an offer to sell to, or a solicitation of an offer to buy from, any person in any jurisdiction to whom it is unlawful to make the offer or solicitation in such jurisdiction. Neither the delivery of this Offering Circular nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the Issuer's or the Guarantor's affairs since the date of this Offering Circular or that the information contained in this Offering Circular is correct as of any time after that date.**

This Offering Circular includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Issuer, the Guarantor and the Bonds. Each of the Issuer and the Guarantor accepts full responsibility for the accuracy of the information contained in this document and confirms, having made all reasonable enquires, that to the best of its knowledge and belief there are no other facts the omission of which would make any statement herein misleading.

Each of the Issuer and the Guarantor, having made all reasonable enquiries, confirms that: (i) this Offering Circular contains all information with respect to the Issuer, the Guarantor and its direct and indirect subsidiaries, which are entities over which the Guarantor controls, including all of the entities through which the Guarantor conducts its operations in the PRC by way of contractual arrangements, the financial accounts of which have been consolidated and accounted for as if they were subsidiaries of the Guarantor (collectively, the "**Group**") and to the Class B Shares and the Bonds which is material in the context of the issue and offering of the Bonds; (ii) the statements contained in this Offering Circular relating to the Issuer, the Guarantor and to the Group are in all material respects true and accurate and not misleading; (iii) the opinions and intentions expressed in this Offering Circular with regard to the Issuer, the Guarantor and to the Group are honestly held, have been reached after considering all relevant circumstances and are based on reasonable assumptions; (iv) there are no other facts in relation to the Issuer, the Guarantor, the Group or the Guarantee, the Class B Shares or the Bonds the omission of which would, in the context of the issue and offering of the Bonds make any statement in this Offering Circular misleading; (v) all reasonable enquiries have been made by the Issuer and the Guarantor to ascertain such facts and to verify the accuracy of all such information and statements in the Offering Circular and (v) this Offering Circular does not include any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements herein, in light of the circumstances under which they were made, not misleading. Each of the Issuer and the Guarantor accepts responsibility accordingly.

This Offering Circular is highly confidential. The Issuer and the Guarantor are providing it solely for the purpose of enabling the investors to consider a purchase of the Bonds. Investors should read this Offering Circular before making a decision whether to purchase the Bonds. Investors must not use this Offering Circular for any other purpose, or disclose any information in this Offering Circular to any other person.

The Issuer and the Guarantor have prepared this Offering Circular and are jointly and severally responsible for its contents. Investors are responsible for making their own examination of the Group and their own assessment of the merits and risks of investing in the Bonds. By purchasing the Bonds, investors will be deemed to have acknowledged that they have made certain acknowledgements, representations and agreements as set forth under the section entitled "*Subscription and Sale*" below.

No representation or warranty, express or implied, is made by Credit Suisse (Hong Kong) Limited, Goldman Sachs (Asia) L.L.C., J.P. Morgan Securities plc and Morgan Stanley & Co. International plc (collectively, the "**Managers**"), the Trustee (as defined in the Conditions) or the Agents (as defined in the Conditions) or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them as to the accuracy, completeness or sufficiency of the information contained in this Offering Circular, and nothing contained in this Offering Circular is, or shall be relied upon as, a promise, representation or warranty by the Managers, the Trustee or the Agents or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them. None of the

Managers, the Trustee or the Agents or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them has independently verified any of the information contained in this Offering Circular and none of them can give any assurance that this information is accurate, truthful or complete. This Offering Circular is not intended to provide the basis of any credit or other evaluation nor should it be considered as a recommendation by the Issuer, the Guarantor, the Managers, the Trustee or the Agents or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them that any recipient of this Offering Circular should purchase the Bonds. Each potential purchaser of the Bonds should determine for itself the relevance of the information contained in this Offering Circular and its purchase of the Bonds should be based upon such investigations with its own tax, legal and business advisers as it deems necessary. To the fullest extent permitted by law, none of the Managers, the Trustee or the Agents or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them accepts any responsibility for the contents of this Offering Circular or for any other statement, made or purported to be made by or on behalf of the Managers, the Trustee or the Agents or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them in connection with the Group, the Bonds, the Guarantee or the Class B Shares. Each of the Managers, the Trustee and the Agents and each of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents and advisers and each person who controls any of them disclaims all and any liability whether arising in tort or contract or otherwise (save as referred to above) which it might otherwise have in respect of this Offering Circular or any such statement.

In making an investment decision, investors must rely on their own examination of the Group and the terms of the offering, including the merits and risks involved. See "*Risk Factors*" for a discussion of certain factors to be considered in connection with an investment in the Bonds.

Each person receiving this Offering Circular acknowledges that: (i) such person has been afforded an opportunity to request from the Issuer and the Guarantor and to review, and has received, all additional information considered by it to be necessary to verify the accuracy of, or to supplement, the information contained herein; (ii) such person has not relied on the Managers, the Trustee or the Agents or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them in connection with any investigation of the accuracy of such information or its investment decision; (iii) no person has been authorized to give any information or to make any representation concerning the Group, the Bonds, the Guarantee or the Class B Shares (other than as contained herein and information given by the Issuer's or the Guarantor's duly authorized officers and employees in connection with investors' examination of the Group and the terms of the offering of the Bonds) and, if given or made, any such other information or representation should not be relied upon as having been authorized by the Issuer, the Guarantor, the Managers, the Trustee or the Agents or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them; (iv) such person (and any nominee and any person on whose behalf such person is subscribing for the Bonds) is not a "connected person" (as defined in the Listing Rules) of the Issuer or the Guarantor, which includes but is not limited to any director, chief executive or substantial shareholder of the Issuer or the Guarantor or any of their respective subsidiaries or any associate of any of them within the meaning of the Listing Rules; and (v) such person (and any nominee and any person on whose behalf such person is subscribing for the Bonds) is, and will immediately after completion of the offering of the Bonds be, independent of and not acting in concert with, any of such connected persons in relation to the control of the Issuer or the Guarantor.

None of the Issuer, the Guarantor or the Managers is making an offer to sell the Bonds, in any jurisdiction except where an offer or sale is permitted. The distribution of this Offering Circular and the offering of the Bonds may in certain jurisdictions be restricted by law. Persons into whose possession this Offering Circular comes are required by the Issuer, the Guarantor and the Managers to inform themselves about and to observe any such restrictions. For a description of the restrictions on offers, sales and resales of the Bonds and distribution of this Offering Circular, see "*Subscription and Sale*" below.

None of the Issuer, the Guarantor, the Managers, the Trustee or the Agents or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them is making any representation to the investors regarding the legality of an investment in the Bonds by the investors under any legal, investment or similar laws or regulations. Investors should not consider any information in this Offering Circular to be legal, business or tax advice. Investors should consult their own professional advisers for legal, business, tax and other advice regarding an investment in the Bonds.

**PRIIPs Regulation/Prohibition of Sales to European Economic Area** ("**EEA**") **and UK Retail Investors** – The Bonds are not intended to be offered, sold or otherwise made available to and should not be offered, sold or otherwise made available to any retail investor in the EEA or in the United Kingdom (the "**UK**"). For these purposes, a retail investor means a person who is one (or more) of: (i) a retail client as defined in point (11) of Article 4(1) of Directive 2014/65/EU (as amended, "**MiFID II**"); and (ii) a customer within the meaning of Directive (EU) 2016/97 (the "**Insurance Distribution Directive**"), where that customer would not qualify as a professional client as defined in point (10) of Article 4(1) of MiFID II. Consequently, no key information document required by Regulation (EU) No 1286/2014 (the "**PRIIPs Regulation**") for offering or selling the Bonds or otherwise making them available to retail investors in the EEA or in the UK has been prepared and therefore offering or selling the Bonds or otherwise making them available to any retail investor in the EEA or in the UK may be unlawful under the PRIIPs Regulation.

***Singapore SFA Product Classification:*** *In connection with Section 309B of the Securities and Futures Act (Chapter 289) of Singapore (the "**SFA**") and the Securities and Futures (Capital Markets Products) Regulations 2018 of Singapore (the "**CMP Regulations 2018**"), the Issuer has determined, and hereby notifies all relevant persons (as defined in Section 309A(1) of the SFA), that the Bonds are 'prescribed capital markets products' (as defined in the CMP Regulations 2018) and Excluded Investment Products (as defined in MAS Notice SFA 04-N12: Notice on the Sale of Investment Products and MAS Notice FAA-N16: Notice on Recommendations on Investment Products).*

## CERTAIN DEFINED TERMS AND CONVENTIONS

In this Offering Circular, references to:

- "**AIoT**" are to artificial intelligence of things, the combination of artificial intelligence technologies with the internet of things infrastructure;

- "**AVC**" are to Beijing All View Cloud Data Technology Co., Ltd., a third-party market research firm;

- "**Company**," "**Guarantor**," "**we**," "**our**" and "**us**" are to Xiaomi Corporation, an exempted company with limited liability incorporated under the laws of the Cayman Islands;

- "**Canalys**" are to Canalys, a third-party market research firm;

- "**CEO**" are to the chief executive officer;

- "**CFO**" are to the chief financial officer;

- "**Class A Shares**" are to class A ordinary shares in the share capital of the Company with a par value of U.S.$0.0000025 each, conferring weighted voting rights in the Company such that a holder of a Class A Share is entitled to 10 votes per share on any resolution tabled at the Company's general meetings, save for resolutions with respect to any reserved matters as set out in amended and restated memorandum and articles of association of the Company, in which case they shall be entitled to one vote per share;

- "**Class B Shares**" are to class B ordinary shares in the share capital of the Company with a par value of U.S.$0.0000025 each, conferring a holder of a Class B Share one vote per share on any resolution tabled at the Company's general meetings;

- "**Group**" are to the Company, its subsidiaries, and its variable interest entities and their respective subsidiaries except as stated otherwise in "*Terms and Conditions of the Bonds*;"

- "**HK$**" and "**HK dollars**" are to Hong Kong dollars, the official currency of the Hong Kong Special Administrative Region of the People's Republic of China;

- "**Iaas**" are to infrastructure as a service, a standardized, highly automated offering, where compute resources, combined with networking and storage capabilities are owned and hosted by a service provider and offered to customers on-demand;

- "**IDC**" are to International Data Corporation, a third-party market research firm;

- "**IoT**" are to internet of things, the network of physical devices with information-sensing capabilities such as two-dimensional code reading, radio frequency identification, infrared sensors, global positioning systems and laser scanners to realize intelligent identification, positioning, tracking, monitoring and management;

- "**iResearch**" are to iResearch Consulting Group, a third-party market research firm;

- "**Issuer**" are to Xiaomi Best Time International Limited, a public company limited by shares incorporated under the laws of Hong Kong;

- "**MAU**" are to monthly active users, the number of devices that activate the app or operating system at least once during a given calendar month and, in the context of MIUI forum, refers to the number of registered users logging in our MIUI forum at least once during a given calendar month;

- "**MIUI**" are to our proprietary operating system built on the Android kernel;

- "**MOFCOM**" are to the Ministry of Commerce of mainland China;
- "**NDRC**" are to the National Development and Reform Commission of mainland China;
- "**Notes**" are to the US$600,000,000 3.375% senior notes due 2030 issued on April 29, 2020;
- "**Ordinary Shares**" are to the Class B Shares, the Class A Shares and any fully-paid and non-assessable shares of any class or classes of the ordinary shares of the Guarantor authorized after the Issue Date which have no preference in respect of dividends or of amounts payable in the event of any voluntary or involuntary liquidation or dissolution of the Guarantor;
- "**PaaS**" are to Platform as a service, a category of cloud computing services that provides a platform allowing customers to develop, run, and manage apps without the complexity of building and maintaining the infrastructure typically associated with developing and launching an app;
- "**PRC**" are to the People's Republic of China, excluding, for purposes of this definition, the Hong Kong Special Administrative Region, the Macau Special Administrative Region and Taiwan;
- "**provinces**" are to provinces and to provincial-level autonomous regions and municipalities in mainland China which are directly under the supervision of the central mainland China government;
- "**RMB**" or "**Renminbi**" are to the Renminbi, the official currency of mainland China;
- "**SAFE**" are to the State Administration of Foreign Exchange of mainland China;
- "**SEHK**" are to The Stock Exchange of Hong Kong Limited;
- "**SFC**" are to the Securities and Futures Commission of Hong Kong;
- "**SKU**" are to stock keeping unit;
- "**System-on-Chip (SoC)**" are to a circuit that integrates all components of a computer or other electronic systems;
- "**TWS**" are to true wireless stereo;
- "**US$**", "**U.S.$**" and "**U.S. dollars**" are to United States dollars, the official currency of the United States of America; and
- "**VIE(s)**" are to variable interest entity(ies).

Solely for your convenience, this Offering Circular contains translations of certain Renminbi amounts into U.S. dollar amounts at specified rates. Unless indicated otherwise, the translation of Renminbi amounts into U.S. dollar amounts has been made at the rate of RMB6.7896 to US$1.00, the exchange rate set forth in the H.10 statistical release (the "**Noon Buying Rate**") of the Board of Governors of the Federal Reserve System of the United States (the "**Federal Reserve Board**") on September 30, 2020. You should not construe these translations as representations that the Renminbi amounts could actually be converted into any U.S. dollar amounts at the rates indicated or at all.

Market data and certain industry forecasts and statistics in this Offering Circular have been obtained from both public and private sources, including market research, publicly available information and industry publications. In many cases, there is no readily available external information (whether from trade associations, government bodies or other organizations) to validate market-related analyzes and estimates, requiring us to rely on our own internally developed estimates regarding our industry, our position in the industry, our market and segment share and the market and segment shares of various industry participants based on experience, our own investigation of market conditions and our review of industry publications, including information made available to the public by our competitors. Although this information is believed to be reliable, it has not been independently verified by the Issuer, the Company, the Managers, the Trustee or the Agents or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them, and none of the Issuer, the Company, the Managers, the Trustee or the Agents or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them makes any representation as to the accuracy or completeness of that information. Such information may not be consistent with other information compiled within or outside of mainland China. In addition, third-party information providers may have obtained information from market participants and such information may not have been independently verified. This Offering Circular summarizes certain documents and other information, and investors should refer to them for a more complete understanding of what is discussed in those documents. In making an investment decision, each investor must rely on its own examination of the Issuer, the Company, the Group and the terms of the offering and the Bonds, including the merits and risks involved.

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## PRESENTATION OF FINANCIAL INFORMATION

Our audited consolidated financial information as at and for the years ended December 31, 2017, 2018 and 2019 included in this Offering Circular have been extracted from the Guarantor's audited consolidated financial statements as at and for the years ended December 31, 2018 and 2019 (the "**Audited Financial Statements**") and our unaudited but reviewed financial results as at and for the nine months ended September 30, 2019 and 2020 included in this Offering Circular have been extracted from the Guarantor's unaudited but reviewed financial results as at and for the nine months ended September 30, 2020 (the "**Interim Financial Results**").

The Audited Financial Statements have been audited by PricewaterhouseCoopers, Certified Public Accountants, Hong Kong ("**PwC**") and the Interim Financial Results have been reviewed by PwC, and are prepared in accordance with International Financial Reporting Standards ("**IFRS**"), which differ in certain respects from generally accepted accounting principles in the United States ("**U.S. GAAP**") and in certain other countries. We have made no attempt to describe or quantify the impact of those differences. In making an investment decision, investors must rely upon their own examination of us, the terms of the Bonds and the financial information we present herein. Potential investors should consult their own professional advisers for an understanding of the differences between IFRS and accounting principles generally accepted in other countries, including the United States, and how those differences might affect the financial information presented herein.

This Offering Circular contains non-IFRS financial measures and ratios that are not required by, or presented in accordance with, IFRS, including Adjusted Net Profit. We believe that the presentation of non-IFRS measures when shown in conjunction with the corresponding IFRS measures provides useful information to investors and management regarding financial and business trends in relation to our financial condition and results of operations, by eliminating any potential impact of items that our management does not consider to be indicative of our operating performance such as certain non-cash items and the impact of certain investment transactions. We also believe that the non-IFRS measures are appropriate for evaluating the Group's operating performance. However, the use of this particular non-IFRS measure has limitations as an analytical tool, and you should not consider it in isolation from, or as a substitute for analysis of, our results of operations or financial conditions as reported under IFRS. In addition, this non-IFRS financial measure may be defined differently from similar terms used by other companies and therefore may not be comparable to similar measures used by other companies. None of the Managers, the Trustee or the Agents or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them make any representation or warranty, express or implied, regarding the sufficiency of any unaudited figures in this offering circular. Potential investors must exercise caution when using such unaudited figures to evaluate the financial condition and results of operations of the Guarantor and its subsidiaries.

## FORWARD-LOOKING STATEMENTS

This Offering Circular includes "**forward-looking statements**". All statements other than statements of historical fact contained in this Offering Circular, including, without limitation, those regarding our future financial position and results of operations, strategy, plans, objectives, goals and targets, future developments in the markets where we participate or are seeking to participate, and any statements preceded by, followed by or that include the words "**believe**", "**expect**", "**aim**", "**intend**", "**will**", "**may**", "**anticipate**", "**seek**", "**should**", "**estimate**", "**target**" or similar expressions or the negative thereof, are forward-looking statements. These forward-looking statements involve known and unknown risks, uncertainties and other factors, some of which are beyond our control, which may cause its actual results, performance or achievements, or industry results to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. These forward-looking statements are based on numerous assumptions regarding our present and future business strategies and the environment in which we will operate in the future. Important factors that could cause our actual results, performance or achievements to differ materially from those in the forward-looking statements include, among others, the following:

- our operations and business prospects;
- our business and operating strategies and our ability to implement such strategies;
- our ability to develop and manage our operations and business;
- our future general and administrative expenses;
- competition for, among other things, capital, technology and skilled personnel;
- our ability to control costs;
- our dividend policy;
- changes to regulatory and operating conditions in the industry and geographical markets in which we operate; and

all other risks and uncertainties described in the section headed "*Risk Factors*."

Any forward-looking statement speaks only as of the date on which it is made, and we do not undertake any obligation to update any forward-looking statement or statements to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time and it is not possible for us to predict which will arise. In addition, we cannot access the impact of each factor on its business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

## SUMMARY

*This summary may not contain all of the information that may be important to you. You should read this entire Offering Circular before making an investment decision to purchase the Bonds.*

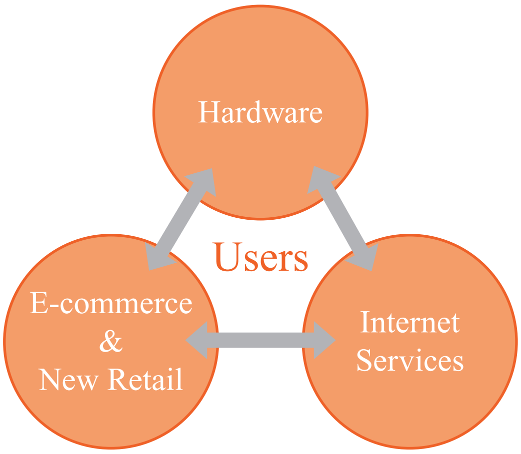
**Business Overview**

Xiaomi is an internet company with smartphones and smart hardware connected by an IoT platform at its core.

***Our Business Model***

Our Company is built on innovation and efficiency. As a company founded by engineers and designers, we embrace a culture of bold innovation to push the boundaries of what technology can offer. A spirit of innovation permeates our Company and guides everything we do. In addition, we are relentless in our pursuit of efficiency. We strive to achieve cost savings to deliver value back to our users.

Our unique and powerful "triathlon" business model comprises three synergistic pillars of growth – (i) innovative, high quality and well-designed hardware focused on exceptional user experience, (ii) highly efficient new retail distribution platform allowing for our products to be priced accessibly and (iii) engaging internet services.




*Hardware*

We offer a broad range of hardware products developed in-house or in collaboration with our ecosystem partners. Innovation, quality, design and user experience are ingrained in all of our products regardless of whether they are developed in-house or in collaboration with our partners. We strive to offer our products at price points that are accessible to the widest user base to enjoy broad adoption and high retention. For our core in-house products, we focus on designing and developing a range of cutting-edge hardware products including smartphones, laptops, smart TVs, AI speakers, smart routers, smart watches, smart refrigerators, smart washing machines and smart air conditioners.

We curate a wide range of additional products by investing in over 300 companies. This has enabled us to build one of the world's leading consumer IoT platforms. As of September 30, 2020, the number of connected IoT devices (excluding smartphones and laptops) on our AIoT platform reached 289.5 million, representing an increase of 35.8% year-over-year. This active and integrated suite of connected technology products enhances the lives of our users and constitutes a proprietary delivery platform for our internet services. We also curate a range of lifestyle products to further drive brand awareness and traffic to our sales points. For more information on our hardware products, see "Business – Hardware."

*New Retail*

Our highly efficient omni-channel new retail distribution platform is a core component of our growth strategy, allowing us to operate efficiently while simultaneously extending our user reach and enhancing our users' experience. Since inception, we have focused on direct online sales of our products to maximize efficiency and build a direct digital relationship with our users. We have continually expanded our direct offline retail network, for example, through our self-operated Mi Home stores. Moreover, to establish our offline new retail presence in lower-tier cities and rural areas of China, we have built a sizable authorized store network. Our offline retail network allows us to broaden our reach and provide a richer user experience, while maintaining similar efficiency and the same product prices as our online channels. Our efficient omni-channel sales strategy enables us to provide our products at accessible price points to the largest user base. For more information on our new retail platform, see "*Business – New Retail*."

*Internet Services*

We provide internet services to give our users a complete mobile internet experience. In September 2020, we had 368.2 million MAU on MIUI, our proprietary operating system built on the Android kernel. MIUI fully embraces the Android ecosystem, including all mobile apps. It functions as an open platform for us to deliver our wide range of internet services, such as content, entertainment, financial services and productivity tools. The connectivity between our devices and the seamless integration between smart hardware and internet services enable us to provide our users with better user experience. Furthermore, we have a proven track record of developing killer apps. Compared to other internet platforms that acquire new users at high costs, we leverage the sale of our hardware to acquire users at a profit. For more information on our internet services, see "*Business – Internet Services*."

*Network Effects*

Our unique and powerful triathlon business model comprises three synergistic pillars that are closely connected. We strive to offer killer products that are high quality, high performance, well designed and honestly priced. These products in turn bring additional traffic to our retail channels. We deliver our products to users at accessible prices through our highly efficient new retail channels such as our e-commerce platforms and our Mi Home stores. With our internet services, we closely engage and interact with users on our platform, thus increasing user stickiness and monetization opportunities.

This business model has led to powerful network effects across our platform, which enhances user experience, engagement and retention. As more of our products and services are connected, we are set to deliver better and richer user experience, which will, in turn, attract more users to our platform.

***Our Business Segment Revenues***

The following table sets forth segment revenue both as an absolute amount and as a percentage of total revenues for the periods indicated:

| | For the year ended December 31, | | | | | | | For the nine months ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2017 | | 2018 | | 2019 | | | 2019 | | 2020 | |
| | RMB | % | RMB | % | RMB | US$ | % | RMB | % | RMB | % |
| | | | | | | | | (Unaudited) | | (Unaudited) | |
| | (in millions, except percentages) | | | | | | | | | | |
| Smartphones | 80,563.6 | 70.3 | 113,800.4 | 65.1 | 122,094.9 | 17,537.8 | 59.3 | 91,298.1 | 61.1 | 109,556.4 | 62.5 |
| IoT and lifestyle products | 23,447.8 | 20.5 | 43,816.9 | 25.1 | 62,088.0 | 8,918.4 | 30.2 | 42,594.0 | 28.5 | 46,356.1 | 26.4 |
| Internet services | 9,896.4 | 8.6 | 15,955.6 | 9.1 | 19,841.6 | 2,850.1 | 9.6 | 14,146.5 | 9.5 | 17,580.2 | 10.0 |
| Others | 716.9 | 0.6 | 1,342.5 | 0.7 | 1,814.2 | 260.6 | 0.9 | 1,330.4 | 0.9 | 1,910.0 | 1.1 |
| **Total** | **114,624.7** | **100.0** | **174,915.4** | **100.0** | **205,838.7** | **29,566.9** | **100.0** | **149,369.0** | **100.0** | **175,402.7** | **100.0** |

***Our Global Operations***

As of September 30, 2020, our products were sold in more than 90 countries and regions. Geographically, we generated 28.0%, 40.0%, 44.3% and 50.5% of our revenues in countries and regions outside mainland China in 2017, 2018, 2019 and the nine months ended September 30, 2020. According to Canalys, we ranked 3rd globally in terms of smartphone shipments in the third quarter of 2020, with an all-time high market share of 13.5%. Our smartphone shipments ranked top in 10 countries and regions, and in the top five in 54 countries and regions, in the third quarter of 2020. As overseas markets are a strong growth driver for us, we will continue to invest heavily in them, expand our sales channels through strengthening our cooperation with local partners, and export our competitive products and services to more countries and regions. For more information on our global operations, see "*Business – Global Operations*."

**Competitive Strengths**

We believe the following competitive strengths contribute to our success and differentiate us from our competitors:

- Triathlon Business Model;
- Scale and Leadership;
- Brand and Passionate Users;
- Innovation and Design;
- 5G and AIoT;
- Global;
- Efficiency;
- Strong Financial Profile; and
- Founders and Management Team.

**Our Strategies**

To achieve our mission and further solidify our leadership, we intend to pursue the following strategies:

- Unwavering focus on innovation, quality, design and user experience;
- Smartphone x AIoT;
- Maintain relentless efficiency;
- Enrich our internet services;
- Broaden our overseas expansion; and
- Invest in and expand our ecosystem.

**Corporate Information**

The Company was incorporated in the Cayman Islands on January 5, 2010 as an exempted company with limited liability. In July 2018, the Company publicly offered its shares for listing on the Main Board of the SEHK under stock code 1810. The Company's principal place of business is located at Xiaomi Campus, Anningzhuang Road, Haidian District, Beijing, The People's Republic of China. Its registered office is located at Maples Corporate Services Limited PO Box 309 Ugland House, Grand Cayman, KY1-1104 Cayman Islands. Our website is *www.mi.com*. Information contained on our website does not constitute part of this Offering Circular.

For information on the Issuer, Xiaomi Best Time International Limited, see "*Description of the Issuer*."

## SUMMARY FINANCIAL INFORMATION

The following summaries of our historical consolidated income statement data for the years ended December 31, 2017, 2018 and 2019 and for the nine months ended September 30, 2019 and 2020, our historical consolidated balance sheet data as of December 31, 2017, 2018 and 2019 and as of September 30, 2020, and our historical consolidated cash flows data for the years ended December 31, 2017, 2018, 2019 and for the nine months ended September 30, 2019 and 2020 have been derived from our Audited Financial Statements and Interim Financial Results, respectively, each as included elsewhere in this Offering Circular. You should read this section in conjunction with the "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the notes to those statements included elsewhere in this Offering Circular. The historical results are not necessarily indicative of the results of operations to be expected in the future.

### Consolidated Summary Income Statement Data of the Company

| | For the year ended December 31, | | | | | | | For the nine months ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | **2017** | | **2018** | | **2019** | | | **2019** | | **2020** | |
| | **RMB** | **%** | **RMB** | **%** | **RMB** | **US$** | **%** | **RMB** | **%** | **RMB** | **%** |
| | | | | | | | | **(Unaudited)** | | **(Unaudited)** | |
| | (in thousands, except percentages) | | | | | | | | | | |
| **Revenue** | **114,624,742** | **100.0** | **174,915,425** | **100.0** | **205,838,682** | **29,566,876** | **100.0** | **149,368,958** | **100.0** | **175,402,749** | **100.0** |
| **Cost of sales** | **(99,470,537)** | **(86.8)** | **(152,723,486)** | **(87.3)** | **(177,284,649)** | **(25,465,346)** | **(86.1)** | **(128,658,228)** | **(86.1)** | **(149,977,190)** | **(85.5)** |
| **Gross profit** | **15,154,205** | **13.2** | **22,191,939** | **12.7** | **28,554,033** | **4,101,530** | **13.9** | **20,710,730** | **13.9** | **25,425,559** | **14.5** |
| Selling and marketing expenses | (5,231,540) | (4.6) | (7,993,072) | (4.6) | (10,378,073) | (1,490,717) | (5.0) | (6,677,015) | (4.5) | (9,449,131) | (5.4) |
| Administrative expenses | (1,216,110) | (1.1) | (12,099,078) | (6.9) | (3,103,901) | (445,847) | (1.5) | (2,199,295) | (1.5) | (2,470,674) | (1.4) |
| Research and development expenses | (3,151,401) | (2.7) | (5,776,826) | (3.3) | (7,492,554) | (1,076,238) | (3.6) | (5,239,839) | (3.5) | (6,150,520) | (3.5) |
| Fair value changes on investments measured at fair value through profit or loss | 6,371,098 | 5.6 | 4,430,359 | 2.5 | 3,813,012 | 547,705 | 1.9 | 1,994,595 | 1.4 | 6,131,958 | 3.5 |
| Share of (losses)/ gains of investments accounted for using the equity method | (231,496) | (0.2) | (614,920) | (0.4) | (671,822) | (96,501) | (0.3) | (398,032) | (0.3) | 1,012,687 | 0.6 |
| Other income | 448,671 | 0.4 | 844,789 | 0.5 | 1,265,921 | 181,838 | 0.6 | 914,979 | 0.6 | 396,069 | 0.2 |
| Other gains/(losses), net | 72,040 | 0.1 | 213,281 | 0.1 | (226,399) | (32,520) | (0.1) | (43,060) | (0.0) | (463,114) | (0.3) |
| **Operating profit** | **12,215,467** | **10.7** | **1,196,472** | **0.7** | **11,760,217** | **1,689,250** | **5.7** | **9,063,063** | **6.1** | **14,432,834** | **8.2** |
| Finance income/ (expenses), net | 26,784 | 0.0 | 216,373 | 0.1 | 402,429 | 57,805 | 0.2 | 383,243 | 0.2 | (1,660,268) | (0.9) |
| Fair value changes of convertible redeemable preferred shares | (54,071,603) | (47.2) | 12,514,279 | 7.2 | – | – | – | – | – | – | – |
| **(Loss)/profit before income tax** | **(41,829,352)** | **(36.5)** | **13,927,124** | **8.0** | **12,162,646** | **1,747,055** | **5.9** | **9,446,306** | **6.3** | **12,772,566** | **7.3** |
| Income tax expenses | (2,059,763) | (1.8) | (449,377) | (0.3) | (2,059,696) | (295,857) | (1.0) | (1,779,575) | (1.2) | (1,254,851) | (0.7) |
| **(Loss)/profit for the year/period** | **(43,889,115)** | **(38.3)** | **13,477,747** | **7.7** | **10,102,950** | **1,451,198** | **4.9** | **7,666,731** | **5.1** | **11,517,715** | **6.6** |
| **Non-IFRS Measure:** | | | | | | | | | | | |
| **Adjusted net profit (unaudited)[(1)]** | **5,361,876** | **4.7** | **8,554,548** | **4.9** | **11,532,296** | **1,656,511** | **5.6** | **9,187,890** | **6.2** | **9,801,972** | **5.6** |

Note:

(1) We define adjusted net profit as profit for the period, as adjusted by adding back (i) fair value changes of convertible redeemable preferred shares, (ii) share-based compensation, (iii) net fair value changes on investments, and (iv) amortization of intangible assets resulting from acquisitions, (v) changes of value of financial liabilities to fund investors, and (vi) income tax effects of Non-IFRS adjustments. Adjusted net profit is not a measure required by, or presented in accordance with IFRS. The use of adjusted net profit has limitation as an analytical tool, and you should not consider it in isolation from, or as a substitute for analysis of, our results of operations or financial condition as reported under IFRS. See "*Management's Discussion and Analysis of Financial Condition and Results of Operations – Non-IFRS Measure: Adjusted Net Profit*" for details.

## Consolidated Summary Balance Sheet Data of the Company

| | As of December 31, | | | | As of September 30, |
|---|---|---|---|---|---|
| | 2017 | 2018 | 2019 | | 2020 |
| | RMB | RMB | RMB | US$ | RMB |
| | | | | | (Unaudited) |
| | (in thousands) | | | | |
| Total non-current assets | 28,731,300 | 39,215,389 | 46,090,121 | 6,620,432 | 61,678,367 |
| Total current assets | 61,138,461 | 106,012,561 | 137,539,086 | 19,756,253 | 149,927,096 |
| **Total assets** | **89,869,761** | **145,227,950** | **183,629,207** | **26,376,685** | **211,605,463** |
| Total non-current liabilities | 169,947,781 | 12,037,663 | 9,790,826 | 1,406,364 | 17,501,273 |
| Total current liabilities | 47,132,671 | 61,940,158 | 92,180,705 | 13,240,930 | 99,535,812 |
| **Total liabilities** | **217,080,452** | **73,977,821** | **101,971,531** | **14,647,294** | **117,037,085** |
| **Net (liabilities)/assets** | **(127,210,691)** | **71,250,129** | **81,657,676** | **11,729,391** | **94,568,378** |
| Share capital | 150 | 377 | 388 | 56 | 392 |
| Reserves | (127,272,511) | 71,322,608 | 81,330,186 | 11,682,350 | 94,228,146 |
| Non-controlling interests | 61,670 | (72,856) | 327,102 | 46,985 | 339,840 |
| **Total equity** | **(127,210,691)** | **71,250,129** | **81,657,676** | **11,729,391** | **94,568,378** |
| **Total equity and liabilities** | **89,869,761** | **145,227,950** | **183,629,207** | **26,376,685** | **211,605,463** |

## Consolidated Summary Cash Flows Data of the Company

| | For the year ended December 31, | | | | For the nine months ended September 30, | |
|---|---|---|---|---|---|---|
| | 2017 | 2018 | 2019 | | 2019 | 2020 |
| | RMB | RMB | RMB | US$ | RMB | RMB |
| | | | | | (Unaudited) | (Unaudited) |
| | (in thousands) | | | | | |
| Net cash (used in)/generated from operating activities | (995,669) | (1,414,571) | 23,810,354 | 3,420,143 | 13,908,001 | 8,350,998 |
| Net cash used in investing activities | (2,677,714) | (7,508,040) | (31,570,136) | (4,534,766) | (11,768,862) | (7,173,063) |
| Net cash generated from financing activities | 6,214,930 | 26,574,172 | 3,121,238 | 448,338 | 2,576,968 | 3,839,898 |
| Net increase/(decrease) in cash and cash equivalents | 2,541,547 | 17,651,561 | (4,638,544) | (666,285) | 4,716,107 | 5,017,833 |
| Cash and cash equivalents at beginning of the year/period | 9,230,320 | 11,563,282 | 30,230,147 | 4,342,289 | 30,230,147 | 25,919,861 |
| Effects of exchange rate changes on cash and cash equivalents | (208,585) | 1,015,304 | 328,258 | 47,151 | 592,910 | (679,982) |
| Cash and cash equivalents at end of the year/period | 11,563,282 | 30,230,147 | 25,919,861 | 3,723,155 | 35,539,164 | 30,257,712 |

## THE OFFERING

*The following contains summary information about the Bonds. Some of the terms described below are subject to important limitations and exceptions. Words and expressions defined in "Terms and Conditions of the Bonds" and "Provisions relating to the Bonds in Global Form" shall have the same meanings in this summary. For a more complete description of the terms of the Bonds, see "Terms and Conditions of the Bonds" in this Offering Circular.*

| | |
|---|---|
| **Issuer** | Xiaomi Best Time International Limited |
| **Guarantor** | Xiaomi Corporation (小米集团) |
| **Issue** | U.S. dollar-denominated zero coupon guaranteed convertible bonds due 2027 in an aggregate principal amount of U.S.$855,000,000, convertible into fully-paid class B ordinary shares in the share capital of the Guarantor with a par value U.S.$0.0000025 each, conferring a holder of a Class B Share one vote per share on any resolution tabled at the Guarantor's general meetings (the "**Class B Shares**"). |
| **Interest** | The Bonds will be zero coupon and will not bear interest. See "*Terms and Conditions of the Bonds – Default Interest*". |
| **Issue Price** | 105.25 per cent. of the principal amount of the Bonds. |
| **Issue Date** | December 17, 2020 |
| **Maturity Date** | December 17, 2027 |
| **Form and Denomination** | The Bonds will be issued in registered form in the denomination of U.S.$200,000 and integral multiples of U.S.$100,000 in excess thereof. |
| **Guarantee** | The due payment of all sums expressed to be payable by the Issuer under the Trust Deed and the Bonds has been unconditionally and irrevocably guaranteed by the Guarantor. The obligations of the Guarantor in that respect (the "**Guarantee**") are contained in the Trust Deed. |
| **Status** | The Bonds will constitute direct, unconditional, unsubordinated and (subject to Condition 4(a) of the Conditions) unsecured obligations of the Issuer and shall at all times rank *pari passu* and without any preference or priority among themselves. The payment obligations of the Issuer under the Bonds and the obligations of the Guarantor under the Guarantee shall, save for such exceptions as may be provided by mandatory provisions of applicable law and subject to Condition 4(a) of the Conditions, at all times rank at least equally with all of their respective other present and future unsecured and unsubordinated obligations. |

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| **Negative Pledge** | So long as any Bond remains outstanding (as defined in the Trust Deed), the Guarantor will not create or have outstanding, and the Guarantor will ensure that none of its Principal Controlled Entities and the Issuer will create or have outstanding, any Lien upon the whole or any part of their respective present or future undertaking, assets or revenues (including any uncalled capital) securing any Relevant Indebtedness, or any guarantee or indemnity in respect of any Relevant Indebtedness either of the Issuer, the Guarantor, or of any of the Guarantor's Principal Controlled Entities, without (i) at the same time or prior thereto securing or guaranteeing the Bonds, as applicable, equally and rateably therewith (or in priority thereto) or (ii) providing such other security or guarantee for the Bonds as shall be approved by an Extraordinary Resolution (as defined in the Trust Deed) of the Bondholders. See "*Terms and Conditions of the Bonds – Covenants – Negative Pledge*". |
| **Conversion Period** | At any time on or after January 27, 2021 (a) up to the close of business (at the place where the Certificate evidencing such Bond is deposited for conversion) on the date falling 10 days prior to the Maturity Date (both days inclusive) (but, except as provided in Condition 6(A)(iii) of the Conditions, in no event thereafter), (b) if such Bond shall have been called for redemption by the Issuer before the Maturity Date, then up to and including the close of business (at the place aforesaid) on a date no later than 10 days (in the place aforesaid) prior to the date fixed for redemption thereof or (c) if notice requiring redemption has been given by the holder of such bond pursuant to Condition 8(D) or Condition 8(E) of the Conditions, then up to the close of business (at the place aforesaid) on the business day (in the place aforesaid) prior to the giving of such notice. See "*Terms and Conditions of the Bonds– Conversion – Conversion Right*". |
| **Conversion Price** | HK$36.74 per Class B Share, subject to adjustment for, among other things, consolidation, subdivision or reclassification, capitalization of profits or reserves, capital distributions, rights issues of or options at less than 95 per cent. of the Current Market Price, rights issues of other securities, issues at less than 95 per cent. of the Current Market Price, other issues at less than 95 per cent. of the Current Market Price, modification of rights of conversion at less than 95 per cent. of the Current Market Price, other offers to Ordinary Shareholders and other events as described in Condition 6(C) of the Conditions. |
| **Final Redemption** | Unless previously redeemed, converted or purchased and canceled as provided in the Conditions, the Issuer will redeem each Bond at its principal amount on the Maturity |

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| | Date. See "*Terms and Conditions of the Bonds – Redemption, Purchase and Cancelation – Maturity*". |
| **Redemption for Taxation Reasons** | The Bonds may be redeemed at the option of the Issuer in whole, but not in part, at any time, on giving not less than 30 nor more than 60 days' notice (a "**Tax Redemption Notice**") to the Bondholders in accordance with the Conditions and in writing to the Trustee and the Principal Agent (which notice shall be irrevocable) at their principal amount if the Issuer satisfies the Trustee immediately prior to the giving of such notice that (i) the Issuer (or if the Guarantee was called, the Guarantor) has or will become obliged to pay Additional Tax Amounts as provided or referred to in Condition 9 of the Conditions as a result of any change in, or amendment to, the laws or regulations of Hong Kong, the Cayman Islands or the PRC or in each case, any political subdivision or any authority thereof or therein having power to tax, or any change in the general application or official interpretation of such laws or regulations, which change or amendment becomes effective on or after December 1, 2020, and (ii) such obligation cannot be avoided by the Issuer (or, as the case may be, the Guarantor) taking reasonable measures available to it, provided that no Tax Redemption Notice shall be given earlier than 90 days prior to the earliest date on which the Issuer (or as the case may be, the Guarantor) would be obliged to pay such Additional Tax Amounts were a payment in respect of the Bonds then due.<br><br>If the Issuer gives a Tax Redemption Notice, each Bondholder will have the right to elect that his Bond(s) shall not be redeemed and that the provisions of Condition 9 of the Conditions shall not apply in respect of any payment to be made in respect of such Bond(s) which falls due after the relevant Tax Redemption Date, whereupon no Additional Tax Amounts shall be payable in respect thereof pursuant to Condition 9 of the Conditions and payment of all amounts shall be made subject to the deduction or withholding of any taxation required to be withheld or deducted. |
| **Redemption at the Option of the Issuer** | On giving not less than 30 nor more than 60 days' notice to the Bondholders in accordance with the Conditions and in writing to the Trustee and the Principal Agent, the Issuer:<br><br>(i) may at any time after December 17, 2025 and prior to the Maturity Date redeem in whole, but not in part, the Bonds for the time being outstanding at their principal amount, provided that the Closing Price of a Class B Share (translated into U.S. dollars at the Prevailing Rate), for 20 out of 30 consecutive Trading Days, the last of which occurs |

not more than five Trading Days prior to the Optional Redemption Date, was at least 130 per cent. of the Conversion Price (translated into U.S. dollars at the Fixed Exchange Rate) then in effect immediately prior to the date upon which notice of such redemption is given; or

(ii) may at any time prior to the Maturity Date redeem in whole, but not in part, the Bonds at their principal amount, if, immediately prior to the date the notice of redemption is given, 90 per cent. or more in principal amount of the Bonds originally issued has already been converted, redeemed or purchased and canceled.

**Redemption at the Option of the Bondholders**

The Issuer will, at the option of the holder of any Bond, redeem all or some only of such holder's Bonds on December 17, 2025 (the "**Put Option Date**") at the principal amount of the Bonds. To exercise such option, the holder must deposit at the specified office of any Paying Agent a duly completed and signed put notice in the form for the time being current, obtainable from the specified office of any Paying Agent, together with the Certificate evidencing the Bonds to be redeemed not more than 60 days and not less than 30 days prior to the Put Option Date.

**Redemption for Relevant Event**

Following the occurrence of a Relevant Event, the holder of each Bond will have the right at such holder's option, to require the Issuer to redeem all or some only of such holder's Bonds on the Relevant Event Put Date at their principal amount.

A "**Relevant Event**" occurs:

(i) when the Class B Shares cease to be listed or admitted to trading or are suspended from trading for a period equal to or exceeding 30 consecutive Trading Days on the Relevant Stock Exchange; or

(ii) when there is a Change of Control; or

(iii) when (a) there is any change in or amendment to the laws, regulations and rules of the PRC or the official interpretation or official application thereof (a "**Change in Law**") that results in (x) the Guarantor and its Controlled Entities (collectively, the "**Group**") (as in existence immediately subsequent to such Change in Law), as a whole, being legally prohibited from operating substantially all of the business operations conducted by the Group (as in existence immediately prior to such Change in Law) as of the last date of the period described in the Guarantor's consolidated financial statements for the most recent fiscal quarter and (y) the Guarantor being unable to continue to derive substantially all of the economic benefits from the business operations conducted by the Group (as in existence immediately prior to such Change in Law) in the same manner as reflected in the Guarantor's consolidated financial statements for the most recent fiscal quarter and (b) the Guarantor has not furnished to the Trustee, prior to the date that is 12 months after the date of the Change in Law, an opinion from an independent financial adviser or external legal counsel stating either (x) that the Guarantor is able to continue to derive substantially all of the economic benefits from the business operations conducted by the Group (as in existence immediately prior to such Change in Law), taken as a whole, as reflected in the Guarantor's consolidated financial statements for the most recent fiscal quarter (including after giving effect to any corporate restructuring or reorganization plan of the Guarantor) or (y) that such Change in Law would not materially adversely affect the Issuer's and the Guarantor's ability to make principal and premium (if any) payments on the Bonds when due or to convert the Bonds in accordance with the Conditions.

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| **Company and Shareholder's Lock-up** | Each of the Issuer and the Guarantor has agreed in the Subscription Agreement that neither the Issuer, the Guarantor nor any person acting on its or their behalf will (a) issue, offer, sell, pledge, contract to sell or otherwise dispose of or grant options, issue warrants or offer rights entitling persons to subscribe or purchase any interest in any Ordinary Shares or securities of the same class as the Bonds or the Ordinary Shares or any securities convertible into, exchangeable for or which carry rights to subscribe or purchase the Bonds, the Ordinary Shares or securities of the same class as the Bonds, the Ordinary Shares or other instruments representing interests in the Bonds, the Ordinary Shares or other securities of the same class as them, (b) enter into any swap or other agreement that transfers, in whole or in part, any of the economic consequences of the ownership of the Ordinary Shares, (c) enter into any transaction with the same economic effect as, or which is designed to, or which may reasonably be expected to result in, or agree to do, any of the foregoing, whether any such transaction of the kind described in (a), (b) or (c) is to be settled by delivery of Ordinary Shares or other securities, in cash or otherwise or (d) announce or otherwise make public an intention to do any of the foregoing, in any such case without the prior written consent of the Managers |

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| | between the date hereof and the date which is 90 days after the Issue Date (both dates inclusive), except for (i) the Bonds and the new Class B Shares issued on conversion of the Bonds, (ii) any Ordinary Shares or options granted pursuant to the Guarantor's publicly disclosed share option schemes and share award scheme, and (iii) the issue of any Ordinary Shares which are issued as consideration for any merger or acquisition.<br><br>Smart Mobile Holdings Limited has executed a lock-up undertaking in respect of the 4,226,640,526 Class A Shares and 2,443,898,616 Class B Shares held directly (or through nominees) or indirectly through companies controlled by it or their subsidiaries (or through their nominees) (collectively, the "**Lock-up Shares**"), representing 90.06 per cent. and 12.57 per cent. respectively of the relevant class of Ordinary Shares of the Guarantor, on the date of the Subscription Agreement, whereby it undertakes not to sell any Lock-up Shares or enter into other transactions with a similar effect for a period from the date of the undertaking to 90 days after the Issue Date provided that the foregoing shall not apply to transfers of any Ordinary Shares or any security convertible into the Ordinary Shares pursuant to any donation for genuine charitable purposes. |
| **Events of Default** | For a description of certain events of default that will permit the Bonds to become immediately due and payable at their principal amount, see "*Terms and Conditions of the Bonds – Events of Default*". |
| **Clearing Systems** | The Bonds will be represented by beneficial interests in the Global Certificate, which will be registered in the name of a nominee of, and deposited on the Issue Date with, a common depositary for Euroclear and Clearstream. Beneficial interests in the Global Certificate will be shown on, and transfers thereof will be effected only through records maintained by, Euroclear and Clearstream. Except as described in the Global Certificate, certificates for Bonds will not be issued in exchange for beneficial interests in the Global Certificate. |
| **Governing Law** | The Bonds, the Trust Deed and the Agency Agreement and any non-contractual obligations arising out of or in connection with them are governed by, and shall be construed in accordance with, the laws of England. |
| **Trustee** | Citicorp International Limited. |
| **Principal Agent and Transfer Agent** | Citibank, N.A., London Branch. |
| **Registrar** | Citigroup Global Markets Europe AG. |
| **Listing** | Application will be made to the Hong Kong Stock Exchange for (i) the listing of, and permission to deal in, the Bonds by way of debt issues to Professional Investors |

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| | only; and (ii) the listing of, and permission to deal in, the Class B Shares issuable on conversion, and such permissions are expected to become effective on December 18, 2020 and when such Class B Shares are issued, respectively. |
| **Use of Proceeds** | See section entitled "*Use of Proceeds*". |
| **Selling Restrictions** | There are certain restrictions on the offer, sale and transfer of the Bonds and the Class B Shares to be issued upon conversion of the Bonds in certain jurisdictions including the United States and Hong Kong. For a description of the restrictions on the distribution of this Offering Circular or any offering material and the offering, sale or delivery of the Bonds and the Class B Shares to be issued upon conversion of the Bonds, see "*Subscription and Sale*". |
| **Ratings** | The Bonds are expected to be rated "Baa2" by Moody's. A credit rating is not a recommendation to buy, sell or hold securities and may be subject to revision, qualification, suspension, reduction or withdrawal at any time by the assigning rating agency. Prospective investors should evaluate each rating independently of any other rating of the Bonds or other securities of the Issuer or the Guarantor. |
| **Legal Entity Identifier** | 254900IGJCVEY8WNJT74 |
| **ISIN** | XS2269112863 |
| **Common Code** | 226911286 |
| **Concurrent Equity Placement** | On or about the date of the Subscription Agreement and in connection with the Offering, the Guarantor has entered into a placing and subscription agreement with the Managers and Smart Mobile Holdings Limited (the "**Seller**"), pursuant to which the Seller has agreed to sell, and the Managers have agreed to act as agents for the Seller, to procure on a fully underwritten basis placees to purchase, or failing which to purchase itself, 1,000,000,000 Class B Shares at the placing price of HK$23.70 for each Class B Share (the "**Concurrent Equity Placement**"). The Concurrent Equity Placement was conducted concurrently with the Offering and closing of the Concurrent Equity Placement occurred on December 4, 2020. The completion of the issuance of the Bonds and the Concurrent Equity Placement are not inter-conditional. |

*You should carefully consider the risks described below and the other information contained in this Offering Circular before making an investment decision. The risks and uncertainties described below may not be the only ones that we face. Additional risks and uncertainties that we are not aware of or that we currently believe are immaterial may also adversely affect our business, financial condition or results of operations. If any of the events described below should occur, our business, financial condition or results of operations could be materially and adversely affected. In such case, we may not be able to satisfy our obligations under the Bonds, and you could lose all or part of your investment.*

## Risks Relating to Our Business and Industry

***Global markets for our products and services are highly competitive and subject to rapid technological changes, and we may be unable to compete effectively in these markets.***

Our products and services compete in highly competitive global markets characterized by aggressive price competition, frequent introduction of new products, short product life cycles, evolving industry standards, continued improvement in product price and performance characteristics, rapid adoption of technological and product advancements by competitors and price sensitivity and preference on the part of consumers.

Our ability to compete successfully depends heavily on our ability to continue to introduce innovative new products, services and technologies in a timely manner to the marketplace. We design and develop a number of our key hardware products, our MIUI proprietary operating system, numerous software applications and related services. Our capability to introduce new or enhanced products, services and technologies in turn depends on a number of factors, including timely and successful research and development efforts by us as well as our ecosystem partners. As a result, we must make significant investments in research and development. The research and development process of new products, services and technologies is complex, time-consuming and costly, and the result is unpredictable. Given the complexity, we could experience delays in completing the development and introduction of new and enhanced products, services and technologies in the future. Our research and development efforts may not yield the benefits we expect to achieve at all after we dedicate our time and resources into it. If we are unable to continue to develop, sell and offer innovative new products and services, or if competitors infringe on our intellectual property, our ability to maintain a competitive advantage could be adversely affected.

We face substantial competition from companies that have significant technical, marketing, distribution and other resources, as well as established hardware, software and digital content supplier relationships. Additionally, we face significant competition as competitors reduce their selling prices and have always attempted to produce products that imitate our product features and applications or, alternatively, collaborate among themselves to offer solutions that are more competitive than those they currently offer. Some of our competitors have greater experience, brand recognition, product breadth and distribution channels than us. Our current competitors and new entrants may also seek to develop new product and service offerings, technologies or capabilities that could render many of the products and services that we offer obsolete or less competitive, and some of them may adopt more aggressive pricing policies or devote greater resources to marketing and promotional campaigns than us. The occurrence of any of these circumstances may hinder our growth and our ability to compete and reduce our market share. As a result, our business, results of operations, financial condition and prospects would be materially and adversely affected.

***If we are unable to manage our growth or execute our strategies effectively, our business and prospects may be materially and adversely affected.***

Our business has grown substantially in recent years, and we expect continued growth in our business, revenues and number of employees. In addition, as we increase our product and service offerings, we will need to work with a larger number of partners efficiently and maintain and expand mutually beneficial relationships with our existing and new partners. We also need to continually enhance and upgrade our infrastructure and technology, improve control over our operational, financial and management aspects, strengthen our supplier and distributor management, refine our reporting systems and procedures, and expand, train and manage our growing employee base. All these efforts will require significant managerial, financial and human resources. We cannot assure you that we will be able to effectively manage our growth, that our current infrastructure, systems, procedures and controls or any new measures to enhance them will be adequate to support our expanding operations or that our strategies and new business initiatives will be executed successfully. If we are not able to manage our growth or execute our strategies effectively, our expansion may not be successful and our business and prospects may be materially and adversely affected.

***Maintaining the trusted brand image of our products and services is critical to our success, and any failure to do so could severely damage our reputation and brand, which would have a material adverse effect on our business, financial condition and results of operations.***

We have established a strong brand name and reputation for our products and services globally, especially in mainland China and other markets such as Western Europe. Any loss of trust in our products and services could harm the value of our brand, which could materially reduce our revenue and profitability. Our ability to maintain our position as a trusted brand for hardware products and internet services is based in large part upon:

- the quality, design and accessible pricing that we offer;
- providing a compelling shopping experience to our users;
- user satisfaction with our products and services;
- increasing brand awareness through marketing and brand promotion activities; and
- preserving our reputation and goodwill in the event of any negative publicity on product quality, service, price or authenticity, or other issues affecting us or other internet companies.

Any public perception that our products and services are defective or otherwise unsatisfactory, even if factually incorrect or based on isolated incidents, could damage our reputation, diminish the value of our brand, undermine the trust and credibility we have established and have a negative impact on our ability to attract new users or retain our current users. If we are unable to maintain our reputation, enhance our brand recognition or increase positive awareness of our products and services, it may be difficult to maintain and grow our user base, and our business and growth prospects may be materially and adversely affected.

***If we fail to successfully manage frequent product introductions and transitions, we may not remain competitive or be able to stimulate customer demand.***

Due to the highly volatile and competitive nature of the industries in which we compete, we must continually introduce new products, services and technologies, improve existing products and services, effectively stimulate customer demand for new and upgraded products and successfully manage the transition to these new and upgraded products. The success of new product introductions depends on a number of factors including, but not limited to, timely and successful product development, market acceptance, our ability to manage the risks associated with new product production ramp-up issues, the availability of application software for new products, the effective management of purchase commitments and inventory levels in line with anticipated product demand, the availability of products in appropriate quantities and at expected costs to meet anticipated demand and the risk that new products may have quality or other defects or deficiencies in the early stages of introduction. Accordingly, we cannot determine in advance the ultimate effect of new product introductions and transitions. In addition, rapid technological development and advancements may render smartphones in the common forms and with the common functionalities that are generally available to consumers today outdated or obsolete, and emerging products and services may substitute smartphones as consumers generally know them today. In such event, we cannot assure you that we will be able to develop and introduce new forms of products, services and technologies to the markets in a timely manner, or at all, that would allow us to maintain or strengthen our leadership position in our industry. Failure to do so, or to generally stay abreast of the latest technological evolutions, could materially and adversely impact our business operations, prospects and financial performance.

***If we fail to grow or retain our user base, or if user engagement ceases to grow or declines, our business and operating results may be materially and adversely affected.***

The size of our user base and the level of user engagement are critical to our success. Our business has been depending and will continue to significantly depend on our users and their loyalty in and level of engagement with our products and services. If users no longer view our products and services as useful and attractive as compared to competing offerings, we may not be able to increase or maintain our user base and the level of user engagement. A number of factors could negatively affect user growth, retention and engagement, including:

- despite our continual research, monitoring and analysis of user needs, we may be unable to identify and meet evolving user demands;

- we may not be able to timely develop and introduce new or updated products and services, or the new or updated products and services we introduce may not be favorably received by users;

- we may fail to update existing technology or develop new technology in time to stay ahead or abreast of market advances;

- we may not be able to continue to successfully drive organic growth of users through word-of-mouth referrals and in-app cross-promotion, which may cause the growth of our user base to slow down or stall or require us to increase our promotion and advertising spending or devote additional resources to acquire users; we may be unable to prevent or combat inappropriate use of our products and services, which may lead to negative public perception of us and damage our brand or reputation;

- we may encounter technical or other problems that prevent our products and services from operating in a smooth and reliable manner or otherwise adversely affect user experience;

- our competitors may launch or develop similar or disruptive products and services with better user experience, which may result in loss of existing users or decline in new user growth;

- we may fail to address user concerns related to privacy and communication, data safety, security or other factors; and

- we may be compelled to modify our products and services to address requirements imposed by legislation, regulations, government policies or requests from government authorities in manners that may compromise user experience.

***Our business is subject to a variety of mainland Chinese and international laws, rules, policies and other obligations regarding data protection. Any losses or unauthorized access to or releases of confidential information and personal data could subject us to significant reputational, financial, legal and operational consequences.***

Our business requires us to use and store confidential information, including, among other things, personally identifiable information, or PII, with respect to our users and employees. We are subject to domestic and international laws relating to the collection, use, retention, security and transfer of PII. In many cases, these laws not only apply to third-party transactions, but also may restrict transfers of PII among us and our overseas subsidiaries. Several jurisdictions have passed laws in this area, and other jurisdictions are considering imposing additional restrictions. These laws continue to develop and may vary from jurisdiction to jurisdiction. Complying with emerging and changing international requirements may cause us to incur substantial costs or require us to change our business practices. Non-compliance could result in significant penalties or legal liability. Foreign data protection, privacy, and other laws and regulations can impose different obligations or be more restrictive than those in mainland China. Regulatory authorities around the world are considering a number of legislative and regulatory proposals concerning data protection. In addition, the interpretation and application of consumer and data protection laws in the U.S., Europe and elsewhere are often uncertain. It is possible that these laws may be interpreted and applied in a manner that is inconsistent with our data practices. These legislative and regulatory proposals, if adopted, and such interpretations could, in addition to the possibility of fines, result in an order requiring that we change our data practices, which could have an adverse effect on our business and results of operations. Complying with these various laws could cause us to incur substantial costs or require us to change our business practices in a manner adverse to our business. Our business operations and sales in Europe have grown significantly in recent years. Recent legal developments in Europe have created compliance uncertainty regarding certain transfers of personal data. For example, the General Data Protection Regulation, or GDPR, which went into effect in the European Union, or EU, on May 25, 2018, applies to all of our activities conducted from an establishment in the EU or related to products and services that we offer to EU users. The GDPR created a range of new compliance obligations that could cause us to change our business practices and significantly increased financial penalties for non-compliance. Additionally, California recently enacted legislation that has been dubbed the first "GDPR-like" law in the U.S. Known as the California Consumer Privacy Act, or CCPA, it creates new individual privacy rights for consumers (as that word is broadly defined in the law) and places increased privacy and security obligations on entities handling personal data of consumers or households. The CCPA, which went into effect on January 1, 2020, requires covered companies to provide new disclosures to California consumers, and provides such consumers new ways to opt-out of certain sales of personal information. The CCPA provides for civil penalties for violations, as well as a private right of action for data breaches that is expected to increase data breach litigation. The CCPA may increase our compliance costs and potential liability. Some observers have noted that the CCPA could mark the beginning of a trend toward more stringent privacy legislation in the U.S., which could increase our potential liability and adversely affect our business.

We make statements about our use and disclosure of PII through our privacy policy, information provided on our internal platform and press statements. Any failure by us to comply with these public statements or with other domestic or international privacy-related or data protection laws and regulations could result in proceedings against us by governmental entities or others. In addition to reputational impacts, penalties could include ongoing audit requirements and significant legal liability. None of the data security measures can provide absolute security, and losses or unauthorized access to or releases of confidential information, in particular PII, may still occur, which could materially and adversely affect our reputation, financial condition and operating results.

From time to time, concerns may be expressed about whether our products, services, or processes compromise the privacy of users, customers, and others. As our products, services and processes become increasingly interconnected and the information we process, use and restore become increasingly diversified to include multimedia content including video footage and image, the likelihood of such concerns will increase accordingly as well. Concerns about our practices with regard to the collection, use, disclosure, or security of PII or other privacy-related matters, even if unfounded, could damage our reputation and adversely affect our operating results.

Our business also requires us to share certain confidential information with suppliers and other third parties. The steps we take to secure confidential information that is provided to third parties may not be effective and losses or unauthorized access to or releases of confidential information may still occur, which could materially and adversely affect our reputation, financial condition and operating results. For example, we may experience a security breach impacting our information technology systems that compromises the confidentiality, integrity or availability of confidential information. Such an incident could, among other things, impair our ability to attract and retain users for our products and services, impact the market price of our Class B Shares, materially damage supplier and distributor relationships, and expose us to litigation or government investigations, which could result in penalties, fines or judgments against us.

Our products and services involve the storage and transmission of users' and customers' proprietary information, and theft and security breaches expose us to a risk of loss of this information, improper use and disclosure of such information, litigation, and potential liability. Any systems failure or compromise of our security that results in the release of our users' data, or in our or our users' ability to access such data, could seriously harm our reputation and brand and, therefore, our business, and impair our ability to attract and retain users. We expect to continue to expend significant resources to maintain internal procedures and security protections that shield against theft and security breaches. We have implemented systems and processes intended to secure our information technology systems and prevent unauthorized access to or loss of sensitive data, including through the use of encryption and authentication technologies. As with all companies, these security measures may not be sufficient for all eventualities and may be vulnerable to hacking, employee error, malfeasance, system error, faulty password management or other irregularities. For example, third parties may attempt to fraudulently induce employees or users into disclosing user names, passwords or other sensitive information, which may in turn be used to access our information technology systems. To help protect users and ourselves, we monitor our services and systems for unusual activity and may freeze accounts under suspicious circumstances, which, among other things, may result in the delay or loss of user orders, impede user access to our products and services, or subject us to claims or other legal proceedings against us.

***We may not be able to sustain our historical growth.***

We have experienced rapid growth since we commenced our business in 2010. Our total revenues increased from RMB114.6 billion in 2017 to RMB174.9 billion in 2018, and further increased to RMB205.8 billion in 2019. Our revenue also increased from RMB149.4 billion for the nine months ended September 30, 2019 to RMB175.4 billion for the nine months ended September 30, 2020, showing year on year growth of 17.4% over the same period. However, there is no assurance that we will be able to maintain our historical growth in future periods. Our revenue growth may slow or our revenues may decline for any number of possible reasons, including decreasing consumer spending, increasing competition, slowing growth of the retail or online retail industry, supply and production bottlenecks, emergence of alternative business models, changes in government policies or general economic conditions in mainland China and globally.

***Smartphone sales account for a majority of our revenue, and any decrease in such sales or any increase in the costs associated with such sales may materially and adversely affect our business.***

For the years ended December 31, 2017, 2018 and 2019 and for the nine months ended September 30, 2020, our smartphones segment contributed 70.3%, 65.1%, 59.3% and 62.5% of our total revenues, respectively. Although we have been diversifying our revenue streams by expanding our internet services, as well as the sale of IoT and lifestyle products, we may continue to heavily rely on smartphone sales for a significant portion of our revenues. A decrease in the sales volume of our smartphones or their prices, changing user preferences or material quality issues concerning our smartphones may materially and adversely affect our business and operating results. Furthermore, we are exposed to increases in the prices of smartphone components and materials. While we may seek to reflect such increases in the pricing of our smartphones, we may not be able to do so completely or in a timely fashion. Our future growth and financial performance may depend in part on our ability to develop, produce and sell our smartphones. If we fail to deliver product enhancements, new releases or new products that our users consider useful and attractive, our business and results of operations would be harmed.

***Our mainland China and overseas businesses and results of operations may be materially and adversely affected by the COVID-19 outbreak.***

In late January 2020, in response to intensifying efforts to contain the spread of COVID-19, the Chinese government took a number of actions, which included extending the Chinese New Year holiday, quarantining and treating individuals in mainland China who had COVID-19, asking mainland China residents to remain at home and to avoid gathering in public, and other actions. In February and March 2020, increasingly numbers of additional cases were confirmed in many other countries and regions around the world. In March 2020, the World Health Organization declared COVID-19 as a global pandemic. Many countries have implemented drastic measures, including but not limited to travel bans, closing of boarders and military interventions, to help contain the spread of the virus. The accelerated spread of the virus globally has caused extreme volatility in the global financial market, including the repeated triggering of stock market “circuit breakers” in the U.S. and many other countries.

Our operations in mainland China and overseas markets have experienced significant disruptions. Operations in many cities throughout mainland China have been negatively affected by the outbreak of and response to COVID-19. During the peak of the outbreak in mainland China, our offline sales were affected throughout mainland China as most of our stores were closed or operated at shortened hours with significantly lower customer traffic. However, we were comparatively less impacted due to our strength in online channels. As of the date of the Offering Circular, as business restrictions were gradually lifted in mainland China, our sales have recovered tangibly. In overseas markets, our operations were also adversely affected by the continuing spread of COVID-19. We experienced a temporary disruption in the assembly of our products in February and March 2020 in mainland China, due to the extended shutdown of Chinese factories. However, our production capacity in mainland China has mostly recovered to our normal levels as of the date of this Offering Circular.

As a result of any of the above developments, our business, financial condition and results of operations are expected to be adversely affected by the COVID-19 outbreak. The full extent to which the pandemic impacts our results will depend on future developments. Given that the pandemic is still affecting countries and regions around the world as of the date of this Offering Circular, we are closely monitoring and assessing its impact, which will likely decrease the overall consumption in the affected countries. In addition, our internet services, particularly our advertising business, also could potentially be impacted if our advertising customers decrease their budgets. These developments are highly uncertain and cannot be predicted, including new information which may emerge concerning the severity of COVID-19, the actions to contain COVID-19 or treat its impact, as well as the overall impact on the financial market and economy in China and globally.

***Our businesses and results of operations may be materially and adversely affected by political turmoil, war, terrorism, public health issues, natural disasters and other disruptive events.***

Political turmoil, war, terrorism, public health issues, natural disasters and other disruptive events have caused and could cause damage or disruption to international commerce and the global economy, and thus could have a material adverse effect on us, our suppliers, logistics providers, outsourcing partners and users. Our business operations are subject to interruption by, among others, natural disasters, whether as a result of climate change or otherwise, fire, power shortages and other industrial accidents, terrorist attacks and other hostile acts, labor disputes, public health issues, the existence of anti-Chinese sentiment and related events, demonstrations or policies such as the implementation of protectionism against mainland Chinese companies, political instability and social unrest in countries and regions in which we operate, and other events beyond our control. Such events could decrease demand for our products, make it difficult or impossible for us to make and deliver products to our users, or to receive components or products from our suppliers and ecosystem partners, and create delays and inefficiencies in our supply chain. While our suppliers are required to maintain safe working environments and operations, an industrial accident could occur and could result in disruption to our business and harm to our reputation. Should major public health issues, including pandemics, arise, we could be adversely affected by more stringent employee travel restrictions, additional limitations in freight services, governmental actions limiting the movement of products between regions, delays in production ramps of new products and disruptions in the operations of our outsourcing partners, component suppliers and ecosystem partners. In the event of a natural disaster, we could incur significant losses, require substantial recovery time and experience significant expenditures in order to resume operations.

***Our business is subject to the risks of overseas operations.***

As we have successfully expanded our overseas businesses in recent years, we derive an increasingly significant portion of our revenues from our overseas operations. We generated 28.0%, 40.0%, 44.3% and 50.5% of our revenues in overseas markets in 2017, 2018, 2019 and for the nine months ended September 30, 2020, respectively. As of September 30, 2020, our products were sold in more than 90 countries and regions. We face risks associated with expanding into an increasing number of markets where we have limited or no experience, we may be less well-known or have fewer local resources and we may need to localize our business practices, culture and operations. We may also face protectionist policies that could, among other things, hinder our ability to execute our business strategies and put us at a competitive disadvantage relative to domestic companies in other jurisdictions. The expansion of our overseas and cross-border businesses will also expose us to risks and challenges inherent in operating businesses globally, including:

- increased resources requirements to manage regulatory compliance across our overseas businesses;
- failure to attract and retain capable talent with international perspectives who can effectively manage and operate local businesses;
- uncertain enforcement of our intellectual property rights in different jurisdictions;
- compliance with privacy laws and data security laws, including heightened restrictions and barriers on the transfer of data between different jurisdictions;
- uncertain, complex and potentially adverse and conflicting customs, import/export laws, currency controls, anti-dumping rules tax rules and regulations or other trade barriers or restrictions, which could negatively affect margins on sales of our products in foreign countries and on sales of products that include components obtained from foreign suppliers;
- credit and collectability risk on our trade receivables with customers in different regions;
- availability, reliability and security of international and cross-border payment systems and logistics infrastructure;
- exchange rate fluctuations;
- political instability and general economic or political conditions in particular countries or regions, including territorial or trade disputes, war and terrorism;
- the shutting down of Chinese mobile applications by overseas governments;
- challenges in replicating or adapting our company policies and procedures to operating environments different from that of mainland China, including technology and logistics infrastructure;
- challenges of maintaining efficient and consolidated internal systems, including information technology infrastructure, and of achieving customization and integration of these systems;
- lack of acceptance of our product and service offerings, and challenges of localizing our offerings to appeal to local tastes;
- increased competition with local players in different markets and sub-markets; and
- protectionist or national security policies that restrict our ability to invest in or acquire companies, develop, import or export certain technologies, or utilize technologies that are deemed by local governmental regulators to pose a threat to their national security.

There is no assurance we will be able to manage these risks and challenges as we continue to grow our overseas businesses. Failure to manage these risks and challenges could negatively affect our ability to expand our overseas and cross-border businesses and operations as well as materially and adversely affect our business, financial condition and results of operations.

***If we fail to retain existing or attract new advertising customers to advertise on our platform, maintain and increase our wallet share of advertising budget or if we are unable to collect accounts receivable in a timely manner, our financial condition and results of operations may be materially and adversely affected.***

We cannot assure you that we will be able to retain our advertising customers in the future, attract new advertising customers continuously or be able to retain our advertising customers at all. If our advertising customers find that they can generate better returns elsewhere, or if our competitors provide better advertising services to suit our advertising customers' goals, we may lose our advertising customers. In addition, third parties may develop and use certain technologies to block the display of our advertising customers' advertisements on our platform, which may in turn cause us to lose advertising customers and adversely affect our results of operations. Since most of our advertising customers are not bound by long-term contracts, they may lessen or discontinue advertising arrangements with us easily without incurring material liabilities. Failure to retain existing advertising customers or attract new advertising customers to advertise on our platform may materially and adversely affect our financial conditions and results of operations.

Our brand advertising customers typically enter into advertising agreements with us through various third-party advertising agencies. As a result, we rely on third-party advertising agencies for sales to, and collection of payment from, our brand advertisers. The financial soundness of our advertising customers and advertising agencies may affect our collection of accounts receivable. In addition, while we evaluate the collectability of the advertising service fees before entering into an advertising contract, we cannot assure you that we are or will be able to accurately assess the creditworthiness of each advertising customer or advertising agency, and any inability of advertising customers or advertising agencies to pay us in a timely manner may adversely affect our liquidity and cash flows. In addition, there has been some consolidation among advertising agencies in mainland China. If this trend continues, a small number of large advertising agencies may be in a position to demand higher rebate for advertising agency services, which could reduce our advertising revenue.

***We generate a significant portion of revenues from our internet services from online games. If we fail to source suitable third-party online games on reasonable terms, our revenues from other internet services may be materially and adversely affected.***

We generate a significant portion of revenues from our internet services from online games. The success of our online games depends on our ability to source suitable third-party games on reasonable terms. We may not be able to identify popular and profitable games and license such games on acceptable terms. Popular games may have a short period of popularity. Game developers with popular games may discontinue their cooperation with us or there might be a change in distribution fee and revenue sharing arrangements. In addition, increased competition in Chinese and overseas games markets may negatively impact the fee-sharing arrangement between game developers and us. Should any of these occur, our revenues from internet value-added services would be materially and adversely affected. As a result, our business, financial condition and results of operations may be adversely affected.

***Our business operations and financial position may be materially and adversely affected by any economic slowdown in mainland China as well as globally.***

Our business performance and results of operations are impacted to a significant extent by economic conditions in mainland China and globally. The global economy, markets and levels of spending by businesses and consumers are influenced by many factors beyond our control. The growth of the Chinese economy has slowed in recent years compared to prior years. According to the National Bureau of Statistics of China, China's real GDP growth rate was 6.7% in 2016, which increased to 6.9% in 2017, slowed to 6.6% in 2018 and further slowed to 6.1% in 2019. Uncertainty about mainland China and global economic conditions poses a risk as consumers and businesses may postpone spending in response to credit constraint, rising unemployment rate, financial market volatility, government austerity programs, negative financial news, declines in income or asset values and/or other factors. These worldwide and regional economic conditions could have a material adverse effect on demand for our products and services. Demand also could differ materially from our expectations as a result of currency fluctuations. Other factors that could influence worldwide or regional demand include changes in fuel and other energy costs, conditions in the real estate and mortgage markets, unemployment, labor and healthcare costs, access to credit, consumer confidence and other macroeconomic factors affecting consumer spending behavior. An economic downturn, whether actual or perceived, a further decrease in economic growth rates or an otherwise uncertain economic outlook in mainland China or any other market in which we may operate could have a material adverse effect on business and consumer spending and, as a result, adversely affect our business, financial condition and results of operations.

***We rely on access to third-party intellectual property, which may not be available to us on commercially reasonable terms, or at all.***

Many of our products and provision of our services include or rely on third-party intellectual property, which requires licenses from those third parties. For example, we have entered into worldwide intellectual property license agreements with a number of global technology leaders in the mobile telecommunications market. In addition, we contract with numerous third parties to offer their digital content, including music, films, TV shows and online literature, to our users. There is no assurance that the necessary licenses can be obtained on acceptable terms, or at all. If we fail to renew any intellectual property license agreements on acceptable terms, we may not be able to use the patents and technologies of these third parties in our products, which are critical to our success. As we continue to introduce new products and services and expand our global footprint, licensing and royalty fees that we pay to third-party intellectual property holders may increase significantly. We cannot assure you that we will be able to effectively control the level of licensing and royalty fees paid to third parties, and significant increases in such fees could have a material and adverse impact on our future profitability. Seeking alternative patents and technologies may be difficult and time-consuming, and we may not be successful in finding alternative technologies or incorporating them into our products. Furthermore, some current or future third-party content providers and distributors may offer competing products and services, and could take action to make it more difficult or impossible for us to license or otherwise distribute their content in the future. Other content owners, providers or distributors may seek to limit our access to, or increase the cost of, such content. In addition, we built our proprietary operating system, MIUI, on the free Android kernel that was developed by Google. In the event that Google limits the access to Android kernel or its modules, charges a fee for the use of Android kernel, or ceases to update Android kernel, the ongoing operation of MIUI may be significantly impacted, and our smartphone and internet services segments, as well as our business operations and financial results as a whole, may be materially and adversely affected. Failure to obtain the right to use third-party intellectual property, or to use such intellectual property on commercially reasonable terms, could preclude us from selling certain products, providing certain services including digital content, or otherwise have a material adverse impact on our financial condition and operating results.

***We could be impacted by unfavorable results of legal and administrative proceedings, such as being found to have infringed on intellectual property rights.***

We are subject to various legal or administrative proceedings and claims that have arisen in the ordinary course of business and have not yet been fully resolved, and new claims may arise in the future. In addition, agreements entered into by us sometimes include indemnification provisions, which may subject us to costs and damages in the event of a claim against an indemnified third party. In particular, we have been, and may continue to be, subject to various intellectual property claims, including patent, copyright and trademark disputes, relating to technologies or intellectual property used in our products and services and claiming infringement or violations of intellectual property rights, and new claims may arise in the future. For example, in 2019, Xiaomi H.K. Limited and Xiaomi Technology France, and Xiaomi Technology UK Ltd and Xiaomi Technology France, among others, were named as defendants in two lawsuits, respectively, filed by IPCom GmbH & Co. KG ("**IPCom**"), a patent licensing and management company based in Germany. IPCom claimed that we had infringed a patent it holds concerning how smartphones gain access to a network, and sought preliminary injunction against us in the United Kingdom and France. As of the date of the Offering Circular, the High Court of Justice in the United Kingdom and Paris District Court in France have denied the application for the injunction. In addition, Xiaomi Corporation and a number of its subsidiaries were named as defendants in a lawsuit in 2019 filed by Sisvel International S.A. ("**Sisvel**"), a patent licensing and management company based in Luxembourg. Sisvel started preliminary injunction proceedings against us based on two patents it holds, arguing that we infringed the patents by implementing certain telecommunication standards with respect to our smartphones sold in the Netherlands. As of the date of the Offering Circular, the Hague Court of Appeal dismissed the preliminary injunction application. In 2020, Koninklijke Philips N.V. initiated proceedings in various jurisdictions including Germany, the United Kingdom, the Netherlands and India claiming global royalty payments and these proceedings are still ongoing.

In addition, we have also been, and may continue to be, subject to various intellectual property infringement or misappropriation claims as a result of digital content and internet services provided by our internet service providers and made available through our platform, such as games, videos and music. We may not be able to, in a timely manner, identify and remove all potential infringing content and services, and cannot assure you that intellectual property right infringement or misappropriation claims resulting from internet services providers' violations of their contractual obligations will not occur.

Regardless of the merit of particular claims, legal and administrative proceedings, such as litigation, injunctions and governmental investigations, may be expensive, time-consuming or disruptive to our operations and distracting to management. In recognition of these considerations, in the past we have entered into, and may enter into, new or further licensing agreements or other arrangements to settle litigation and resolve such disputes. No assurance can be given that such agreements can be obtained on acceptable terms or that litigation will not occur. These agreements may also significantly increase our operating expenses.

Legal or administrative proceedings and claims may arise in the future and the current legal or administrative proceedings and claims we face are subject to inherent uncertainties. If one or more legal or administrative matters were resolved against us or an indemnified third party for amounts in excess of our management's expectations or certain injunctions are granted to prevent us from using certain technologies in our products and services, our business and financial conditions could be materially and adversely affected. Further, such an outcome could result in significant compensatory, punitive or trebled monetary damages, disgorgement of revenue or profits, remedial corporate measures, injunctive relief or specific performance against us that could materially and adversely affect our financial condition and operating results.

***We may not be able to prevent others from unauthorized use of our intellectual property, which could harm our business and competitive position.***

We regard our trademarks, copyrights, patents, domain names, know-how, proprietary technologies and similar intellectual property as critical to our success, and we rely on a combination of intellectual property laws and contractual arrangements, including confidentiality, invention assignment and non-compete agreements with our employees and others, to protect our proprietary rights. We may become an attractive target to counterfeiting and intellectual property theft activity because of our brand recognition. Despite these measures, any of our intellectual property rights could be challenged, invalidated, circumvented or misappropriated, or such intellectual property may not be sufficient to provide us with competitive advantages. In addition, there can be no assurance that our patent applications will be approved, that any issued patents will adequately protect our intellectual property, or that such patents will not be challenged by third parties or found by a judicial authority to be invalid or unenforceable. Further, because of the rapid pace of technological change in our industry, parts of our business rely on technologies developed or licensed by third parties, and we may not be able to obtain or continue to obtain licenses and technologies from these third parties on reasonable terms, or at all.

It is often difficult to register, maintain and enforce intellectual property rights in mainland China. Statutory laws and regulations are subject to judicial interpretation and enforcement and may not be applied consistently due to the lack of clear guidance on statutory interpretation. Confidentiality, invention assignment and non-compete agreements may be breached by counterparties, and there may not be adequate remedies available to us for any such breach. Accordingly, we may not be able to effectively protect our intellectual property rights or to enforce our contractual rights in mainland China. Policing any unauthorized use of our intellectual property is difficult and costly and the steps we take may be inadequate to prevent the infringement or misappropriation of our intellectual property. In the event that we resort to litigation to enforce our intellectual property rights, such litigation could result in substantial costs and a diversion of our managerial and financial resources, and could put our intellectual property at risk of being invalidated or narrowed in scope. We can provide no assurance that we will prevail in any such litigation, and even if we do prevail, we may not obtain a meaningful recovery. In addition, our trade secrets may be leaked or otherwise become available to, or be independently discovered by, our competitors. Any failure in maintaining, protecting or enforcing our intellectual property rights could have a material adverse effect on our business, financial condition and results of operations.

Various other issues may arise with respect to our intellectual property portfolio. We and our ecosystem partners are co-owners of certain patents, certain other intellectual properties and user data related to hardware products produced by such partners. There is a possibility that our ecosystem partners may use these intellectual properties and user data to develop and manufacture competing products on their own or engage other companies to do so by leveraging such resources. In addition, we may not have sufficient intellectual property rights in all countries and regions where unauthorized third-party copying or use of our proprietary technology may occur and the scope of our intellectual property might be more limited in certain countries and regions. Our existing and future patents may not be sufficient to protect our products, services, technologies or designs and/or may not prevent others from developing competing products, services, technologies or designs. We cannot predict the validity and enforceability of our patents and other intellectual property with certainty.

***Our liquidity and financial condition may be materially and adversely affected if we fail to collect trade receivables from our customers in a timely manner, or at all.***

We cannot assure you that our customers will consistently make timely and full payments to us. If we fail to collect all or part of such payments in a timely manner, or at all, or if our major customers extend their trade receivables turnover days, our liquidity and financial condition may be materially and adversely affected.

***We face inventory and other asset risks in addition to purchase commitment cancelation risk.***

We record a write-down for inventories that have exceeded net realizable value. We have recorded provision for impairment of inventories in the amount of RMB652.6 million, RMB3,006.5 million, RMB3,859.7 million and RMB2,528.2 million for the years ended December 31, 2017, 2018, 2019 and for the nine months ended September 30, 2020, respectively. We also review our long-lived assets for impairment whenever events or circumstances indicate the carrying amount of an asset may not be recoverable. In addition, we are exposed to credit risk in relation to our loan receivables, and in the event of a substantial raise in the default exposure of these loan receivables, we will incur significant impairment charges. If we determine that impairment has occurred, we record a write-down equal to the amount by which the carrying value of the asset exceeds its fair value. Although we believe our provisions related to inventory, capital assets, inventory prepayments, loan receivables and other assets are currently adequate, no assurance can be given that we will not incur additional related charges given the rapid and unpredictable pace of product obsolescence in the industries in which we compete.

We must order products or components for our products and build inventory in advance of product announcements and shipments. Because our markets are volatile, competitive and subject to rapid technology and price changes, there is a risk that we may forecast incorrectly and order or produce either excess or insufficient amounts of components or products.

***Future operating results depend upon our ability to obtain raw materials, components and products in sufficient quantities on commercially reasonable terms.***

Because we currently obtain certain core raw materials and components from limited sources, we are subject to supply and pricing risks. Some raw materials and components, including those that are available from multiple sources, are at times subject to industry-wide shortages and significant commodity pricing fluctuations. While we have entered into agreements for the supply of many raw materials, components and IoT and lifestyle products, there can be no assurance that we will be able to extend or renew these agreements on similar terms, or at all. A number of suppliers of raw materials, components and products may suffer from poor financial conditions, which can lead to business failure for the supplier or consolidation within a particular industry, further limiting our ability to obtain sufficient quantities of raw materials and components on commercially reasonable terms. The effects of global or regional economic conditions on our suppliers also could affect our ability to obtain raw materials, components and products. Therefore, we remain subject to significant risks of supply shortages and price increases. Our new products may utilize customized components available from limited sources. When a component or product uses new technologies, initial capacity constraints may exist until the suppliers' yields have matured or manufacturing capacity has increased. Continued availability of these components at acceptable prices, or at all, may be affected for any number of reasons, including if those suppliers decide to concentrate on the production of common components and products instead of components and products customized to meet our requirements. The supply of components for a new or existing product could be delayed or constrained, and a key partner could delay shipments of completed products to us.

***We rely on US technologies for our products.***

We rely on US technologies for our products. Due to the ongoing US-China trade tensions, we cannot assure you that we will not be subjected to export restrictions imposed by the United States government in the future. If we were to experience any material disruption to our sourcing of technologies, equipment, software or raw materials from our US suppliers or those who utilize US technologies, we may not be able to switch to an alternative supplier of technologies, equipment and software within a short period time, or at all. In the event we are subjected to any export restriction that limits our ability to procure technologies, equipment and software, our business operations and financial results may be materially and adversely affected.

***We depend on component, product assembly and logistical services provided by suppliers and outsourcing partners. Such arrangements reduce our direct control over production and distribution. Any failure of our supply, assembly and logistics partners to perform their responsibilities or to be in compliance with all applicable laws and regulations may have a material negative impact on our cost or supply of components or finished goods.***

Substantially all of our assembly is performed in whole or in part by outsourcing partners located in mainland China, India and Indonesia. We have also outsourced much of our transportation and logistics management. While these arrangements may lower operating costs, they also reduce our direct control over production and distribution. We may experience operational difficulties with our suppliers and outsourcing partners, including reductions in the availability of production capacity, failures to comply with product specifications, insufficient quality control, failures to meet production deadlines, increases in assembling costs and required lead times. Our suppliers and outsourcing partners may experience disruptions in their production and assembly operations due to equipment breakdowns, labor strikes or shortages, natural disasters, component or material shortages, cost increases, environmental non-compliance issues or other similar problems. In addition, we may not be able to renew contracts with our suppliers and outsourcing partners or identify substitute partners who are capable of supplying services, components and assembly capacities for new products we target to launch in the future. Although arrangements with these partners may contain provisions for warranty expense reimbursement, we may remain responsible to the consumer for warranty service in the event of product defects and could experience an unanticipated product defect or warranty liability. Any failure of our supply, assembly and logistics partners to perform their responsibilities or to be in compliance with all applicable laws and regulations may have a material negative impact on our cost or supply of components or finished goods. In addition, assembly or logistics in our primary locations or transit to final destinations may be disrupted for a variety of reasons including, but not limited to, natural and man-made disasters, information technology system failures, commercial disputes, military actions or economic, business, labor, environmental, public health, or political issues.

***Any substantial decrease in the purchases for our products or services from our largest customers could have a material and adverse effect on us.***

We cannot assure you that we will be able to maintain good business relationships with our top customers going forward. Our top customers may not continue to provide us with new business in the future at a level similar to that in the past, or at all. Should any of our top customers reduce substantially the size of their purchases from with us or terminate their business relationship with us entirely for any reason, or is wound-up or fails to pay for its purchases on time, we cannot assure you that we will be able to secure new business from other customers to compensate for such substantial reduction in purchases or loss of business entirely. In addition, we cannot assure you that the new business secured from other customers for replacement, if any, will be on commercially comparable terms. If any of the foregoing materializes, our business, operating results and financial condition may be materially and adversely affected.

***Our products and services may experience quality problems from time to time that can result in decreased sales and operating margin and harm to our reputation.***

We offer complex hardware products and services that may contain design and manufacturing defects. Sophisticated operating system software and applications, such as those offered by us, may contain "bugs" that can unexpectedly interfere with the software's intended operation. Our internet services may from time to time experience outages, service slowdowns or are errors, or malicious attacks. Defects may also occur in components and products we purchase from third parties or assembled by our outsourcing partners. There can be no assurance that we will be able to detect and fix all defects in the hardware, software and services we offer. We may also need to conduct product recalls in case of product defects from time to time, which may require substantial costs of operational, managerial and financial resources. There is no assurance the product recalls will achieve satisfactory results. Failure to do so could result in lost revenue, significant warranty and other expenses, disputes and related legal proceedings, and harm to our reputation.

***Our future performance depends in part on support from third-party software developers.***

We believe decisions by users to purchase our hardware products depend in part on the availability of third-party software applications and services. There is no assurance that third-party developers will continue to develop and maintain software applications and services for our products. If third-party software applications and services cease to be developed and maintained for our products, customers may choose not to buy our products. Android devices are subject to rapid technological change, and, if third-party developers are unable to or choose not to keep up with this pace of change, third-party applications might not successfully operate and may result in dissatisfied customers. The availability and development of these applications also depend on developers' perceptions and analysis of the relative benefits of developing, maintaining or upgrading software for our devices rather than our competitors' platforms. If developers focus their efforts on these competing platforms, the availability and quality of applications for our devices may suffer.

***Our expansion into new product categories and substantial increase in SKUs may expose us to new challenges and more risks.***

In recent years, we have expanded our product offerings to include a wide range of IoT and lifestyle products. Expanding into diverse new product categories and substantially increasing our SKUs involves new risks and challenges. Our lack of familiarity with these products and lack of relevant customer data relating to these products may make it more difficult for us to anticipate user demand and preferences. We may misjudge user demand, resulting in inventory buildup and possible inventory write-down. It may also make it more difficult for us to inspect and control quality and ensure proper handling, storage and delivery. We may experience higher return rates on new products, receive more customer complaints about them and face costly product liability claims as a result of selling them, which would harm our brand and reputation as well as our financial performance. Furthermore, we may not have much purchasing power in new categories of products, and we may not be able to negotiate favorable terms with suppliers and ecosystem partners. We may need to price aggressively to gain market share or remain competitive in new categories. It may be difficult for us to achieve profitability in the new product categories and our profit margin, if any, may be lower than we anticipate, which would adversely affect our overall profitability and results of operations. We cannot assure you that we will be able to recoup our investments in introducing these new product categories.

***Rapid technological changes may result in impairment of our intangible assets, which could negatively affect our reported results of operations.***

Our intangible assets amounted to RMB2,274.4 million, RMB2,061.2 million, RMB1,672.0 million and RMB1,355.6 million as of December 31, 2017, 2018, 2019 and September 30, 2020, respectively. Among our intangible assets, trademarks, patents and domain names amounted to RMB723.2 million, RMB667.9 million, RMB550.8 million and RMB494.8 million as of December 31, 2017, 2018, 2019 and September 30, 2020, respectively. Trademarks, patents and domain names have a finite useful life and are carried at cost less accumulated amortization. Amortization is calculated using the straight-line method to allocate the cost of trademarks, patents and domain names over their estimated useful lives of one to 16 years. We are required to review our intangible assets for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable, including a decline in company value and a slowdown in our industry. Our products and services compete in highly competitive global markets characterized by, among other factors, rapid adoption of technological and product advancements by competitors, which could negatively affect the assumptions used in cash flow generated from relevant intangible assets for impairment assessment and the estimated useful lives of intangible assets. If the carrying value of our intangible assets are determined to be impaired, we would be required to write down the carrying value or record charges to earnings in our financial statements, thereby materially and adversely affecting our results of operations.

***We are subject to laws and regulations worldwide, changes to which could increase our costs and, individually or in the aggregate, adversely affect our business.***

We are subject to laws and regulations affecting our domestic and overseas operations in a number of areas. These mainland Chinese and foreign laws and regulations affect our activities including, but not limited to, in areas of labor, advertising, digital content, consumer protection, real estate, billing, e-commerce, promotions, quality of services, telecommunications, mobile communications and media, television, intellectual property ownership and infringement, tax, import and export requirements, anti-corruption, foreign exchange controls and cash repatriation restrictions, data privacy requirements, anti-competition, environmental, health and safety. In the case any of these is violated and such violation leads to legal proceedings, it could disrupt our business, distract our management's attention and subject us to substantial uncertainties as to the outcome of any such legal proceedings.

By way of example, laws and regulations related to mobile communications and media devices in the many jurisdictions in which we operate are extensive and subject to change. Such changes could include, among others, restrictions on the production, assembly, distribution and use of devices. These devices are also subject to certification and regulation by governmental and standardization bodies, as well as by cellular network carriers for use on their networks. These certification processes are extensive and time consuming, and could result in additional testing requirements, product modifications, or delays in product shipment dates, or could preclude us from selling certain products.

Compliance with these laws, regulations and similar requirements may be onerous and expensive, and they may be inconsistent from jurisdiction to jurisdiction, further increasing the cost of compliance and doing business. Any such costs, which may rise in the future as a result of changes in these laws and regulations or in their interpretation, could individually or in the aggregate make our products and services less attractive to our users, delay the introduction of new products in one or more regions, or cause us to change or limit our business practices. There can be no assurance that our employees, contractors, agents, or business partners will not violate such laws and regulations or our compliance policies and procedures.

***Policy changes affecting international trade, including the imposition of tariffs and the resulting consequences, may have a material adverse impact on our business, operating results and financial condition.***

We have exported our products to a large number of foreign countries and derive significant sales from exporting to these countries. In the event that any of these countries which we export to imposes trade sanctions on mainland China or enforces import restriction or tariffs in relation to hardware devices, our business and operations may be adversely affected. Furthermore, we rely on certain overseas suppliers to obtain components and raw materials for the assembling of our hardware devices. In the event that mainland Chinese government imposes import tariffs, trade restrictions or other trade barriers affecting the importation of such components or raw materials, we may not be able to obtain a steady supply of necessary components or raw materials at competitive prices, and our business and operations may be materially and adversely affected.

In particular, there have been ongoing discussions and commentary regarding potential significant changes to the United States trade policies, treaties, tariffs and taxes, including trade policies and tariffs regarding

China. On August 14, 2017, the President of the United States issued a memorandum instructing the United States Trade Representative, or the USTR, to determine whether to investigate under section 301 of the United States Trade Act of 1974, laws, policies, practices, or actions of the Chinese government that may be unreasonable or discriminatory and that may be harming United States intellectual property rights, innovation, or technology development. Based on information gathered in that investigation, the USTR published a report on March 22, 2018 on the acts, policies and practices of the Chinese government supporting findings that such are unreasonable or discriminatory and burden or restrict United States commerce. On March 8, 2018, the President exercised his authority to issue the imposition of significant tariffs on imports of steel and aluminum from a number of countries, including China. Subsequently, the USTR announced an initial proposed list of 1,300 goods imported from China that could be subject to additional tariffs and initiated a dispute with the World Trade Organization against China for alleged unfair trade practices. The President has indicated that his two primary concerns to be addressed by China are (i) a mandatory $100 billion reduction in the China/United States trade deficit and (ii) limiting the planned $300 billion Chinese government support for advanced technology industries including artificial intelligence, semiconductors, electric cars and commercial aircraft. On July 6, 2018, the United States initially imposed a 25% tariff on $34 billion worth of Chinese goods, including agriculture and industrial machinery, which prompted the Chinese government to initially impose tariffs on $34 billion worth of goods from the United States, including beef, poultry, tobacco and cars. Since July 2018, the United States imposed tariffs on $250 billion worth of Chinese products and has threatened tariffs on $325 billion more. In response, China imposed tariffs on $110 billion worth of U.S. goods, and threatened qualitative measures that would affect U.S. businesses operating in China. In May 2019, the United States raised the tariffs on $100 billion of Chinese products to 25% from 10%, and were expected to increase further to 30% on October 15, 2019, however such increase was suspended pending negotiation of a "phase one" trade agreement with China. On August 1, 2019, President Trump announced a new 10% ad valorem duty on additional categories of goods imported from China, which amount was then increased to 15% on August 23, 2019. The new tariff at the rate of 15% became effective September 1, 2019 with respect to certain categories of goods and was expected to become effective for additional categories of goods on December 15, 2019. On December 13, 2019 the U.S. and China signed a "phase one" trade agreement, which avoided the imposition of additional tariffs. However, there can be no assurances that the U.S. or China will not increase tariffs or impose additional tariffs in the future.

Due to security-related concerns, U.S. government actions targeting exports of certain technologies to China are becoming more pervasive. In May 2019, President Trump issued an executive order that invoked national emergency economic powers to implement a framework to regulate the acquisition or transfer of information communications technology in transactions that imposed undue national security risks. The executive order was extended in May 2020. President Trump also issued an additional executive order in November 2020 further restricting investments from the United States into certain categories of PRC corporations. While these executive orders do not currently apply to our products, there is no assurance that these actions would not lead to additional restrictions on the sale of telecommunications products to the United States in the future, including those that we manufacture and produce. Any such restrictions imposed by the United States or any other countries may make it more difficult us to sell our products to these countries, which may in turn have a material adverse effect on our business.

There is significant uncertainty about the future relationship between the United States and other countries with respect to the trade policies, treaties, taxes, government regulations and tariffs that would be applicable. It is unclear what changes might be considered or implemented and what response to any such changes may be by the governments of other countries. Significant tariffs or other restrictions placed on Chinese imports and any related counter-measures that are taken by China could have an adverse effect on our financial condition or results of operations. Even in the absence of further tariffs, the related uncertainty and the market's fear of an escalating trade war might create forecasting difficulties for us and cause our customers and business partners to place fewer orders for our products and services, which could have a material adverse effect on our business, liquidity, financial condition, and/or results of operations. These developments, or the perception that any of them could occur, may have a material adverse effect on global economic conditions and the stability of global financial markets, and may significantly reduce global trade and, in particular, trade between these nations and the United States. Any of these factors could depress economic activity and restrict our access to suppliers or customers and have a material adverse effect on our business, financial condition and results of operations and affect our strategy around the world. Given the relatively fluid regulatory environment in China and the United States and relative uncertainty with respect to tariffs, international trade agreements and policies, a trade war, further governmental action related to tariffs or international trade policies, or additional tax or other regulatory changes in the future could directly and adversely impact our financial results and results of operations.

***We are subject to governmental economic sanctions laws that could subject us to liability and impair our ability to compete in overseas markets.***

Exports of our products must be made in compliance with various economic and trade sanctions laws in different jurisdictions. For example, U.S. economic sanctions prohibit the provision of products and services to countries, governments, and persons targeted by certain U.S. sanctions, and U.S. export control laws restrict the provision of U.S. origin products to certain targets of U.S. export controls. United Kingdom financial sanctions and European Union sanctions also have similar regimes to prohibit the provision of products and services to countries, governments and persons on their respective target list. Even though we take precautions to prevent our products from being provided to any target of these sanctions, there might be unauthorized downstream sales of our products to destinations not permitted under our policy despite such precautions. Any such provision could have negative consequences, including government investigations, penalties and reputational harm. We could be subject to future enforcement action with respect to compliance with governmental economic sanctions laws that result in penalties and costs that could have a material effect on our business and operating results.

***Our success depends largely on the continued service of our senior management and key personnel and the continued thriving of our corporate culture and values.***

Much of our future success depends on the continued contributions of our senior management and other key employees, many of whom are difficult to replace. The loss of the services of any of our executive officers, especially our executive Director, Founder, Chairman and Chief Executive Officer, Lei Jun, our senior management team and other highly skilled employees could harm our business. Competition for qualified talent is intense, particularly in the internet and technology industries. Our future success depends on our ability to attract a large number of qualified employees and retain existing key employees. If we are unable to do so, our business and growth may be materially and adversely affected.

Our unique corporate culture, being genuinely open, dynamic and collaborative, is driven by our founding team members who are all engineers or product designers. We value our users highly and firmly believe that the benefits of technological innovation should be easily accessible to everyone. Our corporate culture and values have empowered our rapid growth in the past, and we may risk losing the trust of our users, employees and partners and our operations may be materially and adversely affected if we fail to maintain our unique corporate culture and values.

***If we are unable to recruit, train and retain qualified personnel or sufficient workforce while controlling our labor costs, our business may be materially and adversely affected.***

We intend to hire additional qualified employees to support our business operations and planned expansion. Our future success depends, to a significant extent, on our ability to recruit, train and retain qualified personnel, particularly technical, marketing and other operational personnel with experience in the Internet industry. Our experienced mid-level managers are instrumental in implementing our business strategies, executing our business plans and supporting our business operations and growth. The effective operation of our managerial and operating systems also depends on the hard work and quality performance of our management and employees. Since our industry is characterized by high demand and intense competition for talent and labor, we can provide no assurance that we will be able to attract or retain qualified staff or other highly skilled employees that we will need to achieve our strategic objectives. Labor costs in mainland China and elsewhere have increased with global economic development. In addition, our ability to train and integrate new employees into our operations may also be limited and may not meet the demand for our business growth in a timely fashion, or at all, and rapid expansion may impair our ability to maintain our corporate culture.

***Any deterioration of our relationship with our third-party online distribution partners could have a material adverse effect on our business and results of operations.***

We sell our products through a global online distribution network comprising of third-party online distribution partners. In mainland China, we cooperate with leading e-commerce players such as JD.com. In many overseas markets, the third-party e-commerce marketplaces in which our products are sold primarily include Flipkart and Amazon. These third-party e-commerce players are important distribution channels for our products. We typically enter into a non-exclusive framework agreement with each of them, receive orders from them on a regular basis and deliver our products within our committed timeline.

Our current agreements with partners and other third parties generally do not prohibit them from working with our competitors or from selling competing products. Our competitors may be more effective in providing incentives to our third-party online distribution partners to favor our competitors' products and promote their sales. In addition, if our third-party online distribution partners are not successful in selling our products due to various reasons, including lower demand, market competition and decreasing efficiency of distribution network, our revenue may decrease. Pursuing, establishing and maintaining relationships with our third-party online distribution partners requires significant time and resources. We cannot assure you that we will be able to renew those framework agreements upon its expiry or on acceptable terms. If, for any reason, our relationship with our third-party online distribution partners deteriorates, our business and results of operations may be materially and adversely affected.

***Our retail stores have required and will continue to require a substantial investment and commitment of resources and are subject to numerous risks and uncertainties.***

Our retail stores have required substantial investment in equipment and leasehold improvements, information systems, inventory and personnel. We also have entered into substantial operating lease commitments for retail space. A decline in sales or the closure or poor performance of individual or multiple stores could result in significant lease termination costs, write-offs of equipment and leasehold improvements and severance costs. Many factors unique to retail operations, some of which are beyond our control, pose risks and uncertainties. These risks and uncertainties include, but are not limited to, macro-economic factors that could have an adverse effect on general retail activity, as well as our inability to manage costs associated with store construction and operation, more challenging environments in managing retail operations, costs associated with unanticipated fluctuations in the value of retail inventory, and our inability to obtain and renew leases in quality retail locations at a reasonable cost.

***We face risks relating to our acquisitions, investments and alliances.***

We have invested, and in the future, may invest, in a diverse array of businesses, technologies and ventures, and may enter into acquisitions and alliances from time to time. Such endeavors may involve significant risks and uncertainties, including distraction of management from current operations, greater than expected liabilities and expenses and unidentified issues not discovered in our due diligence. These new ventures are inherently risky and may not be successful. In addition, upon completion of an investment or acquisition, we may allocate significant resources to the integration of new business into our existing business to realize synergetic benefits. The integration process involves certain risks and uncertainties, some of which are outside our control, and there can be no assurance that we will be able to realize the anticipated benefits, synergies, cost savings or efficiencies. These transactions also involve significant challenges and risks in the following aspects, among others:

- for investments over which we do not obtain control, we may lack influence over the operations of these investees, which may prevent us from achieving our strategic goals in these investments;
- uncertain return of capital;
- unforeseen or hidden liabilities or additional operating losses, costs and expenses that may adversely affect us following our acquisitions or investments; and

- the impact of the fair value changes of investments measured at fair value through profit or loss on our financial performance and the associated uncertainties in accounting estimates as the valuations of these investments require the use of unobservable inputs and judgments.

In addition, we may experience constraints on our liquidity because gains or losses from those investments do not give rise to any change in our cash position unless we dispose of the relevant assets or receive dividend payments.

***Our business and reputation may be impacted by information technology system failures or network disruptions.***

We may be subject to information technology system failures or network disruptions caused by natural disasters, accidents, power disruptions, telecommunications failures, acts of terrorism or war, computer viruses, physical or electronic break-ins, or other events or disruptions. System redundancy and other continuity measures may be ineffective or inadequate, and our business continuity and disaster recovery planning may not be sufficient for all eventualities. Such failures or disruptions could adversely impact our business by, among other things, preventing access to our internet services, interfering with customer transactions or impeding the assembling and shipping of our products. These events could materially and adversely affect our reputation, financial condition and operating results, or result in adverse publicity, claims or other legal proceedings against us.

***Our delivery, return and exchange policies may adversely affect our results of operations.***

We have adopted shipping policies that do not necessarily pass the full cost of shipping onto our users. We also have adopted customer-friendly return and exchange policies that make it convenient and easy for customers to change their minds after completing purchases. We may also be required by law to adopt new or amend existing return and exchange policies from time to time. These policies improve users' shopping experience and promote customer loyalty, which in turn help us acquire and retain users. However, these policies also subject us to additional costs and expenses which we may not recoup through increased revenue. If our return and exchange policy is misused by a significant number of customers, our costs may increase significantly and our results of operations may be materially and adversely affected. If we revise these policies to reduce our costs and expenses, our users may be dissatisfied, which may result in loss of existing users or failure to acquire new users at a desirable pace, which may materially and adversely affect our results of operations.

***We may be subject to product liability claims if people or properties are harmed by the products we sell.***

Some products we sell may be defective. As a result, sales of such products could expose us to product liability claims relating to personal injury or property damage and may require product recalls or other actions. Third parties subject to such injury or damage may bring claims or legal proceedings against us as the seller of the product. Although we would have legal recourse against the suppliers and manufacturers of such products under laws, attempting to enforce our rights against the suppliers and manufacturer may be expensive, time-consuming and ultimately futile. We maintain third-party liability insurance and product liability insurance in relation to products we sell through certain distribution channels and in certain markets. However, such insurance coverage might be insufficient to fully cover all damages sought and the claim process might be prolonged. As a result, any material product liability claim or litigation could have a material and adverse effect on our business, financial condition and results of operations. Even unsuccessful claims could result in the expenditure of funds and managerial efforts in defending them and could have a negative impact on our reputation.

***Failure to renew our current leases or locate desirable alternatives for our facilities could materially and adversely affect our business.***

We lease properties for certain of our offices and offline retail stores. We may not be able to successfully extend or renew such leases upon expiration of the current term on commercially reasonable terms, or at all, and may therefore be forced to relocate our affected operations. This could disrupt our operations and result in significant relocation expenses, which could adversely affect our business, financial condition and results of operations. In addition, we compete with other businesses for premises at certain locations or of desirable sizes. As a result, even though we could extend or renew our leases, rental payments may significantly increase as a result of the high demand for the leased properties. In addition, we may not be able to locate desirable alternative sites for our facilities as our business continues to grow and failure in relocating our affected operations could adversely affect our business and operations.

***We have limited experience in operating an internet finance business, which is an emerging and evolving industry subject to developing regulations in mainland China. Significant deterioration in the asset quality of our internet finance business may have an adverse effect on our business, results of operations and financial condition.***

We have limited experience in operating an internet finance business, and increasing exposure to credit risks or significant deterioration in the asset quality of our financing business may materially and adversely affect our business, financial condition, and results of operation. The internet finance industry in mainland China is new, and the regulatory framework for this industry is also evolving and may remain uncertain for the foreseeable future. We have developed various financial products and consumer financing solutions. Operating and expanding in this new business area involves new risks and challenges. For example, our Airstar Bank, a Hong Kong-based virtual bank is still nascent and may be subject to losses. For certain financial products, we have committed or will commit our own capital. Our lack of familiarity with the internet finance sector may make it difficult for us to anticipate the demands and preferences in the market and develop financial products that meet those preferences. We may not be able to successfully identify new product and service opportunities or develop and introduce these opportunities to our users in a timely and cost-effective manner, or our users may be disappointed in the returns from financial products that we offer. The risk of non-payment of loans is inherent in the internet financing business and we are subject to credit risk resulting from defaults in payment for loans by our customers. Credit risks may be exacerbated in micro-credit financing because there will be relatively limited information available about the credit histories of the borrowers. We cannot assure you that our monitoring of credit risk issues and our efforts to mitigate credit risks through our credit assessment and risk management policies are or will be sufficient to result in lower delinquencies. Furthermore, our ability to manage the quality of our loan portfolio and the associated credit risks will have significant impact on the results of operations of our internet finance business. Deterioration in the overall quality of loan portfolio and the increasing exposure to credit risks may occur due to a variety of reasons, including factors beyond our control, such as a slowdown in the growth of the global or Chinese economies or a liquidity or credit crisis in the global or Chinese finance sectors, which may materially and adversely affect our businesses, operations or liquidity of our consumers or their ability to repay or roll over their debt. Any significant deterioration in the asset quality of our internet finance business and significant increase in associated credit risks may materially and adversely affect our business, financial condition and results of operations.

Meanwhile, the regulatory framework for internet financing business is evolving and may remain uncertain for the foreseeable future. Mainland China's internet financing industry in general remains at a rather preliminary development stage and may not develop at the anticipated pace. It is possible that the PRC laws and regulations may change in ways that do not favor our development. If that happens, our internet financing business may be adversely affected.

***Our financial performance is subject to risks associated with changes in the value of the U.S. dollar versus local currencies.***

Our primary exposure to movements in foreign currency exchange rates relates to sales in overseas markets that are not denominated in Renminbi or U.S. dollars. For example, sales in India are denominated in Indian Rupee, and expenses, especially cost of sales, incurred in many overseas markets are denominated in U.S. dollars. Our sales denominated in euro and a variety of other foreign currencies have also increased in recent years as our overseas operations expanded. Weakening of a foreign currency such as the Indian Rupee relative to the U.S. dollar adversely affects the U.S. dollar value of our sales and earnings denominated in such foreign currency, and generally leads to increased prices in the foreign market, potentially reducing demand for our products. Margins on sales of our products in overseas markets, which include components procured from with U.S. dollars, could be materially and adversely affected by foreign currency exchange rate fluctuations. In some circumstances, for competitive or other reasons, we may decide not to raise local prices to fully offset the U.S. dollar's strengthening, or at all, which would adversely affect the U.S. dollar value of our sales and earnings denominated in foreign currencies. Additionally, strengthening of foreign currencies, primarily the U.S. dollar, may increase our cost of product components denominated in those currencies, thus adversely affecting gross margins.

***Higher labor costs and inflation may adversely affect our business and our profitability.***

Labor costs in mainland China and many overseas markets have risen in recent years. Rising labor costs may be reflected in the manufacturing fees charged by our outsourcing partners to us and in the prices of finished goods. In addition, we have witnessed growing inflation rates in many areas of the world, and particularly in Asia where we procure most of our raw materials, which adversely affects us and our suppliers alike.

The rising costs as a result of higher labor cost of our outsourcing partners and ecosystem partners, as well as increasing raw material prices, cannot be easily passed to end users in the form of higher retail sale prices due to severe competition in the smart device market. Our profitability therefore may be adversely affected if labor cost and inflation continue to rise in the future.

***We could be subject to changes in our tax rates, the adoption of new domestic or international tax legislation or exposure to additional tax liabilities.***

We are subject to taxes in mainland China and numerous jurisdictions in the rest of the world. Due to economic and political conditions, tax rates in various jurisdictions may be subject to significant change. Our effective tax rates could be affected by changes in the mix of earnings in countries with differing statutory tax rates, changes in the valuation of deferred tax assets and liabilities, or changes in tax laws or their interpretation.

We are also subject to the examination of its tax returns and other tax matters by domestic and international tax authorities and governmental bodies. We regularly assess the likelihood of an adverse outcome resulting from these examinations to determine the adequacy of our provision for taxes. There can be no assurance as to the outcome of these examinations. If our effective tax rates were to increase, or if the ultimate determination of our taxes owed is for an amount in excess of amounts previously accrued, our financial condition, operating results and cash flows could be adversely affected.

***Our use of open source software could negatively affect our ability to sell our products and subject us to possible litigation.***

A portion of the technologies we use incorporates open source software, and we may incorporate open source software in the future. For example, some of our technologies for program code writing, compiling and reviewing, code base management and HTTP & HTTP/2 client services use open source software. Such open source software is generally licensed by its authors or other third parties under open source licenses. These licenses may subject us to certain unfavorable conditions, including requirements that we offer our products and services that incorporate the open source software for no cost, that we make publicly available source code for modifications or derivative works we create based upon, incorporating, or using the open source software, or that we license such modifications or derivative works under the terms of the particular open source license. Additionally, if a third-party software provider has incorporated open source software into software that we license from such provider, we could be required to disclose or provide at no cost any of our source code that incorporates or is a modification of such licensed software. If an author or other third party that distributes open source software that we use or license were to allege that we had not complied with the conditions of the applicable license, we could be required to incur significant legal expenses defending against such allegations and could be subject to significant damages and enjoined from the sale of our products and services that contained the open source software. Any of the foregoing could disrupt the distribution and sale of our products and services and harm our business.

***We may need additional capital, and financing may not be available on terms acceptable to us, or at all.***

In light of our historical cash needs and our rapid growth, we may in the future require additional cash resources due to changed business conditions or other future developments, including any changes in our pricing policy, marketing initiatives or investments we may decide to pursue. If these resources are insufficient to satisfy our cash requirements, we may seek to obtain a credit facility or sell additional equity or debt securities. The sale of additional equity securities could result in dilution of our existing shareholders. The incurrence of indebtedness would result in increased debt service obligations and could result in operating and financing covenants that would restrict our operations. It is uncertain whether financing will be available in amounts or on terms acceptable to us, if at all.

***We have limited insurance coverage which could expose us to significant costs and business disruption.***

We maintain various insurance policies to safeguard against risks and unexpected events. We maintain limited third-party insurance policies covering certain potential risks and liabilities including product liability, property and construction liability. We maintain trade insurance for our overseas transactions in many overseas markets. We also provide social security insurance including pension insurance, unemployment insurance, work-related injury insurance and medical insurance for our employees in mainland China, as well as statutorily required insurance coverage for overseas employees. However, as the insurance industry in mainland China is still in an early stage of development, insurance companies in mainland China generally do not offer as extensive an array of insurance products as insurance companies do in countries with more developed economies. We cannot assure you that our insurance coverage is sufficient to cover all our risk exposure and prevent us from any loss or that we will be able to successfully claim our losses under our current insurance policy on a timely basis, or at all. If we incur any loss that is not covered by our insurance policies, or the compensated amount is significantly less than our actual loss, our business, financial condition and results of operations could be materially and adversely affected.

In addition, in line with general market practice, we do not maintain sufficient business interruption insurance, which is not mandatory under laws in mainland China. We also do not maintain sufficient key-man life insurance or insurance policies covering damages to our IT infrastructure or IT systems. Any disruption in our IT infrastructure or IT systems or natural disasters may cause us to incur substantial costs, and we have no insurance to cover such losses. As a result, our business, financial condition and results of operations could be materially and adversely affected.

***We may be the subject of anti-competitive, harassing, or other detrimental conduct by third parties including complaints to regulatory agencies, negative blog postings, and the public dissemination of malicious assessments of our business that could harm our reputation and cause us to lose market share, customers and revenue.***

We may be the target of anti-competitive, harassing, or other detrimental conduct by third parties. Such conduct includes complaints, anonymous or otherwise, to regulatory agencies. We may be subject to government or regulatory investigation as a result of such third-party conduct and may be required to expend significant time and incur substantial costs to address such third-party conduct, and there is no assurance that we will be able to conclusively refute each of the allegations within a reasonable period of time, or at all. Additionally, allegations, directly or indirectly against us, may be posted online by anyone, whether or not related to us, on an anonymous basis. Consumers value readily available information concerning retailers, manufacturers, and their goods and services and often act on such information without further investigation or authentication and without regard to its accuracy. The availability of information on social media is virtually immediate, as is its impact. Social media immediately publish the content their subscribers and participants post, often without filters or checks on the accuracy of the content posted. Information posted may be inaccurate and adverse to us, and it may harm our financial performance, prospects or business. The harm may be immediate without affording us an opportunity for redress or correction. Our reputation may be negatively affected as a result of the public dissemination of anonymous allegations or malicious statements about our business, which in turn may cause us to lose market share, customers and revenues.

***We have incurred a loss and had a net liability position in the past.***

We incurred a loss of RMB43.9 billion in 2017 and generated a profit of RMB13.5 billion and RMB10.1 billion in 2018 and 2019, respectively. In addition, we had net liabilities of RMB127.2 billion as of December 31, 2017 and net assets of RMB71.3 billion and RMB81.7 billion as of December 31, 2018 and 2019, respectively. We cannot assure you that we will be able to continue to generate profits or avoid a net liability position in the future.

***Political instability or a change in economic liberalization and deregulation policies could seriously harm business and economic conditions in India, generally, and our business, in particular.***

Our business could be significantly influenced by political instability and economic policies adopted by the Government of India. Since 1991, successive governments have pursued policies of economic liberalization and financial sector reforms. The Government of India has in recent years sought to implement economic reforms and the current Government of India has implemented policies and undertaken initiatives that continue the economic liberalization policies pursued by previous governments. There can be no assurance that liberalization policies will continue in the future, especially given the current cross-border conflict between India and China. The rate of economic liberalization could change, and specific laws and policies affecting foreign investment, currency exchange rates and other matters affecting investment in India could change as well.

The Government of India has traditionally exercised and continues to exercise influence over many aspects of the economy. A change in the Government of India's economic liberalization and deregulation policies could disrupt business and economic conditions in India generally, and specifically our business and operations, as a substantial portion of our revenues are derived from India. This could have a material adverse effect on our financial condition and results of operations.

***The UK's withdrawal from the EU, commonly referred to as Brexit, could have an adverse effect on our business in Europe.***

Brexit will continue to create significant uncertainty concerning the future relationship between the UK and the EU, particularly if the recent UK withdrawal from the EU in January 2020 is followed by a failure to agree to a future trading relationship between the EU and the UK. Since a significant portion of the regulatory framework in the UK is derived from EU laws, Brexit could materially impact the regulatory regime with respect to the development, importation, approval and marketing of our products in the UK or the EU. All of these changes, if they occur, could have a negative impact on our business in the UK or the EU, such as decreased efficiency in logistics, increased costs related to tariffs and trade barriers and fluctuations in exchange rates.

***Certain facts and statistics are derived from publications not independently verified by us, the Managers or their respective advisors.***

Facts and statistics in this Offering Circular relating to China's economy and the industries in which we operate are derived from publicly available sources. While we have taken reasonable care to ensure that the facts and statistics presented are accurately reproduced from such sources, they have not been independently verified by us, the Managers or their respective advisors and, therefore, we make no representation as to the accuracy of such facts and statistics, which may not be consistent with other information compiled within or outside China. If the calculation and collection methods are ineffective or there are other problems, the facts and statistics herein may be inaccurate or may not be comparable to facts and statistics produced for other economies and should not be unduly relied upon.

## Risks Relating to Doing Business in Mainland China

***If we fail to obtain and maintain the requisite licenses and approvals required under the complex regulatory environment applicable to our businesses in mainland China, or if we are required to take compliance actions that are time-consuming or costly, our business, financial condition and results of operations may be materially and adversely affected.***

The internet and mobile industries in mainland China are highly regulated. Our subsidiaries and variable interest entities in mainland China are required to obtain and maintain applicable licenses and approvals from different regulatory authorities in order to provide their current services. Under the current regulatory scheme in mainland China, a number of regulatory agencies, including but not limited to the State Administration of Radio and TV ("**SART**"), the MOC, the MIIT, and the SCIO, jointly regulate major aspects of the internet industry, including the mobile internet and mobile games businesses. Operators must obtain various government approvals and licenses for relevant internet business.

We have obtained ICP licenses for provision of internet information services, Value-added Telecommunications Business License for information services (excluding internet information services), Value-added Telecommunications Business License for domestic multi-party communications, Approval for Mobile Communications Resale Services, Online Culture Operating Licenses for shows, plays and performances through internet, Online Culture Operating Licenses for the operation of online games, Online Publishing Service Licenses, Payment Business Licenses and Approval for Operating Small-sum Loan Company, which are generally subject to regular government review or renewal. We cannot assure you that we can successfully update or renew the licenses required for our business in a timely manner or that these licenses are sufficient to conduct all of our present or future business.

The financial services industry in China is also highly regulated, and financial institutions are subject to a myriad of regulations, many of which are rapidly evolving. In particular, PRC regulatory authorities have in recent years tightened regulations with respect to conducting online financing business. For example, the CBIRC published the Interim Measures for the Administration of Internet Loans of Commercial Banks (商業銀行互聯網貸款管理暫行辦法) in July 2020 (the "**New Online Lending Rules**"), which stresses the importance of risk data and risk model management and requires commercial banks to build a comprehensive risk management system for online lending business.

On November 2, 2020, the PBOC and the CBIRC issued the draft Interim Measures for the Administration of Online Micro-lending (the "**Draft Online Micro-lending Measures**"). Aiming to enhance the regulation of online micro-lending, the Draft Online Micro-lending Measures, which was open for public feedback until December 2, 2020, proposed, *among other things*, a RMB5 billion registered capital threshold for online micro-lenders that operate across different provincial regions, and a RMB1 billion registered capital threshold for online micro-lenders that only operate within the respective province in which they are established. In addition, the Draft Online Micro-lending Measures also introduces a set of new requirements for online micro-lenders' shareholders, such as the controlling shareholder shall have been profitable for the last two consecutive years and have paid in aggregate no less than RMB12 million in tax. The Draft Online Micro-lending Measures also cap the balance of an online micro-lender through issuance of bonds and asset-backed securities at four times of its net assets and at one time of its net assets if borrowed from its shareholders or banks. The size of loans shall not exceed RMB300,000 for each individual or one-third of the borrower's average annual income for the last three years (whichever is lower), or RMB1 million for each business entity.

Online micro-lending companies that conduct business across the regions will be supervised directly by CBIRC, rather than local authorities and are required to share the borrowers' credit information with credit agencies approved by the central bank or other credit rating system such as the Financial Credit Information Data Center. Existing online micro-lending companies will have certain transition periods (three years for online micro-leaders operating across the provincial regions and one year for other online micro-lenders) to become fully compliant with the Draft Online Micro-lending Measures or their online micro-lending license may be revoked.

Considerable uncertainties exist regarding the interpretation and implementation of existing and future laws and regulations governing our business activities. We cannot assure you that we will not be found in violation of any future laws and regulations or any of the laws and regulations currently in effect due to changes in the relevant authorities' interpretation of these laws and regulations. If we fail to complete, obtain or maintain any of the required licenses or approvals or make the necessary filings, we may be subject to various penalties, such as confiscation of the revenue that was generated through the unlicensed internet or mobile activities, the imposition of fines and the discontinuation or restriction of our operations. Any such penalties may disrupt our business operations and materially and adversely affect our business, financial condition and results of operations.

***Adverse changes in economic and political policies of the mainland Chinese government could have a material adverse effect on overall economic growth in mainland China, which could materially and adversely affect our business and results of operation.***

A significant portion of our operations are conducted in mainland China and a significant portion of our revenue are sourced from mainland China. Accordingly, our results of operations, financial condition and prospects are influenced by economic, political and legal developments in mainland China. Economic reforms have resulted in significant economic growth in mainland China in the past few decades. However, any economic reform policies or measures in mainland China may from time to time be modified or revised. Mainland China's economy differs from the economies of most developed countries in many respects, including with respect to the amount of government involvement, level of development, growth rate, control of foreign exchange and allocation of resources. While the Chinese economy has experienced significant growth in the past few decades, the rate of growth has slowed down since 2012, and growth has been uneven across different regions and among various economic sectors.

The mainland Chinese government exercises significant control over mainland China's economic growth through strategically allocating resources, controlling the payment of foreign currency-denominated obligations, setting monetary policy and providing preferential treatment to particular industries or companies. Although the Chinese economy has grown significantly in the past decade, that growth may not continue and any slowdown may have a negative effect on our business. Any adverse changes in economic conditions in mainland China, in the policies of the mainland Chinese government or in the laws and regulations in mainland China, could have a material adverse effect on the overall economic growth of mainland China. Such developments could adversely affect our businesses, lead to reduction in demand for our products and adversely affect our competitive position.

***The legal system in mainland China embodies uncertainties which could limit the legal protections available to us.***

The legal system in mainland China is a civil law system based on written statutes. Unlike common law systems, it is a system in which decided legal cases have little precedential value. The legal system in mainland China evolves rapidly, and the interpretations of many laws, regulations and rules may contain inconsistencies. Our WFOEs are incorporated in mainland China and are wholly-owned by us. Our WFOEs are subject to laws and regulations applicable to foreign investment in mainland China in general, as well as specific laws and regulations applicable to wholly foreign-owned enterprises. However, these laws, regulations and legal requirements are constantly changing and their interpretation and enforcement involve uncertainties. These uncertainties could limit the legal protections available to us. In addition, we cannot predict the effect of future developments in the mainland Chinese legal system, particularly with regard to internet-related industries, including the promulgation of new laws, changes to existing laws or the interpretation or enforcement thereof, or the preemption of local regulations by national laws. Such unpredictability towards our contractual, property (including intellectual property) and procedural rights could adversely affect our business and impede our ability to continue our operations. Furthermore, any litigation in mainland China may be protracted and result in substantial costs and diversion of resources and management attention.

***Regulation and censorship of information disseminated over the internet in mainland China may adversely affect our business and subject us to liability for content posted on our platform.***

Internet companies in mainland China are subject to a variety of existing and new rules, regulations, policies, and license and permit requirements. In connection with enforcing these rules, regulations, policies and requirements, relevant government authorities may suspend services by, or revoke licenses of, any internet or mobile content service provider that is deemed to provide illicit content online or on mobile devices, and such activities may be intensified in connection with any ongoing government campaigns to eliminate prohibited content online. For example, in July 2016, the Ministry of Public Security launched a "Special Rectification Activities for Live Streaming Websites" campaign. Based on publicly available information, the campaign aims to eliminate illicit or pornographic information and content on live streaming websites by, among other things, holding liable individuals and corporate entities that facilitate the distribution of illicit or pornographic information and content. For details of regulations on information security and censorship, see the section headed "*Regulations – Regulations Relating to Information Security and Censorship*."

We endeavor to eliminate illicit content from our apps and websites. However, government standards and interpretations may change in a manner that could render our current monitoring efforts insufficient. We cannot assure you that our business and operations will be immune from government actions or sanctions in the future. If government actions or sanctions are brought against us, or if there are widespread rumors that government actions or sanctions have been brought against us, our reputation and brand image could be harmed, we may lose users and business partners, our revenue and results of operation may be materially and adversely affected.

***We may be classified as a "resident enterprise in mainland China" for mainland Chinese enterprise income tax purposes, which could result in unfavorable tax consequences to us and our shareholders and have a material adverse effect on our results of operations and the value of your investment.***

Under the People's Republic of China Enterprise Income Tax Law, or the EIT Law, which became effective on January 1, 2008 and subsequently amended on February 24, 2017 and December 29, 2018, an enterprise established outside mainland China whose "de facto management body" is located in mainland China is considered a "resident enterprise in mainland China" and will generally be subject to the uniform 25% enterprise income tax rate, or the EIT rate, on its global income. Under the implementation rules of the EIT Law, "de facto management body" is defined as the organization body that effectively exercises management and control over such aspects as the business operations, personnel, accounting and properties of the enterprise.

On April 22, 2009, the SAT released the Notice Regarding the Determination of Chinese-Controlled Offshore Incorporated Enterprises as People's Republic of China Tax Resident Enterprises on the Basis of De Facto Management Bodies, or SAT Circular 82, that sets out the standards and procedures for determining whether the "de facto management body" of an enterprise registered outside of mainland China and controlled by mainland Chinese enterprises or mainland Chinese enterprise groups is located within mainland China. Further to SAT Circular 82, on July 27, 2011, the SAT issued the Administrative Measures for Enterprise Income Tax of Chinese-Controlled Offshore Incorporated Resident Enterprises (Trial), or SAT Bulletin 45, to provide more guidance on the implementation of SAT Circular 82; the bulletin became effective on September 1, 2011 and revised on April 17, 2015, June 28, 2016, and June 15, 2018. SAT Bulletin 45 clarified certain issues in the areas of resident status determination, post-determination administration and competent tax authorities' procedures.

Under Circular 82, a foreign enterprise controlled by a mainland Chinese enterprise or mainland Chinese enterprise group is considered a mainland Chinese resident enterprise if all of the following apply: (i) the senior management and core management departments in charge of daily operations are located mainly within mainland China; (ii) financial and human resources decisions are subject to determination or approval by persons or bodies in mainland China; (iii) major assets, accounting books, company seals and minutes and files of board and shareholders' meetings are located or kept within mainland China; and (iv) at least half of the enterprise's directors with voting rights or senior management reside within mainland

China. SAT Bulletin 45 specifies that when provided with a copy of Chinese tax resident determination certificate from a Chinese resident controlled offshore incorporated enterprise, the payer should not withhold 10% income tax when paying the Chinese-sourced dividends, interest, royalties, etc. to the mainland Chinese resident controlled offshore incorporated enterprise.

Although Circular 82 and SAT Bulletin 45 explicitly provide that the above standards apply to enterprises which are registered outside of mainland China and controlled by mainland Chinese enterprises or mainland Chinese enterprise groups, Circular 82 may reflect SAT's criteria for determining the tax residence of foreign enterprises in general. If mainland Chinese tax authorities determine that we were treated as a resident enterprise in mainland China for mainland Chinese enterprise income tax purposes, the 25% mainland Chinese enterprise income tax on our global taxable income could materially and adversely affect our ability to satisfy any cash requirements we may have.

***Laws and regulations in mainland China establish more complex procedures for some acquisitions of Chinese companies by foreign investors, which could make it more difficult for us to pursue growth through acquisitions in mainland China.***

A number of mainland Chinese laws and regulations, including the M&A Rules, the Anti-monopoly Law promulgated by the Standing Committee of the National People's Congress in August 2007, and the Rules of Ministry of Commerce on Implementation of Security Review System of Mergers and Acquisitions of Domestic Enterprises by Foreign Investors promulgated by MOFCOM in August 2011, or the Security Review Rules, have established procedures and requirements that are expected to make merger and acquisition activities in mainland China by foreign investors more time-consuming and complex. These include requirements in some instances that the approval from MOFCOM be obtained in circumstances where overseas companies established or controlled by enterprises or residents in mainland China acquire affiliated domestic companies. Mainland Chinese laws and regulations also require certain merger and acquisition transactions to be subject to merger control review or security review. We have grown and may continue to grow our business by acquiring complementary businesses. Complying with the requirements of the above-mentioned regulations and other relevant rules to complete such transactions could be time-consuming, and any required approval processes, including obtaining approval from MOFCOM or its local counterparts may delay or inhibit our ability to complete such transactions. It is unclear whether our business would be deemed to be in an industry that raises "national defense and security" or "national security" concerns. However, MOFCOM or other government agencies may publish explanations in the future determining that our business is in an industry subject to the security review, in which case our future acquisitions in mainland China, including those by way of entering into contractual control arrangements with target entities, may be closely scrutinized or prohibited. Our ability to expand our business or maintain or expand our market share through future acquisitions would as such be materially and adversely affected.

***The heightened scrutiny over acquisition transactions by tax authorities in mainland China may have a negative impact on our business operations, our acquisition or restructuring strategy or the value of your investment in us.***

Pursuant to the Notice of State Administration for Taxation on Strengthening Administration of Enterprise Income Tax for Share Transfers by Non-Resident Enterprises, or SAT Circular 698, issued by the SAT in December 2009 with retroactive effect from January 1, 2008, where a non-resident enterprise transfers the equity interests of a mainland Chinese resident enterprise indirectly by disposition of the equity interests of an overseas non-public holding company, or an Indirect Transfer, and such overseas holding company is located in a tax jurisdiction that (i) has an effective tax rate of less than 12.5% or (ii) does not impose income tax on foreign income of its residents, the non-resident enterprise, being the transferor, must report to the competent tax authority of the mainland Chinese resident enterprise this Indirect Transfer. Using a "substance over form" principle, the mainland Chinese tax authority may disregard the existence of the overseas holding company if it lacks a reasonable commercial purpose and was established for the purpose of reducing, avoiding or deferring mainland Chinese tax.

On March 28, 2011, the SAT released the SAT Public Notice (2011) No. 24, or SAT Public Notice 24, which became effective on April 1, 2011, to clarify several issues related to Circular 698. According to SAT

Public Notice 24, the term "effective tax" refers to the effective tax on the gain derived from disposition of the equity interests of an overseas holding company; and the term "does not impose income tax" refers to the cases where the gain derived from disposition of the equity interests of an overseas holding company is not subject to income tax in the jurisdiction where the overseas holding company is a resident.

On February 3, 2015, the SAT issued the Announcement of the SAT on Several Issues concerning the Enterprise Income Tax on Income from the Indirect Transfer of Assets by Non-Resident Enterprises, or SAT Circular 7, which abolished certain provisions in SAT Circular 698, as well as certain other rules providing clarification on SAT Circular 698. SAT Circular 7 provided comprehensive guidelines relating to, and also heightened the mainland Chinese tax authorities' scrutiny over, indirect transfers by a non-resident enterprise of mainland Chinese taxable assets. Under SAT Circular 7, the tax authorities in mainland China are entitled to reclassify the nature of an indirect transfer of mainland Chinese taxable assets, when a non-resident enterprise transfers mainland Chinese taxable assets indirectly by disposing of equity interests in an overseas holding company directly or indirectly holding such mainland Chinese taxable assets, by disregarding the existence of such overseas holding company and considering the transaction to be a direct transfer of mainland Chinese enterprise income taxes and without any other reasonable commercial purpose. However, SAT Circular 7 contains certain exemptions, including (i) where a non-resident enterprise derives income from the indirect transfer of mainland Chinese taxable assets by acquiring and selling shares of an overseas listed company which holds such mainland Chinese taxable assets on a public market; and (ii) where there is an indirect transfer of mainland Chinese taxable assets, but if the non-resident enterprise had directly held and disposed of such mainland Chinese taxable assets, the income from the transfer would have been exempted from enterprise income tax in mainland China under an applicable tax treaty or arrangement.

On October 17, 2017, the SAT issued the Circular on the Source of Deduction of Income Tax for Non-resident Enterprises, or SAT Circular 37, which became effective on December 1, 2017 and abolish SAT Circular 698 as well as certain provisions in SAT Circular 7. Pursuant to SAT Circular 37, where the party responsible to deduct such income tax did not or was unable to make such deduction, the non-resident enterprise receiving such income should declare and pay the taxes that should have been deducted to the relevant tax authority. The taxable gain is calculated as the income from such transfer net of the net book value of equity interest.

We have conducted and may conduct acquisitions involving changes in corporate structures, and historically our shares were transferred by certain then shareholders to our current shareholders. We cannot assure you that the mainland Chinese tax authorities will not, at their discretion, adjust any capital gains and impose tax return filing obligations on us or require us to provide assistance for the investigation of mainland Chinese tax authorities with respect thereto. Any mainland Chinese tax imposed on a transfer of our Ordinary Shares or any adjustment of such gains would cause us to incur additional costs and may have a negative impact on the value of your investment in us.

***Discontinuation of preferential tax treatments we currently enjoy or other unfavorable changes in tax law could result in additional compliance obligations and costs.***

Operating in the high-technology and software industry, a number of our mainland China operating entities enjoy various types of preferential tax treatment according to the prevailing mainland Chinese tax laws. Our mainland Chinese subsidiaries may, if they meet the relevant requirements, qualify for three main types of preferential treatment, which are high and new technology enterprises specially supported by mainland China, software enterprises and key software enterprises within the scope of the mainland Chinese national plan.

For a qualified high and new technology enterprise, the applicable enterprise income tax rate is 15%. The high and new technology enterprise qualification is re-assessed by the relevant authorities every three years. Moreover, a qualified software enterprise is entitled to a tax holiday consisting of a two-year tax exemption beginning with the first profit-making calendar year and a 50% tax reduction for the subsequent three years. The software enterprise qualification is subject to an annual assessment. For a qualified key software enterprise within the scope of the mainland Chinese national plan, the applicable enterprise income tax rate for a calendar year is 10%. The key software enterprise qualification is subject to assessment every two years. The discontinuation of any of the various types of preferential tax treatment we enjoy could materially and adversely affect our results of operations.

Under the EIT Law and its implementation rules, subject to any applicable tax treaty or similar arrangement between mainland China and your jurisdiction of residence that provides for a different income tax arrangement, mainland Chinese withholding tax at the rate of 10% (unless a treaty or similar arrangement otherwise provides) is normally applicable to dividends from mainland Chinese sources payable to investors that are resident enterprises outside of mainland Chinese, which do not have an establishment or place of business in mainland China, or which have such establishment or place of business if the relevant income is not effectively connected with the establishment or place of business. Any gain realized on the transfer of shares by such investors is subject to 10% (or a lower rate) mainland China income tax if such gain is regarded as income derived from sources within mainland China unless a treaty or similar arrangement otherwise provides. Under the Individual Income Tax Law of the People's Republic of China and its implementation rules, dividends from sources within mainland China paid to foreign individual investors who are not residents in mainland China are generally subject to a mainland Chinese withholding tax at a rate of 20% and gains from mainland Chinese sources realized by such investors on the transfer of shares are generally subject to 20% mainland Chinese income tax, in each case, subject to any reduction or exemption set forth in applicable tax treaties and mainland Chinese laws.

Although a majority of our business operations are in mainland China, it is unclear whether dividends we pay with respect to our Ordinary Shares, or the gain realized from the transfer of our Ordinary Shares, would be treated as income derived from sources within mainland China and as a result be subject to mainland Chinese income tax if we are considered a mainland Chinese resident enterprise. If mainland Chinese income tax is imposed on gains realized through the transfer of our Ordinary Shares or on dividends paid to our non-resident investors, the value of your investment in our Ordinary Shares may be materially and adversely affected. Furthermore, our Ordinary Shareholders whose jurisdictions of residence have tax treaties or arrangements with mainland China may not qualify for benefits under such tax treaties or arrangements.

***Mainland Chinese regulations of loans and direct investment by offshore holding companies to mainland Chinese entities may delay or prevent us from using the proceeds of this offering to make loans or additional capital contributions to our mainland Chinese subsidiaries, which could materially and adversely affect our liquidity and our ability to fund and expand our business.***

We may transfer funds to our mainland Chinese subsidiaries or finance our mainland Chinese subsidiaries by means of shareholders' loans or capital contributions after completion of this offering. Any loans to our mainland Chinese subsidiaries, which are foreign-invested enterprises, or FIEs, cannot exceed statutory limits based on the difference between the registered capital and the investment amount of such subsidiaries, and shall be registered with SAFE or its local counterparts.

Furthermore, any capital contributions we make to our mainland Chinese subsidiaries shall be (i) registered with the competent branch of State Administration for Market Regulation and reported to MOFCOM via the online enterprise registration system, and (ii) registered with the local banks authorized by SAFE. We may not be able to obtain these government registrations or approvals on a timely basis, if at all. If we fail to receive such registrations or approvals, our ability to provide loans or capital contributions to our mainland Chinese subsidiaries in a timely manner may be negatively affected, which could materially and adversely affect our liquidity and our ability to fund and expand our business.

On March 30, 2015, SAFE promulgated the Circular on Reforming the Administration Measures on Conversion of Foreign Exchange Registered Capital of Foreign-invested Enterprises, or Circular 19, which will replace Circular 142 from June 1, 2015. Circular 19, however, allows foreign invested enterprises whose main business is investment in mainland China to use their registered capital settled in RMB converted from foreign currencies to make equity investments, but the registered capital of such a foreign invested company settled in RMB converted from foreign currencies remains not allowed to be used for investment in the security markets, offering entrustment loans or purchases of any investment properties, unless otherwise regulated by other laws and regulations. On October 23, 2019, SAFE promulgated the Notice by the State Administration of Foreign Exchange of Further Facilitating Cross-border Trade and Investment, or Circular 28 which allows all foreign invested enterprises in mainland China to use their registered capital settled in RMB converted from foreign currencies to make equity investments. Circular 19 and Circular 28 may limit our ability to transfer the net proceeds from this offering to our mainland Chinese subsidiaries and convert the net proceeds into RMB.

***We may be subject to penalties, including restriction on our ability to inject capital into our mainland Chinese subsidiaries and our mainland Chinese subsidiaries' ability to distribute profits to us, if our resident shareholders or beneficial owners in mainland China fail to comply with relevant mainland Chinese foreign exchange regulations.***

SAFE issued the Notice on Relevant Issues Relating to Domestic Residents' Investment and Financing and Round-Trip Investment through Special Purpose Vehicles, or Circular 37, effective on July 4, 2014, which replaced the previous Notice on Relevant Issues Concerning Foreign Exchange Administration for the People's Republic of China Residents Engaging in Financing and Round-trip Investments via Overseas Special Purpose Vehicles, or Circular 75. Circular 37 requires mainland Chinese residents, including mainland Chinese individuals and institutions, to register with SAFE or its local branches in connection with their direct establishment or indirect control of an offshore special purpose vehicle, for the purpose of overseas investment and financing, with such mainland Chinese residents' legally owned assets or equity interests in domestic enterprises or offshore assets or interests. In addition, such residents in mainland China must update their foreign exchange registrations with SAFE or its local branches when the offshore special purpose vehicle undergoes material events relating to any change of basic information (including change of such mainland Chinese individual shareholder, name and operation term), increases or decreases in investment amount, share transfers or exchanges, or mergers or divisions.

If any shareholder holding interest in an offshore special purpose vehicle, who is a mainland Chinese resident as determined by Circular 37, fails to fulfill the required foreign exchange registration with the local SAFE branches, the mainland Chinese subsidiaries of that offshore special purpose vehicle may be prohibited from distributing their profits and dividends to their offshore parent company or from carrying out other subsequent cross-border foreign exchange activities, and the offshore special purpose vehicle may be restricted in its ability to contribute additional capital to its mainland Chinese subsidiaries. Moreover, failure to comply with the SAFE registration described above could result in liability under mainland Chinese laws for evasion of applicable foreign exchange restrictions.

We may not be fully informed of the identities of all our shareholders or beneficial owners who are mainland Chinese residents, and therefore, we may not be able to identify all our shareholders or beneficial owners who are mainland Chinese residents to ensure their compliance with Circular 37 or other related rules. In addition, we cannot provide any assurance that all of our shareholders and beneficial owners who are residents in mainland China will comply with our request to make, obtain or update any applicable registrations or comply with other requirements required by the Circular 37 or other related rules in a timely manner. Even if our shareholders and beneficial owners who are residents in mainland China comply with such request, we cannot provide any assurance that they will successfully obtain or update any registration required by the Circular 37 or other related rules in a timely manner due to many factors, including those beyond our and their control. If any of our shareholders who is a resident in mainland China as determined by Circular 37 fails to fulfill the required foreign exchange registration with the local SAFE branches, our mainland Chinese subsidiaries may be prohibited from distributing their profits and dividends to us or from carrying out other subsequent cross-border foreign exchange activities, and we may be restricted in our ability to contribute additional capital to our subsidiaries in mainland China, which may adversely affect our business.

***We rely on dividends and other distributions on equity paid by our subsidiaries in mainland China to fund any cash and financing requirements we may have. Any limitation on the ability of our mainland Chinese subsidiaries to make payments to us could have a material adverse effect on our ability to conduct our business or financial condition.***

We are a holding company, and we rely on dividends and other distributions on equity that may be paid by our subsidiaries in mainland China and remittances from our VIEs, for our cash and financing requirements, including the funds necessary to pay dividends and other cash distributions to the holders of our ordinary shares and service any debt we may incur. If our mainland Chinese subsidiaries or our VIEs incur debt on their own behalf in the future, the instruments governing the debt may restrict their ability to pay dividends or make other distributions to us.

Under mainland Chinese laws and regulations, wholly foreign-owned enterprises in mainland China, may pay dividends only out of their retained earnings as determined in accordance with mainland Chinese accounting standards and regulations. In addition, a wholly foreign-owned enterprise is required to set aside at least 10% of its after-tax profits each year, after making up previous years' accumulated losses, if any, to fund certain statutory reserve funds, until the aggregate amount of such a fund reaches 50% of its registered capital. At the discretion of the board of director of the wholly foreign-owned enterprise, it may allocate a portion of its after-tax profits based on mainland Chinese accounting standards to staff welfare and bonus funds. These reserve funds and staff welfare and bonus funds are not distributable as cash dividends. Any limitation on the ability of our VIEs to make remittance to our wholly-owned subsidiaries in mainland China to pay dividends or make other distributions to us could materially and adversely limit our ability to grow, make investments or acquisitions that could be beneficial to our business, pay dividends, or otherwise fund and conduct our business.

***Restrictions on the remittance of RMB into and out of mainland China and governmental control of currency conversion may limit our ability to pay dividends and other obligations, and affect the value of your investment.***

The mainland Chinese government imposes controls on the convertibility of RMB into foreign currencies and the remittance of currency out of mainland China. We receive a considerable portion of our revenue in RMB. Under our current corporate structure, our income is primarily derived from dividend payments from our subsidiaries in mainland China. We may convert a portion of our revenue into other currencies to meet our foreign currency obligations, such as payments to certain suppliers and payments of dividends declared in respect of our Ordinary Shares, if any. Shortages in the availability of foreign currency may restrict the ability of our subsidiaries in mainland China to remit sufficient foreign currency to pay dividends or other payments to us, or otherwise satisfy their foreign currency denominated obligations.

Under existing mainland Chinese foreign exchange regulations, payments of current account items, including profit distributions, interest payments and trade and service-related foreign exchange transactions, can be made in foreign currencies without prior SAFE approval by complying with certain procedural requirements. However, approval from or registration with competent government authorities is required where RMB is to be converted into foreign currency and remitted out of mainland China to pay capital expenses such as the repayment of loans denominated in foreign currencies. The mainland Chinese government may at its discretion restrict access to foreign currencies for current account transactions in the future. If the foreign exchange control system prevents us from obtaining sufficient foreign currencies to satisfy our foreign currency demands, we may not be able to pay dividends in foreign currencies to our Shareholders. Further, there is no assurance that new regulations will not be promulgated in the future that would have the effect of further restricting the remittance of RMB into or out of mainland China.

***Fluctuations in exchange rates could result in foreign currency exchange losses.***

The value of RMB against the Hong Kong dollar, the U.S. dollar and other foreign currencies fluctuates, is subject to changes resulting from the mainland Chinese government's policies and depends to a large extent on domestic and international economic and political developments as well as supply and demand in the local market. Any significant revaluation of Renminbi may materially and adversely affect our revenues, earnings and financial position. To the extent that we need to convert foreign currencies into RMB for capital expenditures and working capital and other business purposes, appreciation of the RMB against foreign currencies would have an adverse effect on the RMB amount we would receive from the conversion. Conversely, a significant depreciation of the Renminbi against foreign currencies may significantly reduce the foreign currencies' equivalent of our earnings, and if we decide to convert RMB into foreign currencies for strategic acquisitions or investments or other business purposes, appreciation of the foreign currencies against the RMB would have a negative effect on the amount available to us in foreign currencies. With the development of the foreign exchange market and progress toward interest rate liberalization and Renminbi internationalization, the mainland Chinese government may in the future announce further changes to the exchange rate system, and we cannot assure you that the Renminbi will not appreciate or depreciate significantly in value against the Hong Kong dollar, the U.S. dollar or other foreign currencies in the future. In addition, our currency exchange losses may be magnified by mainland China's exchange control regulations that restrict our ability to convert Renminbi into foreign currency. As a result, fluctuations in exchange rates may have a material adverse effect on our financial position.

***It may be difficult to effect service of process upon us or our directors or officers named in this document who reside in mainland China or to enforce non-mainland China court judgments against them in mainland China.***

We conduct a majority of our operations in mainland China and most of our directors and officers named in this document reside in mainland China. As a result, it may be difficult to effect service of process outside mainland China upon most of our directors and officers, including with respect to matters arising under applicable securities laws. Mainland China does not have treaties providing for the reciprocal recognition and enforcement of judgments of courts with the United States, the United Kingdom and many other countries. Consequently, it may be difficult for you to enforce against us or our directors or officers in mainland China any judgments obtained from courts outside of mainland China. On July 14, 2006, Hong Kong and mainland China signed the Arrangement on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters by the Courts of the Mainland and of the Hong Kong Special Administrative Region Pursuant to Choice of Court Agreements between Parties Concerned, or the 2006 Arrangement**,** as revised on February 29, 2008, pursuant to which a party with a final judgment rendered by a Hong Kong court requiring payment of money in a civil and commercial case pursuant to a choice of court agreement in writing may apply for recognition and enforcement of the judgment in mainland China. Similarly, a party with a final judgment rendered by a mainland Chinese court requiring payment of money in a civil and commercial case pursuant to a choice of court agreement in writing may apply for recognition and enforcement of the judgment in Hong Kong. A choice of court agreement in writing is defined as any agreement in writing entered into between parties after the effective date of the 2006 Arrangement in which a Hong Kong court or a mainland Chinese court is expressly designated as the court having sole jurisdiction for the dispute. Therefore, it is not possible to enforce a judgment rendered by a Hong Kong court in mainland China if the parties in dispute have not agreed to enter into a choice of court agreement in writing.

On January 18, 2019, Hong Kong and mainland China signed the Arrangement on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters by the Courts of the Mainland and of the Hong Kong Special Administrative Region, or the 2019 Arrangement. The 2019 Arrangement seeks to establish a mechanism for recognition and enforcement of judgments in a wider range of civil and commercial matters, based on criteria other than a written bilateral choice of court agreement. The 2019 Arrangement will only apply to judgments made after its commencement date, which is not yet known. The 2006 Arrangement shall be terminated when the 2019 Arrangement comes into effect. However, the 2006 Arrangement will continue to apply to a choice of court agreement in writing signed before the 2019 Arrangement comes into effect. Therefore, there are still uncertainties about the outcomes and effectiveness of enforcement or recognition of judgments under the 2019 Arrangement.

## Risks Relating to Our Corporate Structure

***If the mainland Chinese government finds that the agreements that establish the structure for operating our business do not comply with mainland Chinese laws and regulations, or if these regulations or their interpretations change in the future, we could be subject to severe penalties or be forced to relinquish our interests in those operations.***

Current mainland Chinese laws and regulations impose certain restrictions or prohibitions on foreign ownership of companies that engage in value-added telecommunications services and other related businesses, including the provision of internet information and cultural services. In particular, under the Guidance Catalog of Industries for Foreign Investment, the operation of certain of our internet services falls into the value-added telecommunications services business and is considered "restricted," and the operation of online and mobile games, provision of audio-visual program services and online reading services to the public fall into the internet cultural services business and are considered "prohibited." We are an exempted company incorporated under the laws of the Cayman Islands. To comply with mainland Chinese laws and regulations, we conduct our internet-related business in mainland China through a number of VIEs incorporated in mainland China. The VIEs are owned by mainland Chinese citizens who are our founder, co-founders or shareholders, with whom we have contractual arrangements. The contractual arrangements give us effective control over each of the VIEs and enable us to obtain substantially all of the economic benefits arising from the VIEs as well as consolidate the financial results of the VIEs in our results of operations. The mainland Chinese government may not agree that these arrangements comply with mainland Chinese licensing, registration or other regulatory requirements, with existing policies or with requirements or policies that may be adopted in the future. These VIEs and their subsidiaries hold the licenses, approvals and key assets that are essential for the operations of our businesses in China.

There are substantial uncertainties regarding the interpretation and application of current or future mainland Chinese laws and regulations. The relevant regulatory authorities in mainland China have broad discretion in determining whether a particular contractual structure violates mainland Chinese laws and regulations. If we are found in violation of any mainland Chinese laws or regulations or if the contractual arrangements among our material wholly-foreign owned enterprises, our material VIEs and subsidiaries and their respective equity holders are determined as illegal or invalid by any mainland Chinese court, arbitral tribunal or regulatory authorities, the relevant governmental authorities would have broad discretion in dealing with such violation, including, without limitation:

- revoke the agreements constituting the contractual arrangements;
- revoke our business and operating licenses;
- require us to discontinue or restrict operations;
- restrict our right to collect revenue;
- shut down all or part of our websites or services;
- levy fines on us and/or confiscate the proceeds that they deem to have been obtained through non-compliant operations;
- require us to restructure the operations in such a way as to compel us to establish a new enterprise, re-apply for the necessary licenses or relocate our businesses, staff and assets;
- impose additional conditions or requirements with which we may not be able to comply; or
- take other regulatory or enforcement actions that could be harmful to our business.

Furthermore, any of the assets under the name of any record holder of equity interest in our material VIEs, including such equity interest, may be put under court custody in connection with litigation, arbitration or other judicial or dispute resolution proceedings against that record holder. We cannot be certain that the equity interest will be disposed of in accordance with the contractual arrangements. In addition, new mainland Chinese laws, rules and regulations may be introduced to impose additional requirements that may impose additional challenges to our corporate structure and contractual arrangements. The occurrence of any of these events or the imposition of any of these penalties may result in a material and adverse effect on our ability to conduct internet-related businesses. In addition, if the imposition of any of these penalties causes us unable to direct the activities of such VIEs and its subsidiary or lose the right to receive their economic benefits, we would no longer be able to consolidate such VIEs into our financial statements, thus adversely affect our results of operation.

***Uncertainties exist with respect to the interpretation and implementation of the newly enacted Foreign Investment Law and how it may impact the viability of our current corporate structure, corporate governance and business operations.***

The National People's Congress approved the Foreign Investment Law on March 15, 2019 and the State Council approved the Regulation on Implementing the Foreign Investment Law (the "**Implementation Regulations**") on December 12, 2019, effective from January 1, 2020, to replace the trio of existing laws regulating foreign investment in mainland China, namely, the Sino-foreign Equity Joint Venture Enterprise Law, the Sino-foreign Cooperative Joint Venture Enterprise Law and the Wholly Foreign-invested Enterprise Law, together with their implementation rules and ancillary regulations. The Foreign Investment Law embodies an expected regulatory trend to rationalize its foreign investment regulatory regime in line with prevailing international practice and the legislative efforts to unify the corporate legal requirements for both foreign and domestic investments. However, since it is relatively new, uncertainties still exist in relation to its interpretation and implementation. For instance, under the Foreign Investment Law, "foreign investment" refers to the investment activities directly or indirectly conducted by foreign individuals, enterprises or other entities in mainland China. Though it does not explicitly classify contractual arrangements as a form of foreign investment, there is no assurance that foreign investment via contractual arrangement would not be interpreted as a type of indirect foreign investment activities under the definition in the future. In addition, the definition contains a catch-all provision which includes investments made by foreign investors through means stipulated in laws or administrative regulations or other methods prescribed by the State Council. Therefore, it still leaves leeway for future laws, administrative regulations or provisions promulgated by the State Council to provide for contractual arrangements as a form of foreign investment. In any of these cases, it will be uncertain whether our contractual arrangements will be deemed to be in violation of the market access requirements for foreign investment under the applicable laws and regulations. Furthermore, if future laws, administrative regulations or provisions prescribed by the State Council mandate further actions to be taken by companies with respect to existing contractual arrangements, we may face substantial uncertainties as to whether we can complete such actions in a timely manner, or at all. Failure to take timely and appropriate measures to cope with any of these or similar regulatory compliance challenges could materially and adversely affect our current corporate structure, corporate governance and business operations.

***Our contractual arrangements with respect to our VIE structure may not be as effective in providing operational control as direct ownership and our viable interest entities shareholders may fail to perform their obligations under our contractual arrangements.***

We operate our certain restricted businesses in mainland China through certain variable interest entities and their subsidiaries, in which we have no ownership interest and rely on a series of contractual arrangements to control and operate these businesses. Our revenue and cash flow from our businesses are attributed to our VIEs. The contractual arrangements may not be as effective as direct ownership in providing us with control over our VIEs. Direct ownership would allow us, for example, to directly or indirectly exercise our rights as a shareholder to effect changes in the boards of directors of our VIEs, which, in turn, could effect changes, subject to any applicable fiduciary obligations at the management level. However, under the contractual arrangements, as a legal matter, if our VIEs or their respective equity holders fail to perform their respective obligations under the contractual arrangements, we may have to incur substantial costs and expend significant resources to enforce those arrangements and resort to litigation or arbitration and rely on legal remedies under mainland Chinese laws. These remedies may include seeking specific performance or injunctive relief and claiming damages, any of which may not be effective. In the event we are unable to enforce these contractual arrangements or we experience significant delays or other obstacles in the process of enforcing these contractual arrangements, we may not be able to exert effective control over our affiliated entities and may lose control over the assets owned by our VIEs. As a result, we may be unable to consolidate our VIEs in our consolidated financial statements, which could materially and adversely affect our results of operations and financial condition.

***We may lose the ability to use, or otherwise benefit from, the licenses, approvals and assets held by our VIEs and their subsidiaries, which could render us unable to conduct some or all of our business operations and constrain our growth.***

Although the significant majority of our revenues are generated, and the significant majority of our operational assets are held, by our wholly-foreign owned enterprises, which are our subsidiaries, our VIEs and their subsidiaries hold licenses and approvals and assets that are necessary for the related business operations, as well as equity interests in a series of our portfolio companies, to which foreign investments are typically restricted or prohibited under applicable mainland Chinese law. The contractual arrangements with respect to our VIE structure contain terms that specifically obligate VIEs equity holders to ensure the valid existence of the VIEs and restrict the disposal of material assets or any equity interest of the VIEs. However, in the event the VIEs equity holders breach the terms of these contractual arrangements and voluntarily liquidate our VIEs, or any of our VIEs declares bankruptcy and all or part of its assets become subject to liens or rights of third-party creditors, or are otherwise disposed of without our consent, we may be unable to conduct some or all of the relevant business operations or otherwise benefit from the assets held by the VIEs, which could have a material adverse effect on our relevant business, financial condition and results of operations. Furthermore, if any of our VIEs undergoes a voluntary or involuntary liquidation proceeding, its equity holders or unrelated third-party creditors may claim rights to some or all of the assets of such VIEs, thereby hindering our ability to operate our business as well as constrain our growth.

***The contractual arrangements with our VIEs may be subject to scrutiny by the tax authorities in mainland China. Any adjustment of related party transaction pricing could lead to additional taxes, and therefore substantially reduce our consolidated profit and the value of your investment.***

The tax regime in mainland China is rapidly evolving and there is significant uncertainty for taxpayers in mainland China as mainland Chinese tax laws may be interpreted in significantly different ways. The mainland Chinese tax authorities may assert that we or our subsidiaries or VIEs or their equity holders owe and/or are required to pay additional taxes on previous or future revenue or income. In particular, under applicable mainland Chinese laws, rules and regulations, arrangements and transactions among related parties, such as the contractual arrangements with our VIEs, may be subject to audit or challenge by the mainland Chinese tax authorities. If the mainland Chinese tax authorities determine that any contractual arrangements were not entered into on an arm's length basis and therefore constitute a favorable transfer pricing, the mainland Chinese tax liabilities of the relevant subsidiaries and/or VIEs and/ or equity holders of VIEs could be increased, which could increase our overall tax liabilities. In addition, the mainland Chinese tax authorities may impose late payment interest. Our profit may be materially reduced if our tax liabilities increase.

***The equity holders, directors and executive officers of the VIEs, as well as our employees who execute other strategic initiatives may have potential conflicts of interest with our Company.***

The laws of mainland China provide that a director and an executive officer owes a fiduciary duty to the company he or she directs or manages. The directors and executive officers of the VIEs, including Lei Jun, our executive director, Founder, Chairman and Chief Executive Officer, must act in good faith and in the best interests of the variable interest entities and must not use their respective positions for personal gain. On the other hand, as a director of our Company, Lei Jun has a duty of care and loyalty to our Company and to our shareholders as a whole under Cayman Islands law. We control our VIEs through contractual arrangements and the business and operations of our VIEs are closely integrated with the business and operations of our subsidiaries. Nonetheless, conflicts of interests for these individuals may arise due to dual roles both as directors and executive officers of the VIEs and as directors or employees of our Company, and may also arise due to dual roles both as VIEs equity holders and as directors or employees of our Company.

We cannot assure you that these individuals will always act in the best interests of our Company should any conflicts of interest arise, or that any conflicts of interest will always be resolved in our favor. We also cannot assure you that these individuals will ensure that the VIEs will not breach the existing contractual arrangements. If we cannot resolve any such conflicts of interest or any related disputes, we would have to rely on legal proceedings to resolve these disputes and/or take enforcement action under the contractual arrangements. There is substantial uncertainty as to the outcome of any such legal proceedings. See the section headed "– *We may lose the ability to use, or otherwise benefit from, the licenses, approvals and assets held by our VIEs, which could, render us unable to conduct some or all of our business operations and constrain our growth*" above.

***We conduct our business operation in mainland China through our VIEs by way of the contractual arrangements, but certain of the terms of the contractual arrangements may not be enforceable under mainland Chinese laws.***

All the agreements which constitute the contractual arrangements are governed by mainland Chinese laws and provide for the resolution of disputes through arbitration in mainland China. Accordingly, these agreements would be interpreted in accordance with mainland Chinese laws and disputes would be resolved in accordance with mainland Chinese legal procedures. The legal environment in mainland China is not as developed as in other jurisdictions and uncertainties in the mainland Chinese legal system could limit our ability to enforce the contractual arrangements. In the event that we are unable to enforce the contractual arrangements, or if we suffer significant time delays or other obstacles in the process of enforcing them, it would be very difficult to exert effective control over our VIEs and their subsidiaries, and our ability to conduct our business and our financial condition and results of operations may be materially and adversely affected.

The contractual arrangements contain provisions to the effect that the arbitral body may award remedies over the shares and/or assets of our VIEs and their subsidiaries, injunctive relief and/or winding up of our VIEs and their subsidiaries. These agreements also contain provisions to the effect that courts of competent jurisdictions are empowered to grant interim remedies in support of the arbitration pending the formation of an arbitral tribunal. However, under mainland Chinese laws, these terms may not be enforceable. Under mainland Chinese laws, an arbitral body does not have the power to grant injunctive relief or to issue a provisional or final liquidation order for the purpose of protecting assets of or equity interests in our VIEs and their subsidiaries in case of disputes. In addition, interim remedies or enforcement order granted by overseas courts such as Hong Kong and the Cayman Islands may not be recognizable or enforceable in mainland China. Mainland Chinese laws do allow the arbitral body to grant an award of transfer of assets of or equity interests in our VIEs and their subsidiaries in favor of an aggrieved party. Therefore, in the event of breach of any agreements constituting the contractual arrangements by our VIEs and their subsidiaries and/or their respective equity holders, and if we are unable to enforce the contractual arrangements, we may not be able to exert effective control over our VIEs and their subsidiaries, which could negatively affect our ability to conduct our business.

**Risks Relating to the Bonds, the Guarantee and the Class B Shares**

***The Bonds will be unsecured obligations.***

The Bonds will constitute direct, unconditional, unsubordinated and (subject to Condition 4(a) of the Conditions) unsecured obligations of the Issuer ranking *pari passu* and without any preference or priority among themselves. The payment obligations of the Issuer under the Bonds, save for such exceptions as may be provided by mandatory provisions of applicable law and subject to the negative pledge contained in Condition 4(a) of the Conditions, will rank at least equally with all of its other present and future unsecured and unsubordinated obligations. The Guarantee will constitute direct, unconditional, unsubordinated and (subject to Condition 4(a) of the Conditions) unsecured obligations of the Guarantor and shall at least at all times rank at least equally with all of its other present and future unsecured and unsubordinated obligations as contained in the Trust Deed. Therefore, the Bonds and the Guarantee will be unsecured obligations of the Issuer and the Guarantor, respectively. The payment obligations under the Bonds and the Guarantee may be adversely affected if:

- the Group enters into bankruptcy, liquidation, rehabilitation or other winding-up proceedings;
- there is a default in payment under the Group's future secured indebtedness or other unsecured indebtedness; or
- there is an acceleration of any of the Group's indebtedness.

If any of the above events occurs, the Group's assets may not be sufficient to pay amounts due on the Bonds. Although we do not expect any of these events to occur with respect to the Issuer, since it is not permitted under the terms of the Conditions to carry on any business activities other than in connection with the issuance of the Bonds and advance of the proceeds therefrom to us or our subsidiaries, if any of these events occur, the Issuer's and our assets and any amounts received from the sale of such assets may not be sufficient to pay amounts due on the Bonds.

***The Trustee may request the Bondholders to provide an indemnity and/or security and/or prefunding to its satisfaction.***

In certain circumstances (including, without limitation, the giving of notice to the Issuer and the Guarantor pursuant to Condition 10 of the Conditions and the taking of enforcement steps pursuant to Condition 15 of the Conditions), the Trustee may request Bondholders to provide an indemnity and/or security and/or prefunding to its satisfaction before it takes actions on behalf of Bondholders. The Trustee shall not be obliged to take any such actions if it is not first indemnified and/or secured and/or prefunded to its satisfaction. Negotiating and agreeing to an indemnity and/or security and/or prefunding could be a lengthy process and may affect when such actions can be taken. The Trustee may not be able to take actions, notwithstanding the provision of an indemnity or security or prefunding to it, in breach of the terms of the Trust Deed and/or the Conditions and in such circumstances, or where there is uncertainty or dispute as to the applicable law or regulations, to the extent permitted by the agreements and the applicable law and regulations, it would be for the Bondholders to take such actions directly.

***Bondholders will have no rights as holders of the Class B Shares prior to conversion of the Bonds.***

Unless and until the Bondholders acquire the Class B Shares upon conversion of the Bonds, Bondholders will have no rights with respect to the Class B Shares, including any voting rights or rights to receive any regular dividends or other distributions with respect to the Class B Shares. Upon conversion of the Bonds, these holders would be entitled to exercise the rights of holders of the Class B Shares only as to actions for which the applicable record date occurs after the date of conversion.

***Securities law restrictions on the resale and conversion of the Bonds may limit Bondholders' ability to sell the Bonds in the United States.***

The Bonds and the Class B Shares into which the Bonds are convertible have not been and will not be registered under the Securities Act, any state securities laws or the securities laws of any other jurisdiction. Unless and until they are registered, the Bonds and the Class B Shares issuable upon conversion may not be offered, sold or resold except pursuant to an exemption from registration under the Securities Act and applicable state laws or in a transaction not subject to such laws. The Bonds are being offered and sold outside the U.S. in reliance on Regulation S under the Securities Act. Hence, future resales of the Bonds and the Class B Shares into which the Bonds are convertible may only be made pursuant to an exemption from registration under the Securities Act and applicable state laws or in a transaction not subject to such laws.

***The Bondholders may be subject to tax on their income or gain from the Bonds.***

Prospective purchasers of the Bonds are advised to consult their own tax advisers concerning the overall tax consequences of the acquisition, ownership or disposition (including upon conversion of the Bonds) of the

Bonds or the Class B Shares. See "*Taxation*" for certain Cayman Islands, PRC and Hong Kong tax consequences.

***Gains on the transfer of the Bonds may be subject to income tax under PRC tax laws.***

Under the Enterprise Income Tax Law of the PRC that came into effect on January 1, 2008 and amended on February 24, 2017 (the "**EIT Law**") and its implementation rules, gains on the transfer of the Bonds may be subject to income tax under PRC tax laws.

In accordance with the EIT Law and its implementation regulations, a non-resident enterprise is generally subject to enterprise income tax at a rate of 10% with respect to PRC-sourced income if it (i) does not have an establishment or place of business in the PRC or (ii) has an establishment or place of business in the PRC but its PRC-sourced income is not connected with such establishment or place of business in the PRC. The aforesaid income tax payable by a non-resident enterprise is subject to withholding at source. The income tax must be withheld by the withholding agent at the time of payment of the gains. This tax could be exempted or reduced in accordance with the relevant tax treaty or agreement for avoiding double taxation. As at the date of this Offering Circular, no specific legislation or implementation rule has expressly provided whether it is required to and how to collect the tax from non-PRC resident enterprises on gains derived by them from the sale or transfer of the Bonds. It is possible that taxation authorities may formulate and promulgate specific implementation rules or relevant regulations for the collection of enterprise income tax on such gains in the future.

In addition, according to the Individual Income Tax Law of the PRC as amended on June 30, 2011 and August 31, 2018 (the "**IIT Law**") and the implementation regulations, non-resident individuals are generally subject to individual income tax at a rate of 20% with respect to PRC-sourced income from interest, dividends and transfer of property unless such tax is reduced or exempted under relevant double taxation treaties. Under the IIT Law, a "non-resident individual" means any non-resident PRC individual who has no domicile and does not reside in the PRC or who has no domicile but has resided in mainland China for less than one year. As at the date of this Offering Circular, no specific legislation or implementation rules have expressly provided whether it is required to and how to collect the tax from non-PRC resident individuals on the gains derived by them from the sale or transfer of the Bonds. It is possible that taxation authorities may formulate and promulgate specific implementation rules or relevant regulations for the collection of individual income tax on such gains in the future.

If a Bondholder, being a non-resident enterprise or non-resident individual, is required to pay any PRC income tax on gains on the transfer of the Bonds, the value of the relevant Bondholder's investment in the Bonds may be materially and adversely affected. See "*Taxation – PRC*". Any payment of interest on the Bonds would be subject to withholding at a rate of 10% for non-PRC resident enterprises and at a rate of 20% for non-PRC resident individuals.

***The market value of the Bonds may fluctuate.***

Trading prices of the Bonds are influenced by numerous factors, including the results of operations and/or financial condition and business strategy (in particular further issuance of debt or corporate events such as share sales, reorganizations, takeovers or share buybacks) of the Group and/or the subsidiaries and/or associated companies of the Group, political, economic, financial, regulatory and any other factors that can affect the capital markets, the industry, the Group and/or the subsidiaries and/or associated companies of the Group generally. Adverse economic developments in the PRC could have a material and adverse effect on the results of operations and/or the financial condition of the Group and/or the subsidiaries and/or associated companies of the Group.

In addition, the market price of the Bonds is expected to be affected by fluctuations in the market price of the Class B Shares. There can be no certainty as to the effect, if any, that future issues or sales of Class B Shares, or the availability of such Class B Shares for future issue or sale, would have on the market price of the Class B Shares prevailing from time to time and therefore on the market price of the Bonds. Disposals of Class B Shares by shareholders or a perception in the market that such disposals could occur, may adversely affect the prevailing market price of the Class B Shares and the Bonds.

***The return on the Bonds may decrease due to inflation.***

Bondholders may suffer erosion on the return of their investments due to inflation. Bondholders would have an anticipated rate of return based on expected inflation rates on the purchase of the Bonds. An unexpected increase in inflation could reduce the actual returns.

***An active trading market for the Bonds may not develop.***

The Bonds will be a new issue of securities for which there is currently no trading market. Application will be made to the Hong Kong Stock Exchange for the listing, and permission to deal in, the Bonds by way of debt issues to Professional Investors only. However, no assurance can be given that an active trading market for the Bonds would develop or as to the liquidity or sustainability of any such market, the ability of Bondholders to sell their Bonds or the price at which Bondholders would be able to sell their Bonds. If an active market for the Bonds fails to develop or be sustained, the trading price of the Bonds could fall.

If an active trading market were to develop, the Bonds could trade at prices that may be lower than their initial offering price. Whether or not the Bonds would trade at lower prices depends on many factors, including:

- prevailing interest rates and the markets for similar securities;
- the price of the Class B Shares;
- the market prices of the Bonds;
- the publication of earnings estimates or other research reports and speculation in the press or the investment community;
- changes in the Group's industry and competition; and general market and economic conditions; or
- the Group's financial condition and historical financial performance and future prospects.

***The Bonds may not be a suitable investment for all investors.***

Each potential investor in the Bonds must determine the suitability of that investment in light of its own circumstances. In particular, each potential investor should:

- have sufficient knowledge and experience to make a meaningful evaluation of the Bonds, the merits and risks of investing in the Bonds and the information contained in this Offering Circular;
- have access to, and knowledge of, appropriate analytical tools to evaluate, in the context of its particular financial situation, an investment in the Bonds and the impact such investment will have on its overall investment portfolio;
- have sufficient financial resources and liquidity to bear all of the risks of an investment in the relevant Bonds, including where principal or default interest is payable in one or more currencies, or where the currency for principal or default interest payments is different from the potential investor's currency;
- understand thoroughly the terms of the Bonds and be familiar with the behavior of any relevant indices and financial markets; and
- be able to evaluate (either alone or with the help of a financial adviser) possible scenarios for economic, interest rate and other factors that may affect its investment and its ability to bear the applicable risks.

The Bonds will be complex financial instruments. Sophisticated institutional investors generally do not purchase complex financial instruments as stand-alone investments. They purchase complex financial instruments as a way to reduce risk or enhance yield with an understood, measured, appropriate addition of risk to their overall portfolios. A potential investor should not invest in the Bonds unless he/she has the expertise (either alone or with a financial adviser) to evaluate how the Bonds will perform under changing conditions, the resulting effects on the value of the Bonds and the impact this investment will have on the potential investor's overall investment portfolio.

***The Bonds contain provisions regarding modification and waivers, which could affect the rights of Bondholders.***

The Conditions and the Trust Deed will contain provisions for calling meetings of Bondholders to consider matters affecting their interests generally. These provisions will permit defined majorities to bind all Bondholders including Bondholders who did not attend and vote at the relevant meeting and Bondholders who voted in a manner contrary to the majority. There is a risk that the decision of the majority of holders of the Bonds may be adverse to the interests of individual holders of the Bonds.

The Conditions will also provide that the Trustee may, without the consent of the holders of the Bonds, agree (i) to any modification (other than in respect of certain reserved matters) to, or the waiver or authorization of any breach or proposed breach of, the Bonds, the Agency Agreement and/or the Trust Deed which in the opinion of the Trustee would not be materially prejudicial to the interests of the holders of the Bonds and (ii) to any modification of the Bonds, the Agency Agreement or the Trust Deed which is in the Trustee's opinion of a formal, minor or technical nature or is made to correct a manifest error or to comply with mandatory provisions of law.

In addition, the Trustee may (but shall not be obliged to), without the consent of the Bondholders, determine any Event of Default or a Potential Event of Default (both terms as defined in the Trust Deed) should not be treated as such, provided that in the opinion of the Trustee, the interests of the Bondholders will not be materially prejudiced thereby.

***If the Issuer, the Guarantor or any of their respective subsidiaries is unable to comply with the restrictions and covenants in their respective debt agreements, there could be a default under the terms of these agreements, which could cause repayment of its debt to be accelerated.***

If the Issuer, the Guarantor or any of their respective subsidiaries is unable to comply with the restrictions and covenants in their respective current or future debt obligations and other agreements, there could be a default under the terms of these agreements. In the event of a default under these agreements, the holders of the debt could terminate their commitments to lend, accelerate repayment of the debt and declare all outstanding amounts due and payable or terminate the agreements, as the case may be. Furthermore, some of the Issuer's or the Guarantor's debt agreements, contain cross-acceleration or cross-default provisions. As a result, a default under one debt agreement may cause the acceleration of repayment of not only such debt but also other debt, including the Bonds, or result in a default under the Issuer's the Guarantor's or such other subsidiary's other debt agreements. If any of these events occur, there is no assurance that the Issuer or the Guarantor would have sufficient assets and cash flow to repay in full all of its indebtedness, or that the Issuer or the Guarantor would be able to find alternative financing. Even if the Issuer or the Guarantor could obtain alternative financing, it could not guarantee that it would be on terms that are favorable or acceptable to the Issuer or the Guarantor.

***Renminbi is not freely converted into foreign currency and remitted out of China, which may limit our ability to utilize its revenue effectively and affect the value of your investment.***

We expect that a substantial majority of our future revenues will be denominated in Renminbi. Under existing PRC foreign exchange regulations, payments of current account items, including profit distributions, interest payments and trade and service-related foreign exchange transactions, can be made in foreign currencies without prior SAFE approval as long as certain routine procedural requirements are fulfilled. Therefore, our PRC subsidiaries are allowed to pay dividends in foreign currencies to us without prior SAFE approval by following certain routine procedural requirements. However, approval from or registration with competent government authorities is required where the Renminbi is to be converted into foreign currency and remitted out of China to pay capital expenses such as the repayment of loans denominated in foreign currencies. The PRC government may at its discretion restrict access to foreign currencies for current account transactions in the future.

***Any failure to complete the relevant filings under the NDRC Circular within the prescribed time frame following the completion of the issue of the Bonds may have adverse consequences for the Issuer, the Guarantor and/or the investors in the Bonds.***

On September 14, 2015, the NDRC promulgated the NDRC Circular, which came into effect on the same day. According to the NDRC Circular, if a PRC enterprise or an offshore enterprise controlled by a PRC enterprise wishes to issue bonds outside of the PRC with a maturity of more than one year, such enterprise must in advance of issuing such bonds, file certain prescribed documents with the NDRC and obtain a registration certificate from the NDRC in respect of such issue. According to the NDRC Circular, the NDRC will decide whether to accept a submission within five working days upon receipt of the submission and is expected to issue a decision on the submission within seven working days after it accepts the submission. The enterprise must also report certain details of the bonds to the NDRC within 10 business days upon the completion of the bond issue. The NDRC Circular is silent on the legal consequences of non-compliance with the pre-issue registration requirement. Similarly, there is no clarity on the legal consequences of non-compliance with the post-issue notification requirement under the NDRC Circular. Failure to comply with the post-issuance filing requirement may result in the relevant entities being put on the credit blacklist in the PRC and subject them to credit-related sanctions. Potential investors in the Bonds are advised to exercise due caution when making their investment decisions.

***Exchange rate risks and exchange controls may affect an investor's returns on the Bonds.***

The Group will pay principal on the Bonds in U.S. dollars. This presents certain risks relating to currency conversions if an investor's financial activities are denominated principally in a currency or currency unit (the "**Investor's Currency**") other than U.S. dollars. These include the risk that exchange rates may significantly change (including changes due to devaluation of the U.S. dollar or revaluation of the Investor's Currency) and the risk that authorities with jurisdiction over the Investor's Currency may impose or modify exchange controls. An appreciation in the value of the Investor's Currency relative to the U.S. dollar would decrease (i) the Investor's Currency-equivalent yield on the Bonds; (ii) the Investor's Currency-equivalent value of the principal payable on the Bonds; and (iii) the Investor's Currency-equivalent market value of the Bonds. Government and monetary authorities may impose (as some have done in the past) exchange controls that could adversely affect an applicable exchange rate. As a result, investors may receive less principal than expected, or no principal.

***Legal investment considerations may restrict certain investments.***

The investment activities of certain investors are subject to legal investment laws and regulations, or review or regulation by certain authorities. Each potential investor should consult its legal advisers to determine whether and to what extent:

- the Bonds are legal investments for it;
- the Bonds can be used as collateral for various types of borrowing; and
- any other restrictions apply to its purchase or pledge of the Bonds.

Financial institutions should consult their legal advisers or the appropriate regulators to determine the appropriate treatment of the Bonds under any applicable risk-based capital or similar rules.

***The Issuer's ability to make payments under the Bonds depends on timely payments by the Guarantor or its subsidiaries and affiliates under the on-lent loans.***

The Issuer is a direct wholly-owned subsidiary of the Guarantor with limited operations of its own and will on-lend the entire proceeds from the issue of the Bonds to the Guarantor or its subsidiaries and affiliates.

The Issuer has limited net assets other than such loans and its ability to make payments under the Bonds depends on timely payments under such loans. In the event that the Guarantor or its subsidiaries and affiliates do not make such payments, due to the Guarantor's lack of available cash flow or other factors, the Issuer's ability to make payments under the Bonds may be adversely affected.

***The insolvency laws of Hong Kong, the Cayman Islands and other local insolvency laws may differ from those of any other jurisdiction with which holders of the Bonds are familiar.***

Since the Issuer is incorporated under the laws of Hong Kong and the Guarantor is incorporated under the laws of the Cayman Islands, an insolvency proceeding relating to the Issuer or the Guarantor, even if brought in other jurisdictions, would likely involve Hong Kong or Cayman Islands (as the case may be) insolvency laws, the procedural and substantive provisions of which may differ from comparable provisions of bankruptcy law in other jurisdictions. We conduct most of our business operations in the PRC. The laws and regulations in the PRC relating to bankruptcy and insolvency and the legal proceedings in that regard may significantly differ from those of other jurisdictions with which the holders of the Bonds are familiar. Investors should analyze the risks and uncertainties carefully before they invest in the Bonds.

***Potential dilution of the ownership interest of existing Shareholders.***

The conversion of some or all of the Bonds will dilute the ownership interests of the existing shareholders of the Guarantor. Any sales in the public market of the Class B Shares issuable upon such conversion could adversely affect prevailing market prices for the Class B Shares. In addition, the existence of the Bonds may facilitate short selling of the Class B Shares by market participants.

***The Group relies on dividends paid by its subsidiaries for cash needs, and limitations under PRC laws on the ability of the Group's PRC subsidiaries to distribute dividends to the Group could adversely affect the Group's ability to utilize such funds.***

As a holding company, the Guarantor relies on dividends paid by its PRC subsidiaries for the Group's cash and financing requirements, including the funds necessary to perform its payment obligations under the Bonds, to service any foreign currency debt the Group may incur and to make any offshore acquisitions. If any of the Group's PRC subsidiaries incur debt on its own behalf in the future, the loan agreements may restrict its ability to pay dividends or make other distributions to the Group. Under PRC laws and regulations, the Group's PRC subsidiaries may pay dividends only out of their respective accumulated profits as determined in accordance with PRC accounting standards and regulations. In addition, a wholly foreign-owned enterprise is required to set aside at least 10% of its accumulated after-tax profits each year, if any, to fund a certain statutory reserve fund, until the aggregate amount of such fund reaches 50% of its registered capital. Such reserve funds cannot be distributed to the Group as dividends. These limitations on the ability of the Group's PRC subsidiaries to transfer funds to the Group limit the Group's ability to receive and utilize such funds.

As a result of the foregoing, there is no assurance that the Guarantor will have sufficient cash flow from dividends or advances from its subsidiaries to satisfy its obligations under the Guarantee. Should the Guarantor be unable to make due payments under the terms of the Guarantee, the Bondholders would need to rely on the Trustee to take enforcement actions to recover their investment in the Bonds, the prospects of which are uncertain.

***The Bonds and the Guarantee will be structurally subordinated to subsidiary debt.***

Payments under the Bonds and the Guarantee will be structurally subordinated to the claims of all holders of debt securities and other creditors, including trade creditors, of the Issuer's and the Guarantor's subsidiaries, and to all secured creditors of the Issuer and the Guarantor. A substantial part of the Guarantor's operations are conducted through its subsidiaries, associated companies and jointly controlled entities. Accordingly, the Guarantor is and will be dependent on the operations of its subsidiaries, associated companies and jointly controlled entities to service its indebtedness, including interest and principal on the Bonds. In the event of an insolvency, bankruptcy, liquidation, reorganization, dissolution or winding up of the business of any subsidiary of the Issuer or the Guarantor, creditors of such subsidiary generally will have the right to be paid in full before any distribution is made to the Issuer or the Guarantor (as the case may be).

***The liquidity and price of the Bonds following the offering may be volatile.***

The price and trading volume of the Bonds may be highly volatile. Factors such as variations in our revenue, earnings and cash flows, proposals for new investments, strategic alliances and/or acquisitions, changes in interest rates, fluctuations in price for comparable companies, government regulations and changes thereof applicable to its industry and general economic conditions nationally or internationally could cause the price of the Bonds to change. Any such developments may result in large and sudden changes in the trading volume and price of the Bonds. There is no assurance that these developments will not occur in the future.

***The Issuer and the Guarantor may not have the ability to redeem the Bonds.***

Bondholders may require the Issuer, subject to certain conditions, to redeem for cash some or all of their Bonds at the option of the Bondholders upon a Relevant Event as described under "*Terms and Conditions of the Bonds – Redemption, Purchase and Cancelation – Redemption for Relevant Event*" or on the Put Option Date as described under "*Terms and Conditions of the Bonds – Redemption, Purchase and Cancelation – Redemption at the Option of the Bondholders*". The Issuer or the Guarantor (whom will be required to may payments pursuant to the Guarantee) may not have sufficient funds or other financial resources to make the required redemption in cash at such time or the ability to arrange necessary financing on acceptable terms, or at all. The Issuer's or the Guarantor's ability to redeem the Bonds in such event may also be limited by the terms of other debt instruments. Failure to repay, repurchase or redeem tendered Bonds by the Issuer or the Guarantor would constitute an event of default under the Bonds, which may also constitute a default under the terms of other indebtedness held by the Issuer or the Guarantor.

***The Bonds may be early redeemed at the Issuer's option.***

The Issuer may, on giving not less than 30 nor more than 60 days' notice, redeem the Bonds in whole, but not in part at their principal amount: (i) at any time after December 17, 2025, provided that the Closing Price of a Share (translated into U.S. dollars at the Prevailing Rate), for 20 out of 30 consecutive Trading Days, the last of which occurs not more than five Trading Days prior to the date upon which notice of such redemption is given, was at least 130 per cent. of the Conversion Price (translated into U.S. dollars at the Fixed Exchange Rate) then in effect immediately prior to the date upon which notice of such redemption is given; or (ii) at any time if, immediately prior to the date of such notice, Conversion Rights shall have been exercised and/or purchases (and corresponding cancelations) and/or redemptions effected in respect of 90 per cent. or more in aggregate principal amount of the Bonds originally issued. In addition, the Bonds may be redeemed at the option of the Issuer in whole and not in part, on giving not less than 30 days' nor more than 60 days' notice, at their principal amount, if the Issuer satisfies the Trustee immediately prior to the giving of such notice that the Issuer (or if the Guarantee was called, the Guarantor) has or will become obliged to pay Additional Tax Amounts as a result of certain events set out in the Conditions and such obligation cannot be avoided by the Issuer (or, as the case may be, the Guarantor) taking reasonable measures available to it. As a result, the trading price of the Bonds may be affected when any redemption option of the Issuer becomes exercisable. Accordingly, Bondholders may not be able to sell their Bonds at an attractive price, thereby having a material adverse effect on the trading price and liquidity of the Bonds.

***Bondholders have limited anti-dilution protection.***

The Conversion Price will be adjusted in the event that there is a sub-division, consolidation or re-denomination, rights issues, bonus issue, reorganization, capital distribution or other adjustment including an offer or scheme which affects Class B Shares, but only in the circumstances and only to the extent provided in "*Terms and Conditions of the Bonds – Conversion*". There is no requirement that there should be an adjustment for every corporate or other event that may affect the value of the Class B Shares. Events in respect of which no adjustment is made may adversely affect the value of the Class B Shares and, therefore, adversely affect the value of the Bonds.

***Future issuances of Class B Shares or equity-related securities may depress the trading price of the Shares.***

Any issuance of the Guarantor's equity securities after this offering could dilute the interest of the existing shareholders and could substantially decrease the trading price of the Class B Shares. The Guarantor may issue equity securities in the future for a number of reasons, including to finance its operations and business strategy (including in connection with acquisitions, strategic collaborations or other transactions), to adjust its ratio of debt-to-equity, to satisfy its obligations upon the exercise of outstanding warrants, options or other convertible bonds or for other reasons. Sales of a substantial number of Class B Shares or other equity-related securities in the public market (or the perception that such sales may occur) could depress the market price of the Class B Shares. The Guarantor cannot predict the effect that future sales of the Class B Shares or other equity-related securities would have on the market price of the Class B Shares. In addition, the price of the Class B Shares could be affected by possible sales of the Class B Shares by investors who view the Bonds as a more attractive means of obtaining equity participation in the Guarantor and by hedging or engaging in arbitrage trading activity involving the Bonds.

***There may be less publicly available information about the Guarantor than is available for public companies in certain other jurisdictions.***

There may be less publicly available information about companies listed in Hong Kong, such as the Guarantor, than is regularly made available by public companies in certain other countries. In addition, our financial information in this Offering Circular has been prepared in accordance with IFRS which differ in certain respects from generally accepted accounting principles ("**GAAPs**") in certain jurisdictions which might be material to the financial information contained in this Offering Circular. In making an investment decision, investors must rely upon their own examination of us, the terms of the offering and our financial information, and should consult their own professional advisers for an understanding of the differences between IFRS and the GAAPs in their home jurisdictions and how those differences might affect the financial information contained in this Offering Circular.

***The Bonds will initially be represented by the Global Certificate and holders of a beneficial interest in the Global Certificate must rely on the procedures of the relevant Clearing System.***

The Bonds will initially be represented by the Global Certificate. Such Global Certificate will be deposited with a common depositary for Euroclear and Clearstream (each of Euroclear and Clearstream, a "**Clearing System**"). Except in the circumstances described in the Global Certificate, investors will not be entitled to receive definitive Bonds. The relevant Clearing System will maintain records of the beneficial interests in the Global Certificate. While the Bonds are represented by the Global Certificate, investors will be able to trade their beneficial interests only through the Clearing Systems.

While the Bonds are represented by the Global Certificate, the Issuer will discharge its payment obligations under the Bonds by making payments to the common depositary for Euroclear and Clearstream, for distribution to their account holders. A holder of a beneficial interest in the Global Certificate must rely on the procedures of the relevant Clearing System to receive payments under the Bonds. The Issuer has no responsibility or liability for the records relating to, or payments made in respect of, beneficial interests in the Global Certificate.

Holders of beneficial interests in the Global Certificate will not have a direct right to vote in respect of the Bonds. Instead, such holders will be permitted to act only to the extent that they are enabled by the relevant Clearing System to appoint appropriate proxies.

***Short selling of the Class B Shares by Bondholders could materially and adversely affect the market price of the Class B Shares.***

The issuance of the Bonds may result in downward pressure on the market price of the Class B Shares. Investors in convertible securities may seek to hedge their exposure in the underlying equity securities, often through short selling of the underlying equity securities or similar transactions. Any short selling and similar hedging activity could place significant downward pressure on the market price of the Class B Shares, thereby having a material adverse effect on the market value of the Class B Shares owned by an investor as well as on the trading price of the Bonds.

## CAPITALIZATION AND INDEBTEDNESS

The following table sets forth on an actual basis the Guarantor's borrowings and capitalization as of September 30, 2020 and as adjusted to give effect to the issuance of the Bonds in this offering after deducting the Managers' commissions and other estimated expenses payable by the Guarantor in connection with this offering. The table should be read in conjunction with the financial statements and the accompanying notes included elsewhere in this Offering Circular.

| | As of September 30, 2020 | | | |
|---|---|---|---|---|
| | Actual | | Adjusted | |
| | RMB | US$ | RMB | US$ |
| | (in thousands) | | | |
| Cash and cash equivalents | 30,257,712 | 4,456,479 | 36,294,006 | 5,345,529 |
| Restricted cash | 3,257,432 | 479,768 | 3,257,432 | 479,768 |
| **Total cash** | **33,515,144** | **4,936,247** | **39,551,438** | **5,825,297** |
| Short-term bank deposits | 14,156,263 | 2,084,992 | 14,156,263 | 2,084,992 |
| Short-term investments measured at fair value through profit or loss | 21,097,732 | 3,107,360 | 21,097,732 | 3,107,360 |
| **Short-term debt:** | | | | |
| Borrowings | 11,385,210 | 1,676,860 | 11,385,210 | 1,676,860 |
| **Total short-term debt** | **11,385,210** | **1,676,860** | **11,385,210** | **1,676,860** |
| **Long-term debt:** | | | | |
| Borrowings | 7,183,648 | 1,058,037 | 7,183,648 | 1,058,037 |
| Bonds offered hereby(1) | – | – | 6,036,294 | 889,050 |
| **Total long-term debt** | **7,183,648** | **1,058,037** | **13,219,942** | **1,947,087** |
| Share capital | 392 | 58 | 392 | 58 |
| Reserves | 94,228,146 | 13,878,306 | 94,228,146 | 13,878,306 |
| **Equity attributable to equity holders of the Company** | **94,228,538** | **13,878,364** | **94,228,538** | **13,878,364** |
| Non-controlling interests | 339,840 | 50,053 | 339,840 | 50,053 |
| **Total equity** | **94,568,378** | **13,928,417** | **94,568,378** | **13,928,417** |
| **Total capitalization(2)** | **101,412,186** | **14,936,401** | **107,448,480** | **15,825,451** |

Notes:

(1) As adjusted as of September 30, 2020 to give effect to the issue of the Bonds and the net proceeds we are expecting to receive from the issue of the Bonds (after deducting underwriting commissions and certain estimated offering expenses). In accordance with International Accounting Standard *Financial Instruments: Presentation*, the Bonds are accounted for as compound financial instruments containing both a liability component and an equity component. For illustrative purpose, the aggregate net proceeds we are expecting to receive from the issue of the Bonds (after deducting underwriting commissions and certain estimated offering expenses) will be assumed as the liability component and no allocation to the equity component will be made.

(2) Total capitalization equals total long-term debt plus equity attributable to equity holders of the Company.

Except as disclosed herein and the placing of 1,000,000,000 Class B Shares to placees as set out in the Company's announcements dated December 2, 2020 and December 3, 2020, there have been no material changes in the Company's total capitalization since September 30, 2020.

# DESCRIPTION OF THE ISSUER

## Formation

The Issuer is a public company limited by shares incorporated in Hong Kong on December 20, 2018. Its registered office is located at Suite 3210, 32/F, Tower 5, The Gateway, Harbour City, 15 Canton Road, Tsim Sha Tsui, Kowloon, Hong Kong.

## Business Activity

The Issuer's primary purpose is to engage in financing related activities, including the issuance and offering of the Notes and the Bonds, in relation to the Company and the Group. As of the date of this Offering Circular, the Issuer has no material assets. In the future, the Issuer may engage in other financing related activities in relation to the Company and the Group and may incur substantial liabilities and indebtedness.

## Directors

The directors of the Issuer are Lin Bin and Chew Shou Zi.

## Share Capital

The Issuer is authorized to issue up to a maximum of 500,000,000 ordinary shares of a single class, all of which have been issued and are fully paid. No part of the equity securities of the Issuer is listed or dealt in on any stock exchange.

# USE OF PROCEEDS

The net proceeds we expect to receive from this offering, after deducting underwriting commissions and certain estimated offering expenses, will be approximately US$889.1 million. We intend to use the net proceeds of this offering for (i) strengthening our working capital for business expansion, (ii) investments to increase market share in key markets, (iii) strategic ecosystem investments, and (iv) other general corporate purposes.

The foregoing represents our current intentions based upon our present plans and business conditions to use and allocate the net proceeds of this offering. Our management, however, will have significant flexibility and discretion to apply the net proceeds of this offering subject to the applicable mainland China laws and regulations. If an unforeseen event occurs or business conditions change, we may use the proceeds of this offering differently than as described in this Offering Circular subject to the applicable mainland China laws and regulations.

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

*The following discussion should be read in connection with "Summary Financial Information" and our consolidated financial statements, including the notes thereto, included elsewhere in this Offering Circular. Certain statements in this "Management's Discussion and Analysis of Financial Condition and Results of Operations" are forward-looking statements. See "Forward-Looking Statements" regarding these statements. Our historical consolidated financial statements have been prepared in accordance with IFRS.*

### OVERVIEW

Xiaomi is an internet company with smartphones and smart hardware connected by an IoT platform at its core. Our unique and powerful "triathlon" business model comprises three synergistic pillars of growth – (i) innovative, high quality and well-designed hardware focused on exceptional user experience, (ii) highly efficient new retail distribution platform allowing for our products to be priced accessibly and (iii) engaging internet services.

We offer a broad range of hardware products developed in-house or in collaboration with our ecosystem partners. Innovation, quality, design and user experience are ingrained in all of our products regardless of whether they are developed in-house or in collaboration with our partners. We strive to offer our products at price points that are accessible to the widest user base to enjoy broad adoption and high retention. For our core in-house products, we focus on designing and developing a range of cutting-edge hardware products including smartphones, laptops, smart TVs, AI speakers, smart routers, smart watches, smart refrigerators, smart washing machines and smart air conditioners. We curate a wide range of additional products by investing in an ecosystem of over 300 companies. We also curate a range of lifestyle products to further drive brand awareness and traffic to our sales points.

Our highly efficient omni-channel new retail distribution platform is a core component of our growth strategy, allowing us to operate efficiently while simultaneously extending our user reach and enhancing our users' experience. Since inception, we have focused on direct online sales of our products to maximize efficiency and build a direct digital relationship with users. We have continually expanded our direct offline retail network, for example, through our self-operated Mi Home stores. Moreover, to establish our offline new retail presence in lower-tier cities and rural areas of China, we have built a sizable authorized store network. Our offline retail network allows us to broaden our reach and provide a richer user experience, while maintaining similar efficiency and the same product prices as our online channels. Our efficient omni-channel sales strategy enables us to provide our products at accessible price points to the largest user base.

We provide internet services to give our users a complete mobile internet experience. In September 2020, we had 368.2 million MAU on MIUI, our proprietary operating system built on the Android kernel. MIUI fully embraces the Android ecosystem, including all mobile apps. It functions as an open platform for us to deliver our wide range of internet services, such as content, entertainment, financial services and productivity tools. The connectivity between our devices and the seamless integration between smart hardware and internet services enable us to provide our users with better user experience. Compared to other internet platforms that acquire new users at high costs, we leverage the sale of our hardware to acquire users at a profit.

Our total revenues increased from RMB114.6 billion in 2017 to RMB174.9 billion in 2018; and increased to RMB205.8 billion in 2019. Our total revenue was RMB175.4 billion for the nine months ended September 30, 2020. We had a loss of RMB43.9 billion in 2017, and profits of RMB13.5 billion, RMB10.1 billion and RMB11.5 billion in 2018, 2019 and for the nine months ended September 30, 2020, respectively. We had non-IFRS Adjusted Net Profit of RMB5.4 billion, RMB8.6 billion, RMB11.5 billion and RMB9.8 billion in 2017, 2018, 2019 and for the nine months ended September 30, 2020, respectively. See "– *Consolidated Income Statements*" and "– *Non-IFRS Measure: Adjusted Net Profit*" for details.

## MAJOR FACTORS AFFECTING OUR RESULTS OF OPERATIONS

Our results of operations have been, and are expected to continue to be, materially affected by a number of factors, many of which are outside of our control, including the following:

### General Factors

Our business and operating results are affected by general factors affecting the broader internet industry and the consumer electronics industry in mainland China and in the overseas markets where we focus. These factors include:

- overall economic growth and level of per capita disposable income;
- growth of mobile internet usage and penetration rate;
- growth and competition of the smartphone, IoT and lifestyle product markets;
- growth and competition of the internet service markets; and
- new and substantially more superior technology products and services.

Unfavorable changes in any of these general industry conditions could negatively affect demand for our products and services and materially adversely affect our results of operations.

### Specific Factors

Our results of operations are also affected by specific factors affecting our results of operations, including the following major factors:

#### *Popularity of Our Products*

A substantial majority of our revenues is derived from sales of products, in particular smartphones, as well as the IoT and lifestyle products. Revenue growth in our smartphones segment and our IoT and lifestyle products segment in recent years was primarily driven by increased sales of existing products, including new models, and the category expansion of our product offerings. To maintain our growth momentum, we must continue to innovate and develop high-quality, well-designed and user-centric products to increase sales. Furthermore, revenues from our smartphones and our IoT and lifestyle products segments are affected by the selling price of our products, which is in turn affected by changes in the cost of components and raw materials, the anticipated demand for new models, the income levels of target users, changes in the mix of sales channels, the historical sales volume of previous models, and the prices of comparable products. In particular, the average selling price for smartphones typically declines during its life cycle. The effect of such declining average selling prices of our existing smartphone models has been offset by our continued introduction of new and enhanced models and our expanded product category offerings.

#### *Expansion and Penetration in Overseas Markets*

We have experienced significant growth in international operations in recent years in many overseas markets. Geographically, we generated 28.0%, 40.0%, 44.3% and 50.5% of our revenues in countries and regions outside mainland China in 2017, 2018, 2019 and for the nine months ended September 30, 2020, respectively. As of September 30, 2020, we sell our products in over 90 countries and regions across five continents. We believe our global opportunity is significant, and we will continue to enhance our sales and marketing efforts, expand our distribution channels, and invest in infrastructure and personnel to support our international expansion. We intend to leverage our strong execution abilities to localize our unique business model internationally. We believe our smartphone's leading position in many overseas markets lays a strong foundation for us to further expand our user base and internet services offerings to enhance user experience and further increase user monetization in those markets. We may have to adapt our business model to the local markets due to various legal requirements and market conditions. Fluctuation in currency exchange rates between our main transaction currencies and foreign currencies used in overseas markets may impact our financial condition and operating results.

### *Growth of Internet Services Revenues*

Our internet services segment has achieved high gross profit margins, which plays a significant role in our overall profitability.

The growth of our internet services revenues ultimately depends on the breadth of our internet service offerings, the size of our user base and the level of user engagement and spending. We derive our internet services revenue primarily from advertising and internet value-added services. Advertisers are drawn to our platform because of the size of our user base, the level of our user engagement and the attractive demographics of our user base. Our value-added services depend on the overall size of our user base, in particular the number of paying users, as well as the level of user engagement. Our ability to maintain and expand our user base, as well as maintaining and enhancing user engagement and spending, depends on, among other things, our ability to continuously offer popular services, recommend personalized services and content through technological innovation and provide a superior user experience. We will continue to leverage our big data analytic capabilities and the resulting nuanced understanding of user interests to stay abreast of evolving user demand and preferences and introduce more popular and personalized products and services.

### *Strategic Investments*

We have invested in a large number of companies both in mainland China and in the rest of the world. As of September 30, 2020, the Company had invested in more than 300 companies with an aggregated book value of approximately RMB39.5 billion, as compared with RMB30.0 billion as of December 31, 2019. Many of our investments have since become very successful. Our investee companies Huami Corporation (NYSE: HMI) and Viomi Technology Co., Ltd (Nasdaq: VIOT) successfully completed their listings on the New York Stock Exchange in February 2018 and on the Nasdaq Stock Market in September 2018, respectively. In February 2020, Roborock (SH: 688169), an investee company which produces robot vacuum cleaners for our Company, was successfully listed on the Science and Technology Innovation Board of Shanghai Stock Exchange in mainland China. In May 2020, Kingsoft Cloud Holdings Ltd. (Nasdaq: KC), an investee company, successfully listed on the Nasdaq Stock Market. In October 2020, Ninebot Limited (SH: 689009), one of our investee companies that produces electric scooters, successfully listed on the Science and Technology Innovation Board of the Shanghai Stock Exchange. These investee companies can efficiently expand our product and service offerings, provide proprietary technologies complementary to ours, or expand our overseas footprint. We believe our strategic investments can provide us with an additional stream of recurring income. We plan to continue to invest in businesses that are complementary to our business and growth strategies. Such investments may impact our results of operations and financial condition, depending on the amount involved and the performance of the companies in which we invest. In 2017, 2018, 2019 and the nine months ended September 30, 2020, our fair value gains on investments measured at fair value through profit or loss were RMB6.4 billion, RMB4.4 billion, RMB3.8 billion and RMB6.1 billion, respectively.

### *Management of Supply-related Costs*

For our smartphones segment and IoT and lifestyle products segment, raw materials, component and assembly costs of our in-house products, as well as the cost of procuring ecosystem products from our partners, have historically accounted for the largest portion of our cost of sales. Since the early stage of our development, we have adopted a contract-based outsourcing model for the assembly of our in-house products under which we strictly control the procurement, production and quality assurance processes. Our ability to effectively control our supply and other production-related costs has affected and will continue to affect our profitability. For products not developed in-house, we rely on our ecosystem partners to supply finished products. Cost of sales for the sale of such ecosystem products comprises primarily the production cost of such products and revenue-sharing with our partners. We proactively manage the cost of the ecosystem products supplied by our partners, and we believe maintaining a mutually beneficial relationship with our ecosystem partners is critical to our business and growth prospects. We provide ecosystem partners with significant business demand, allowing them to commercially launch their products and ramp up their business rapidly. Our ecosystem partners, on the other hand, leverage their research and development capabilities and help us quickly enter into new market segments, enabling us to expand our product portfolio.

To a lesser extent, our cost of sales had been impacted by fluctuations in foreign currency exchange rates as a result of our global operations. We are exposed to foreign exchange risks from trade receivables and trade payables when we receive foreign currencies from, or pay foreign currencies to overseas business partners.

For our internet services segment, revenue-sharing with game developers and other content providers accounted for a significant portion of our cost of sales. Our ability to maintain a mutually beneficial relationship with our internet service partners in order to assure and improve the high quality and attractiveness of our internet services to users will significantly affect our results of operations.

***Investment in People, Technology and Infrastructure***

We are a technology company operating in intensely competitive markets. We have made, and will continue to make, significant investments in people, technology and infrastructure, to solidify our market leadership and to provide great user experience. Talent attraction and retention are critical for our business operations and growth prospects as we invest more in R&D, expand our product and service offerings, and broaden our retail channels. We will continue to invest in our people, particularly engineers, designers and product management personnel.

In addition, we have dedicated and will continue to dedicate significant resources to research and development. Our patent portfolio, especially global patent portfolio, has grown rapidly in recent years as a result of our continued investments. We expect our future investments will include designing and developing new products and services with enhanced functionalities and features, as well as continued building of our patent reserve around the world. We will also continue to upgrade and expand our technology infrastructure to keep pace with the growth of our business. We have invested significant resources in the development of our 5G, cloud, big data and AI capabilities in recent years, and we expect to continue to do so in the near future.

***Marketing and Brand Promotion***

One of our growth strategies is to attract new users through enhancing our brand recognition. Instead of incurring a large amount of selling and marketing expenses for a company of our size, we rely on word-of-mouth marketing through continued offering of popular products and services. We broadened our user base beyond the tech-savvy crowd through a variety of selected sales and marketing initiatives, as well as effective brand promotion campaigns which resulted in an increase in our selling and marketing expenses both in absolute amount and also as a percentage of our total revenues. Such efforts include expanding the large network of Mi Home stores, conducting online, TV and other offline advertising campaigns, as well as engaging popular celebrities for the promotion of our brands. As we continue to increase our domestic and global footprints, our marketing and brand promotion expenses may continue to increase in the near future.

***Management of Working Capital***

Our ability to effectively control our working capital has affected and will continue to affect our cash flow from operations. We actively manage our trade receivables for sales of goods and provision of services, and our trade payables for goods and services from our suppliers. We leverage our scale to negotiate attractive contractual terms with our customers and suppliers. In addition, we intend to maintain appropriate inventory levels to meet the market demand for our products.

***Capital Expenditures on Land Use Rights and Office Buildings***

To accommodate our growth in staff headcount, as well as our expanding domestic and global footprint in the most cost-effective manner, we have acquired and will continue to acquire land use rights and dedicate resources towards the construction of office buildings in favorable locations. As we expand our footprint into more countries and regions, our capital expenditures may influence our overall liquidity.

## CRITICAL ACCOUNTING POLICIES AND ESTIMATES

We set forth below the principal accounting policies applied in the preparation of our historical consolidated financial statements.

Some of our accounting policies require us to apply estimates and assumptions as well as complex judgments related to accounting items. The estimates and assumptions we use and the judgments we make in applying our accounting policies have a significant impact on our financial position and operating results. Our management continually evaluates such estimates, assumptions and judgments based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

We make estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal to the related actual results. We set forth below those estimates and assumptions that we believe may have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

For more details on our significant accounting policies and critical accounting estimates and judgments, see Note 2 and Note 4 of the consolidated financial statements included in this Offering Circular.

### Revenue Recognition

We principally derive revenue from sales of products and provision of internet services.

Revenue is measured at the fair value of the consideration received or receivable, and represents amounts receivable for goods sold or services performed, stated net of discounts, returns and value-added taxes. We recognize revenue when the specific criteria have been met for each of our activities, as described below.

#### *Sales of Products*

Revenue from the sale of products, which mainly includes smartphones, IoT and lifestyle products, directly to our customers is recognized when the control of the goods has been transferred upon the acceptance of products by our customers. Customers have full discretion over the products, and there is no unfulfilled obligation that could affect customers' acceptance of the products.

We collect cash from our customers before or upon deliveries of products mainly through banks or third-party online payment platforms. Cash collected from our customers before the acceptance of products is recognized as advance from customers. In mainland China, we generally allow customers to return our products purchased online for any reason within seven days from the date of purchase except for certain limited products that we allow return only if the packages of the products are unpacked, and we generally allow customers to exchange any defective products within 15 days from the date of purchase. We base our estimates of sales return on historical results, taking into consideration the type of customers, the type of transactions and the specifics of each arrangement.

#### *Internet Services*

Internet services mainly comprise advertising services and internet value-added services.

*Advertising Services*

We generate advertising revenues primarily from display-based and performance-based advertisements.

Revenue from display-based advertisements to our users of smartphones and other devices are recognized on a straight-line basis over the contract period.

Revenue from performance-based advertisements is recognized based on actual performance measurement. We recognize revenue from the delivery of advertisements, typically based on (i) per-click when the users click on the content, (ii) per-impression when the advertising contents are displayed to users, or (iii) per-download when the third-party apps are downloaded by users.

*Internet Value-Added Services*

We recognize revenues from internet valued-added services, including online games and fintech business, on a gross or net basis depending on whether we are acting as a principal or an agent in the transaction. For online games, we defer related revenues, over the estimated user relationship periods, when there is an explicit or implicit obligation for us to maintain the relevant applications and allow users to have access to them.

Our fintech revenues primarily consist of financial interest income and intermediary services income.

We generate financial interest income from provision of loans through our own online finance platform. Financial interest income is recognized over the terms of loan receivables using the effective interest method.

We also provide intermediary services to the borrowers and third party funding parties (as the lenders). We are determined as neither the legal lender nor the legal borrower in the loan origination and repayment process. Therefore, we do not record loans receivable and payable arising from the loans between lenders and borrowers. We act as an agent to facilitate such loans. We consider the loan facilitation and post-lending management services as distinct performance obligations because both the borrowers and lenders can benefit from the loan facilitation services and post-lending management services on their own, and those services are clearly stated in the contract and are separately identifiable, they are not integrated or interrelated with each other, and do not significantly affect each other. For intermediary services with a financial guarantee obligation, the Group first allocates the total transaction price to the financial guarantee liability, then the remaining consideration is allocated to loan facilitation and post-lending management services on the basis of the relative standalone selling prices, determined by using the cost plus margin approach; for intermediary services with no financial guarantee obligation, the Group allocates the total consideration to loan facilitation and post-lending management services on the basis of the relative standalone selling prices, determined by using the cost plus margin approach. Revenues from loan facilitation services are recognized at point-in-time upon the successful matching between the borrowers and the lenders. Revenues from post-lending management services are recognized ratably over the terms of the underlying loans as the performance obligation is satisfied over time.

We determine whether our revenue should be reported gross or net based on a continuing assessment of various factors. When determining whether we are acting as the principal or agent in offering goods or services to a customer, we need to first identify who control the specified goods or services before the goods are sold or services are provided to the customer. We are a principal in a transaction if we obtain control of the goods or services before they are sold or provided to the customer. We are deemed to have control if we own: (i) a product or another asset from another party before the control is transferred to customers; (ii) a right to a service to be performed by another party, which provides us with the ability to direct such party to provide the service to customers on our behalf; or (iii) a product or service from another party before being combined with other products or services and provided to customers. If the control is unclear, we consider the following factors: (i) who is the primary obligor in the arrangement; (ii) who has latitude in establishing the selling price; and (iii) who has inventory risks. Therefore, we have adopted different revenue recognition methods based on our specific roles and responsibilities in different goods or services offerings.

We do not expect to have any contracts under which the period between the transfer of the subject products or services to customers and the payment by the customers exceeds one year. As a result, we do not adjust any of the transaction prices for the time value of money.

**Foreign Currency Translation**

***Functional and Presentation Currency***

Items included in the financial information of each of our entities are measured using the currency of the primary economic environment in which the entity operates, or the functional currency. The functional currency of our Company is United States dollar. Our primary subsidiaries were incorporated in mainland China and these subsidiaries considered RMB as their functional currency. We determined to present our historical financial information in RMB (unless otherwise stated).

***Transactions and Balances***

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation when items are re-measured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the consolidated income statements.

Foreign exchange gains and losses are presented as "other gains/(losses), net" in our consolidated income statements.

Translation differences on non-monetary financial assets and liabilities, such as instruments held at fair value through profit or loss, are recognized in profit or loss as part of the fair value changes.

***Group Companies***

The results and financial position of all of our entities (none of which has the currency of a hyper-inflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;

- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions); and

- all resulting currency translation differences are recognized in other comprehensive income, or OCI.

Goodwill and fair value adjustments arising from the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated using the exchange rate on the closing date of the transaction. Currency translation differences are recognized in other comprehensive income.

***Disposal of Foreign Operation and Partial Disposal***

On the disposal of a foreign operation (that is, a disposal of our entire interest in a foreign operation, or a disposal involving loss of control over a subsidiary that includes a foreign operation, a disposal involving loss of joint control over a joint venture that includes a foreign operation, or a disposal involving loss of significant influence over an associate that includes a foreign operation), all of the currency translation differences accumulated in equity in respect of that operation attributable to the owners of our Company are reclassified to profit or loss.

In the case of a partial disposal that does not result in us losing control over a subsidiary that includes a foreign operation, the proportionate share of accumulated currency translation differences are re-attributed to non-controlling interests and are not recognized in profit or loss. For all other partial disposals (that is, reductions in our ownership interest in associates or joint ventures that do not result in us losing significant influence or joint control), the proportionate share of the accumulated exchange difference is reclassified to profit or loss.

**Financial assets**

***Classification***

We classify our financial assets in the following measurement categories:

- those to be measured subsequently at fair value (either through other comprehensive income, or through profit or loss), and

- those to be measured at amortized cost.

The classification depends on our business model for managing the financial assets and the contractual terms of the cash flows.

For assets measured at fair value, gains and losses will either be recorded in profit or loss or other comprehensive income. For investments in debt instruments, this will depend on the business model in which the investment is held. For investments in equity instruments that are not held for trading, this will depend on whether we have made an irrevocable election at the time of initial recognition to account for the equity investment at fair value through other comprehensive income.

We reclassify debt investments when and only when our business model for managing those assets changes.

***Measurement***

At initial recognition, we measure a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at fair value through profit or loss are recorded in profit or loss.

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

***Debt Instruments***

Subsequent measurement of debt instruments depends on our business model for managing the asset and the cash flow characteristics of the asset. There are three measurement categories into which we classify our debt instruments:

- *Amortized cost*. Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortized cost. A gain or loss on a debt investment that is subsequently measured at amortized cost and is not part of a hedging relationship is recognized in profit or loss when the asset is derecognized or impaired. Interest income from these financial assets is included in finance income using the effective interest method.

- *Fair value through other comprehensive income, or FVOCI*. Assets that are held for collection of contractual cash flows and for selling the financial assets, where the assets' cash flows represent solely payments of principal and interest, are measured at FVOCI. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest income and foreign exchange gains and losses which are recognized in profit or loss. When the financial asset is derecognized, the cumulative gain or loss previously recognized in OCI is reclassified from equity to profit or loss and recognized in other gains/(losses), net. Interest income from these financial assets is included in finance income using the effective interest method. Foreign exchange gains and losses are presented in other gains/(losses), net.

- *Fair value through profit or loss*. Assets that do not meet the criteria for amortized cost or FVOCI are measured at fair value through profit or loss. A gain or loss on a debt investment that is subsequently measured at fair value through profit or loss and is not part of a hedging relationship is recognized in profit or loss and presented net in the consolidated income statement within other gains/(losses), net in the period in which it arises.

***Equity Instruments***

We subsequently measure all equity investments at fair value. Where we have elected to present fair value gains and losses on equity investment in OCI, there is no subsequent reclassification of fair value gains and losses to profit or loss following the derecognition of the investment. Dividends from such investments continue to be recognized in profit or loss as other income when our right to receive payments is established.

Changes in the fair value of financial assets at fair value through profit or loss are recognized in the consolidated income statements. Impairment losses (and reversal of impairment losses) on equity investments measured at FVOCI are not reported separately from other changes in fair value.

***Impairment***

We have the following types of financial assets subject to IFRS 9's expected credit loss model:

- loan receivables from fintech business;
- trade receivables for sales of goods or provision of services; and
- other receivables.

We assess the expected credit losses associated with its debt instruments carried at amortized cost on a forward-looking basis, and with the exposure arising from financial guarantee contracts. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

For trade receivables, we apply the simplified approach permitted by IFRS 9, which requires expected lifetime losses to be recognized from initial recognition of the receivables.

Impairment on other receivables is measured as either 12-month expected credit losses or lifetime expected credit loss, depending on whether there has been a significant increase in credit risk since the initial recognition. If a significant increase in credit risk of a receivable has occurred since the initial recognition, then impairment is measured as lifetime expected credit losses.

***Derecognition***

*Financial assets*

We derecognize a financial asset, if the part being considered for derecognition meets one of the following conditions: (i) the contractual rights to receive the cash flows from the financial asset expire; or (ii) the contractual rights to receive the cash flows from the financial asset have been transferred and we transfer substantially all the risks and rewards of ownership of such financial asset; or (iii) we retain the contractual rights to receive the cash flows of the financial asset, but assume a contractual obligation to pay the cash flows to the eventual recipient in an agreement that meets all the conditions of derecognition of transfer of cash flows ("pass through" requirement), and we transfer substantially all the risks and rewards of ownership of such financial asset.

Where a transfer of a financial asset in its entirety meets the criteria for derecognition, the difference between the two amounts below is recognized as profit or loss:

- the carrying amount of the financial asset transferred; and
- the sum of the consideration received from the transfer and any cumulative gains or losses that have been recognized directly in equity.

If we neither transfer nor retain substantially all the risks and rewards of ownership and continue to control the transferred asset, we continue to recognize the asset to the extent of its continuing involvement, and we recognize such asset as an associated liability.

*Asset-backed securities*

As part of our operations, we securitize financial assets, generally through the sale of these assets to special purpose vehicles which issue securities to investors. Further details on prerequisites for derecognition of financial assets are set out above. When the securitization of financial assets that qualify for derecognition, the relevant financial assets are derecognized in their entirety and a new financial asset or liabilities is recognized regarding the interest in the unconsolidated securitization vehicles that we acquired. When the securitization of financial assets that do not qualify for derecognition, the relevant financial assets are not derecognized, and the consideration paid by third parties are recorded as a financial liability; when the securitization of financial assets that partially qualify for derecognition, the book value of the transferred asset should be recognized between the derecognized portion and the retained portion based on their respective relative fair values, and the difference between the book value of the derecognized portion and the total consideration received from the derecognized portion shall be recorded in profit or loss.

*Other financial liabilities*

A financial liability is derecognized when the obligation under the liability is discharged, canceled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and a recognition of a new liability, and the difference between the respective carrying amounts is recognized in profit or loss.

**Intangible Assets**

***Goodwill***

Goodwill arises from the acquisition of subsidiaries and represents the excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identified net assets acquired.

For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the cash-generating units, or CGUs, or groups of CGUs, that is expected to benefit from the synergies of the combination. Each unit or group of units to which the goodwill is allocated represents the lowest level within the entity at which the goodwill is monitored for internal management purposes. Goodwill is monitored at the operating segment level.

Goodwill impairment reviews are undertaken annually or more frequently if events or changes in circumstances indicate a potential impairment. The carrying value of the CGU containing the goodwill is compared to the recoverable amount, which is the higher of value in use and the fair value less costs of disposal. Any impairment is recognized immediately as an expense and is not subsequently reversed.

***Licenses***

License includes third-party payment license and other licenses. Third-party payment license represents the license issued by the People's Republic of China government authorities that enable the Group to operate third-party payment business. Other licenses mainly include the licenses to use certain intellectual properties purchased from third parties. These acquired licenses are shown at historical cost. License that have an indefinite useful life are tested annually for impairment and carried at cost less accumulated impairment losses. Others are amortized over their estimated useful lives of 1 to 10 years using straight-line method.

***Trademarks, Patents and Domain Names***

Separately acquired trademarks, patents and domain names are shown at historical cost. Trademarks, patents and domain names acquired in a business combination are recognized at fair value at the acquisition date. Trademarks, patents and domain names have a finite useful life and are carried at cost less accumulated amortization. Amortization is calculated using the straight-line method to allocate the cost of trademarks, patents and domain names over their estimated useful lives of 1 to 16 years.

*Other Intangible Assets*

Other intangible assets mainly include computer software. They are initially recognized and measured at costs incurred to acquire and bring them to use. Other intangible assets are amortized on a straight-line basis over their estimated useful lives, and recorded in amortization within operating expenses in the consolidated income statements.

*Research and Development Expenditures*

Research expenditure is recognized as an expense as incurred. Costs incurred on development projects (relating to the design and testing of new or improved products) are capitalized as intangible assets when recognition criteria are fulfilled. These criteria include:

- it is technically feasible to complete the software product so that it will be available for use;
- management intends to complete the software product and use or sell it;
- there is an ability to use or sell the software product;
- it can be demonstrated how the software product will generate probable future economic benefits;
- adequate technical, financial and other resources to complete the development and to use or sell the software product are available; and
- the expenditure attributable to the software product during its development can be reliably measured.

Other development expenditures that do not meet these criteria are recognized as an expense as incurred.

*Leases*

We have changed our accounting policy for leases where we are the lessee. The new policy is described below.

Until December 31, 2018, leases of plant and equipment and office where we, as lessee, had substantially all the risks and rewards of ownership were classified as finance leases. Finance leases were capitalized at the lease's inception at the fair value of the leased property or, if lower, the present value of the minimum lease payments. The corresponding rental obligations, net of finance charges, were included in other short-term and long-term payables. Each lease payment was allocated between the repayment of lease liability and finance cost. The finance cost was charged to the profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The property and equipment acquired under finance leases was depreciated over the asset's useful life or over the shorter of the asset's useful life and the lease term if there was no reasonable certainty that we will obtain ownership at the end of the lease term. Leases in which a significant portion of the risks and rewards of ownership were retained by the lessor were classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) were charged to the consolidated income statement on a straight-line basis over the period of the lease.

From January 1, 2019, leases are recognized as a right-of-use asset and a corresponding liability at the date at which the leased asset is available for use by us.

Contracts may contain both lease and non-lease components. We allocate the consideration in the contract to the lease and non-lease components based on their relative stand-alone prices.

Assets and liabilities arising from a lease are initially measured on a present value basis. Lease liabilities include the net present value of the following lease payments:

- fixed payments (including in-substance fixed payments), less any lease incentives receivable;

- variable lease payment that are based on an index or a rate, initially measured using the index or rate as at the commencement date;

- amounts expected to be payable by us under residual value guarantees;

- the exercise price of a purchase option if we are reasonably certain to exercise that option; and

- payments of penalties for terminating the lease, if the lease term reflects us exercising that option.

Lease payments to be made under reasonably certain extension options are also included in the measurement of the liability.

The lease payments are discounted using the interest rate implicit in the lease. If that rate cannot be readily determined, which is generally the case for leases of us, the lessee's incremental borrowing rate is used, being the rate that the individual lessee would have to pay to borrow the funds necessary to obtain an asset of similar value to the right-of-use asset in a similar economic environment with similar terms, security and conditions.

To determine the incremental borrowing rate, we:

- where possible, use recent third-party financing received by the individual lessee as a starting point, adjusted to reflect changes in financing conditions since third party financing was received;

- use a build-up approach that starts with a risk-free interest rate adjusted for credit risk for leases held by us, which does not have recent third party financing; and

- make adjustments specific to the lease, e.g. term, country, currency and security.

Lease payments are allocated between principal and finance cost. The finance cost is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

Right-of-use assets are measured at cost comprising the following:

- the amount of the initial measurement of lease liability;

- any lease payments made at or before the commencement date less any lease incentives received;

- any initial direct costs; and

- restoration costs.

Right-of-use assets are generally depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis. If we are reasonably certain to exercise a purchase option, the right-of-use asset is depreciated over the underlying asset's useful life. We have chosen not to revalue its right-of-use assets.

Payments associated with short-term leases of cloud servers are recognized on a straight-line basis as an expense in profit or loss. Short-term leases are leases with a lease term of 12 months or less.

Lease income from operating leases where we are a lessor is recognized in income on a straight-line basis over the lease term. Initial direct costs incurred in obtaining an operating lease are added to the carrying amount of the underlying asset and recognized as expense over the lease term on the same basis as lease income. The respective leased assets are included in the balance sheet based on their nature. We did not need to make any adjustments to the accounting for assets held as lessor as a result of adopting the new leasing standard.

## CONSOLIDATED INCOME STATEMENTS

The following table sets forth a summary of our consolidated income statements with line items in absolute amounts and as percentages of our revenues for the periods indicated.

| | For the year ended December 31, | | | | | | | For the nine months ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2017 | | 2018 | | 2019 | | | 2019 | | 2020 | |
| | RMB | % | RMB | % | RMB | US$ | % | RMB | % | RMB | % |
| | | | | | | | | (Unaudited) | | (Unaudited) | |
| | (in thousands, except percentages) | | | | | | | | | | |
| **Revenue** | **114,624,742** | **100.0** | **174,915,425** | **100.0** | **205,838,682** | **29,566,876** | **100.0** | **149,368,958** | **100.0** | **175,402,749** | **100.0** |
| **Cost of sales** | **(99,470,537)** | **(86.8)** | **(152,723,486)** | **(87.3)** | **(177,284,649)** | **(25,465,346)** | **(86.1)** | **(128,658,228)** | **(86.1)** | **(149,977,190)** | **(85.5)** |
| **Gross profit** | **15,154,205** | **13.2** | **22,191,939** | **12.7** | **28,554,033** | **4,101,530** | **13.9** | **20,710,730** | **13.9** | **25,425,559** | **14.5** |
| Selling and marketing expenses | (5,231,540) | (4.6) | (7,993,072) | (4.6) | (10,378,073) | (1,490,717) | (5.0) | (6,677,015) | (4.5) | (9,449,131) | (5.4) |
| Administrative expenses | (1,216,110) | (1.1) | (12,099,078) | (6.9) | (3,103,901) | (445,847) | (1.5) | (2,199,295) | (1.5) | (2,470,674) | (1.4) |
| Research and development expenses | (3,151,401) | (2.7) | (5,776,826) | (3.3) | (7,492,554) | (1,076,238) | (3.6) | (5,239,839) | (3.5) | (6,150,520) | (3.5) |
| Fair value changes on investments measured at fair value through profit or loss | 6,371,098 | 5.6 | 4,430,359 | 2.5 | 3,813,012 | 547,705 | 1.9 | 1,994,595 | 1.4 | 6,131,958 | 3.5 |
| Share of (losses)/ gains of investments accounted for using the equity method | (231,496) | (0.2) | (614,920) | (0.4) | (671,822) | (96,501) | (0.3) | (398,032) | (0.3) | 1,012,687 | 0.6 |
| Other income | 448,671 | 0.4 | 844,789 | 0.5 | 1,265,921 | 181,838 | 0.6 | 914,979 | 0.6 | 396,069 | 0.2 |
| Other gains/(losses), net | 72,040 | 0.1 | 213,281 | 0.1 | (226,399) | (32,520) | (0.1) | (43,060) | (0.0) | (463,114) | (0.3) |
| **Operating profit** | **12,215,467** | **10.7** | **1,196,472** | **0.7** | **11,760,217** | **1,689,250** | **5.7** | **9,063,063** | **6.1** | **14,432,834** | **8.2** |
| Finance income/ (expenses), net | 26,784 | 0.0 | 216,373 | 0.1 | 402,429 | 57,805 | 0.2 | 383,243 | 0.2 | (1,660,268) | (0.9) |
| Fair value changes of convertible redeemable preferred shares | (54,071,603) | (47.2) | 12,514,279 | 7.2 | – | – | – | – | – | – | – |
| **(Loss)/profit before income tax** | **(41,829,352)** | **(36.5)** | **13,927,124** | **8.0** | **12,162,646** | **1,747,055** | **5.9** | **9,446,306** | **6.3** | **12,772,566** | **7.3** |
| Income tax expenses | (2,059,763) | (1.8) | (449,377) | (0.3) | (2,059,696) | (295,857) | (1.0) | (1,779,575) | (1.2) | (1,254,851) | (0.7) |
| **(Loss)/profit for the year/period** | **(43,889,115)** | **(38.3)** | **13,477,747** | **7.7** | **10,102,950** | **1,451,198** | **4.9** | **7,666,731** | **5.1** | **11,517,715** | **6.6** |
| **Non-IFRS Measure: Adjusted net profit (unaudited)[1]** | **5,361,876** | **4.7** | **8,554,548** | **4.9** | **11,532,296** | **1,656,511** | **5.6** | **9,187,890** | **6.2** | **9,801,972** | **5.6** |

Note:

(1) We define Adjusted Net Profit as profit for the period, as adjusted by adding back (i) fair value changes of convertible redeemable preferred shares, (ii) share-based compensation, (iii) net fair value changes on investments, and (iv) amortization of intangible assets resulting from acquisitions, (v) changes of value of financial liabilities to fund investors, and (vi) income tax effects of Non-IFRS adjustments. See "– Non-IFRS Measure: Adjusted Net Profit" for details.

## DESCRIPTION OF MAJOR COMPONENTS OF OUR RESULTS OF OPERATIONS

### Revenue

We generate revenues from four business segments: smartphones, IoT and lifestyle products, internet services and others. Our revenues from smartphones segment are derived from the sale of smartphones. Our revenues from the IoT and lifestyle products segment comprise revenues from sales of (i) our other in-house products, such as laptops, smart TVs, AI speakers, smart routers, smart watches, smart refrigerators, smart washing machines and smart air conditioners, and (ii) our ecosystem products, including certain IoT and other smart hardware products, as well as certain lifestyle products. Our revenues from internet services segment are derived from advertising services and internet value-added services. Revenues from other segment are primarily derived from repair services for our hardware products and sales of materials.

The following table sets forth segment revenue both as an absolute amount and as a percentage of total revenues for the periods indicated:

| | For the year ended December 31, | | | | | | | For the nine months ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2017 | | 2018 | | 2019 | | | 2019 | | 2020 | |
| | RMB | % | RMB | % | RMB | US$ | % | RMB | % | RMB | % |
| | | | | | | | | (Unaudited) | | (Unaudited) | |
| | (in millions, except percentages) | | | | | | | | | | |
| Smartphones | 80,563.6 | 70.3 | 113,800.4 | 65.1 | 122,094.9 | 17,537.8 | 59.3 | 91,298.1 | 61.1 | 109,556.4 | 62.5 |
| IoT and lifestyle products | 23,447.8 | 20.5 | 43,816.9 | 25.1 | 62,088.0 | 8,918.4 | 30.2 | 42,594.0 | 28.5 | 46,356.1 | 26.4 |
| Internet services | 9,896.4 | 8.6 | 15,955.6 | 9.1 | 19,841.6 | 2,850.1 | 9.6 | 14,146.5 | 9.5 | 17,580.2 | 10.0 |
| Others | 716.9 | 0.6 | 1,342.5 | 0.7 | 1,814.2 | 260.6 | 0.9 | 1,330.4 | 0.9 | 1,910.0 | 1.1 |
| **Total** | **114,624.7** | **100.0** | **174,915.4** | **100.0** | **205,838.7** | **29,566.9** | **100.0** | **149,369.0** | **100.0** | **175,402.7** | **100.0** |

Geographically, we generated 72.0%, 60.0%, 55.7% and 49.5% of our revenues in mainland China in 2017, 2018, 2019 and for the nine months ended September 30, 2020. The following table sets forth revenues from mainland China and the rest of the world both as an absolute amount and as a percentage of total revenues for the periods indicated:

| | For the year ended December 31, | | | | | | | For the nine months ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2017 | | 2018 | | 2019 | | | 2019 | | 2020 | |
| | RMB | % | RMB | % | RMB | US$ | % | RMB | % | RMB | % |
| | | | | | | | | (Unaudited) | | (Unaudited) | |
| | (in millions, except percentages) | | | | | | | | | | |
| Mainland China | 82,543.5 | 72.0 | 104,944.8 | 60.0 | 114,608.6 | 16,462.5 | 55.7 | 84,580.5 | 56.6 | 86,773.1 | 49.5 |
| Rest of the world | 32,081.2 | 28.0 | 69,970.6 | 40.0 | 91,230.1 | 13,104.4 | 44.3 | 64,788.5 | 43.4 | 88,629.6 | 50.5 |
| **Total** | **114,624.7** | **100.0** | **174,915.4** | **100.0** | **205,838.7** | **29,566.9** | **100.0** | **149,369.0** | **100.0** | **175,402.7** | **100.0** |

### *Smartphones*

We sell our smartphones through our new retail channels directly to end users and through our online and offline distribution partners. We strive to offer our smartphones at price points that are accessible to the widest user base. The following table sets forth the average selling prices, the number of smartphones sold, and the total revenue from smartphone sales for the periods indicated.

| | For the year ended December 31, | | | For the nine months ended September 30, | |
|---|---|---|---|---|---|
| | 2017 | 2018 | 2019 | 2019 | 2020 |
| Average selling price (RMB)[(1)] | 881.3 | 959.1 | 979.9 | 992.2 | 1,052.3 |
| Number of smartphones sold (millions) | 91.4 | 118.7 | 124.6 | 92.0 | 104.1 |
| **Total revenues from smartphones segment (RMB millions)** | **80,563.6** | **113,800.4** | **122,094.9** | **91,298.1** | **109,556.4** |

Note:

(1) Averaging selling price equals our total revenue from smartphones segment divided by the total number of smartphones sold.

### *IoT and Lifestyle Products*

We have significantly expanded our product categories in recent years and systematically introduced a series of popular products. Our core in-house products (excluding smartphones) include laptops, smart TVs, AI speakers, smart routers, smart watches, smart refrigerators, smart washing machines and smart air conditioners. We also collaborate with our ecosystem partners to design and develop a wide range of smart home, health and fitness, travel, audio, kids and other IoT products, as well as certain lifestyle products, the sales of which have driven the growth of our user base. Revenues from the IoT and lifestyle products segment increased by 41.7% from 2018 to 2019, compared to an increase of 86.9% from 2017 to 2018.

***Internet Services***

The growth of our internet services revenues ultimately depends on the size of our user base and the level of user engagement and spending. MAU of our MIUI operating system increased by 41.7% from 170.8 million in December 2017 to 242.1 million in December 2018 and by 27.9% to 309.6 million in December 2019. In September 2020, the MAU of MIUI increased by 26.3% year-over-year to 368.2 million.

We derive our internet services revenues from advertising and internet value-added services. We generate advertising revenue primarily by offering advertisements through our online distribution channels, which include our mobile apps and smart TVs. For online games operations, we generate revenue from sales of virtual currency for purchase of virtual items that can be used in the games we operate, which is subject to the revenue-sharing arrangements with third-party game developers. Our other sources of internet value-added service revenues are mainly from fintech business, paid subscription by users of premium entertainment content (such as online videos) and the Youpin e-commerce platform.

***Others***

Revenues from other segment are primarily derived from repair services for our hardware products and sale of materials.

**Cost of Sales**

Our cost of sales for smartphones segment and IoT and lifestyle products segment primarily consist of (i) procurement cost of raw materials and components for our in-house products, (ii) assembly cost charged by our outsourcing partners for our in-house products, (iii) royalty fees for certain technologies embedded in our in-house products, (iv) costs, in the forms of production costs and profit-sharing, paid to our partners for procuring ecosystem products, (v) warranty expenses, and (vi) provision for impairment of inventories. Our cost of sales for internet services segment primarily consist of (i) bandwidth, server custody and cloud service related costs, and (ii) content fees to game developers and video providers. Cost of sales for others segment primarily consists of hardware repair costs and costs from sale of materials.

The following table sets forth our cost of sales by segment and as a percentage of total revenues for the periods indicated:

| | For the year ended December 31, | | | | | | | For the nine months ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2017 | | 2018 | | 2019 | | | 2019 | | 2020 | |
| | RMB | % | RMB | % | RMB | US$ | % | RMB | % | RMB | % |
| | | | | | | | | (Unaudited) | | (Unaudited) | |
| | (in millions, except percentages) | | | | | | | | | | |
| Smartphones | 73,462.3 | 64.1 | 106,757.1 | 61.0 | 113,335.5 | 16,279.6 | 55.1 | 84,930.3 | 56.9 | 100,824.0 | 57.5 |
| IoT and lifestyle products | 21,497.0 | 18.8 | 39,306.1 | 22.5 | 55,134.3 | 7,919.5 | 26.8 | 37,475.1 | 25.1 | 40,296.7 | 23.0 |
| Internet services | 3,935.6 | 3.4 | 5,683.9 | 3.2 | 6,998.1 | 1,005.2 | 3.4 | 4,929.7 | 3.3 | 7,160.0 | 4.1 |
| Others | 575.6 | 0.5 | 976.4 | 0.6 | 1,816.7 | 261.1 | 0.8 | 1,323.1 | 0.8 | 1,696.5 | 1.0 |
| **Total** | **99,470.5** | **86.8** | **152,723.5** | **87.3** | **177,284.6** | **25,465.4** | **86.1** | **128,658.2** | **86.1** | **149,977.2** | **85.6** |

The following table sets forth a breakdown of our cost of sales for the periods indicated:

| | For the year ended December 31, | | | | For the nine months ended September 30, | |
|---|---|---|---|---|---|---|
| | 2017 | 2018 | 2019 | | 2019 | 2020 |
| | RMB | RMB | RMB | US$ | RMB | RMB |
| | | | | | (Unaudited) | (Unaudited) |
| | (in millions) | | | | | |
| Cost of inventories sold | 89,468.5 | 138,237.7 | 157,935.8 | 22,686.1 | 114,275.0 | 132,383.3 |
| Royalty fees | 3,447.5 | 4,263.4 | 5,042.1 | 724.3 | 3,633.6 | 4,798.3 |
| Warranty expenses | 1,828.6 | 1,068.3 | 2,641.8 | 379.5 | 2,080.2 | 2,385.7 |
| Content fees to game developers and video providers | 1,383.6 | 1,629.1 | 1,754.6 | 252.0 | 1,226.8 | 1,815.1 |
| Cloud service, bandwidth and server custody fees | 929.9 | 1,725.2 | 1,724.1 | 247.7 | 1,318.5 | 1,467.7 |
| Provision for impairment of inventories | 652.6 | 3,006.5 | 3,859.7 | 554.4 | 3,112.1 | 2,528.2 |
| Others | 1,759.8 | 2,793.3 | 4,326.5 | 621.4 | 3,012.0 | 4,598.9 |
| **Total** | **99,470.5** | **152,723.5** | **177,284.6** | **25,465.4** | **128,658.2** | **149,977.2** |

### Gross Profit

The following table sets forth our gross profit in absolute amounts and as a percentage of revenues, or gross margins, for the periods indicated:

| | For the year ended December 31, | | | | | | | For the nine months ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2017 | | 2018 | | 2019 | | | 2019 | | 2020 | |
| | RMB | % | RMB | % | RMB | US$ | % | RMB | % | RMB | % |
| | | | | | | | | (Unaudited) | | (Unaudited) | |
| | (in millions, except percentages) | | | | | | | | | | |
| Gross profit | 15,154.2 | 13.2 | 22,191.9 | 12.7 | 28,554.1 | 4,101.5 | 13.9 | 20,710.7 | 13.9 | 25,425.6 | 14.5 |

The following table sets forth our gross profit and gross margin by segment for the periods indicated:

| | For the year ended December 31, | | | | | | | For the nine months ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2017 | | 2018 | | 2019 | | | 2019 | | 2020 | |
| | RMB | % | RMB | % | RMB | US$ | % | RMB | % | RMB | % |
| | | | | | | | | (Unaudited) | | (Unaudited) | |
| | (in millions, except percentages) | | | | | | | | | | |
| Smartphones | 7,101.3 | 8.8 | 7,043.3 | 6.2 | 8,759.4 | 1,258.2 | 7.2 | 6,367.8 | 7.0 | 8,732.4 | 8.0 |
| IoT and lifestyle products | 1,950.9 | 8.3 | 4,510.8 | 10.3 | 6,953.7 | 998.8 | 11.2 | 5,118.9 | 12.0 | 6,059.4 | 13.1 |
| Internet services | 5,960.8 | 60.2 | 10,271.7 | 64.4 | 12,843.5 | 1,844.9 | 64.7 | 9,216.8 | 65.2 | 10,420.2 | 59.3 |
| Others | 141.2 | 19.7 | 366.1 | 27.3 | (2.5) | (0.4) | (0.1) | 7.2 | 0.5 | 213.6 | 11.2 |
| **Total** | **15,154.2** | **13.2** | **22,191.9** | **12.7** | **28,554.1** | **4,101.5** | **13.9** | **20,710.7** | **13.9** | **25,425.6** | **14.5** |

### Selling and Marketing Expenses

Our selling and marketing expenses primarily consist of (i) offline promotional and advertising expenses, (ii) online promotional and advertising expenses, (iii) employee benefit expenses (including salaries, bonuses and share-based compensation) relating to selling and marketing personnel, and (iv) freight and transportation expenses.

### Administrative Expenses

Our administrative expenses primarily consist of (i) employee benefit expenses (including salaries, bonuses and share-based compensation) relating to administrative personnel, (ii) certain third-party consulting and professional service fees, (iii) depreciation and amortization expenses allocated to administrative expenses, and (iv) rent, utility and other office expenses allocated to administrative expenses.

### Research and Development Expenses

Our research and development expenses primarily comprise (i) employee benefit expenses (including salaries, bonuses and share-based compensation) relating to research and development personnel, (ii) sample testing, data service and certification expenses, (iii) certain third-party consulting and professional service fees and (iv) rent, utility and other office expenses allocated to research and development expenses.

### Fair Value Changes on Investments Measured at Fair Value through Profit or Loss

We recognize the fair value changes on the following types of investments in profits or losses: (i) short-term investments measured at fair value through profit or loss, which are RMB-denominated wealth management products whose returns are not guaranteed, (ii) equity investments other than those accounted for using the equity method, and (iii) investments in convertible redeemable preferred shares or ordinary shares with preferential rights.

### Share of (Losses)/Gains of Investments Accounted for Using the Equity Method

We recorded share of (losses)/gains from investments primarily because we had accounted for several investee companies that had (losses)/gains using the equity method.

### Other Income

Our other income primarily includes (i) government grants, (ii) value-added tax and other tax refunds, (iii) dividend income and (iv) income from wealth management products.

### Other Gains/(Losses), Net

Our other gains/(losses), net primarily include (i) gains on disposal of investments, (ii) remeasurement of loss of significant influence in an associate, (iii) foreign exchanges losses, net, (iv) impairment on investments accounted for using the equity method, and (v) costs resulting from our financial guarantee. Gains on disposal of investments primarily arise from disposal of our equity investments in our investee companies. Foreign exchanges losses, net are incurred primarily due to fluctuations in exchange rates between RMB and U.S. dollars.

### Operating Profit

The following table sets forth our operating profit in absolute amounts and as a percentage of our revenues, or operating margin, for the periods indicated:

| | For the year ended December 31, | | | | | | | For the nine months ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2017 | | 2018 | | 2019 | | | 2019 | | 2020 | |
| | RMB | % | RMB | % | RMB | US$ | % | RMB | % | RMB | % |
| | | | | | | | | (Unaudited) | | (Unaudited) | |
| | (in millions, except percentages) | | | | | | | | | | |
| Operating Profit | 12,215.5 | 10.7 | 1,196.5 | 0.7 | 11,760.2 | 1,689.3 | 5.7 | 9,063.1 | 6.1 | 14,432.8 | 8.2 |

**Finance Income/(Expenses), Net**

Finance income/(expenses), net represents finance income net against finance costs. Finance income consists of interest income from bank deposits, including bank balance and term deposits, whereas finance cost consists of interest expenses.

**Fair Value Changes of Convertible Redeemable Preferred Shares**

Fair value changes of convertible redeemable preferred shares represent changes in fair value of the preferred shares issued by us prior to our initial public offering. Please refer to Note 35 to the consolidated financial statements included in this Offering Circular for details. We designate preferred shares as financial liabilities at fair value. Any changes in the fair value of the preferred shares are recorded as "fair value changes of convertible redeemable preferred shares" in the consolidated income statements.

**Taxation**

Income tax expenses were RMB2.1 billion, RMB0.4 billion and RMB2.1 billion for 2017, 2018 and 2019, respectively. Income tax expenses were RMB1.3 billion for the nine months ended September 30, 2020. We are subject to various rates of income tax under different jurisdictions. The following summarizes the major factors affecting our applicable tax rates in the Cayman Islands, the BVI, Hong Kong, mainland China and India.

*Cayman Islands and the British Virgin Islands*

The following is a discussion of certain Cayman Islands income tax consequences of an investment in the Bonds. The discussion is a general summary of present law, which is subject to prospective and retroactive change. It is not intended as tax advice, does not consider any investor's particular circumstances, and does not consider tax consequences other than those arising under Cayman Islands law.

Under existing Cayman Islands law, payments of interest and principal on the Bonds will not be subject to taxation in the Cayman Islands and no withholding will be required on the payment of interest and principal or a dividend or capital to any holder of the Bonds, nor will gains derived from the disposal of the Bonds be subject to Cayman Islands income or corporation tax. The Cayman Islands currently have no income, corporation or capital gains tax and no estate duty, inheritance tax or gift tax. No stamp duty is payable in respect of the issue of the Bonds. An instrument of transfer in respect of a Bond is stampable if executed in or brought into the Cayman Islands.

Under existing British Virgin Islands law, payments of interest and principal on the Bonds will not be subject to taxation in the British Virgin Islands and no withholding will be required on the payment of interest and principal to any holder of the Bonds nor will gains derived from the disposal of the Bonds be subject to British Virgin Islands income or corporation tax, provided that the payments are made to persons who are not resident in the British Virgin Islands.

No estate, inheritance, succession or gift tax, rate, duty, levy or other charge is payable by persons who are not resident in the British Virgin Islands with respect to the Bonds.

There are currently no withholding taxes or exchange control regulations in the British Virgin Islands applicable to the Company. If neither the Company nor any subsidiary holds an interest in real estate in the British Virgin Islands, no stamp duty is payable in respect of the issue of the Bonds or on an instrument of transfer in respect of the Bonds.

*Hong Kong*

Hong Kong profits tax was 16.5% up to April 1, 2018 when the two-tiered profits tax regime took effect, under which the tax rate is 8.25% for assessable profits in the first HK$2 million and 16.5% for any assessable profits in excess.

*Mainland China*

Our income tax provision in respect of our operations in mainland China was calculated at tax rate of 25% on the assessable profits, based on the existing legislation, interpretations and practices in respect thereof.

Certain subsidiaries are entitled to preferential tax rates ranging from 10% to 15%. Main subsidiaries with preferential EIT rates are as follows: Beijing Xiaomi Mobile Software Co., Ltd. ("**Xiaomi Mobile**") was qualified as a "Key Software Enterprise" in the third quarter of 2018, hence it enjoys a preferential income tax rate of 10% retroactively from January 1, 2017. Accordingly, Xiaomi Mobile was entitled to tax refund for the income tax paid in 2017 and such tax refund was received by Xiaomi Mobile from local tax bureau in December 2018. Xiaomi Mobile enjoys the preferential EIT rate of 10% for the years ended December 31, 2019 and 2018. Beijing Xiaomi Digital Technology Co., Ltd. was qualified as a "High and New Technology Enterprise" in November 2018, hence it enjoys a preferential income tax rate of 15% for three years from 2018 to 2020.

According to the relevant laws and regulations promulgated by the State Council of the People's Republic of China that was effective from 2008 onwards, enterprises engaging in research and development activities were entitled to claim 150% of their research and development expenses so incurred as tax deductible expenses when determining their assessable profits for that year ("**Super Deduction**"). The State Taxation Administration of The People's Republic of China announced in September 2018 that enterprises engaging in research and development activities would entitle to claim 175% of their research and development expenses as Super Deduction from January 1, 2018 to December 31, 2020. The Group has made its best estimate for the Super Deduction to be claimed for the Group's entities in ascertaining their assessable profits during the year.

**Net (Loss)/Profit**

The following table sets forth our net (loss)/profit in absolute amounts and as a percentage of our revenues, or net margin, for the periods indicated:

| | For the year ended December 31, | | | | | | | For the nine months ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2017 | | 2018 | | 2019 | | | 2019 | | 2020 | |
| | RMB | % | RMB | % | RMB | US$ | % | RMB | % | RMB | % |
| | | | | | | | | (Unaudited) | | (Unaudited) | |
| | (in millions, except percentages) | | | | | | | | | | |
| Net (Loss)/profit.............. | (43,889.1) | (38.3) | 13,477.7 | 7.7 | 10,103.0 | 1,451.2 | 4.9 | 7,666.7 | 5.1 | 11,517.7 | 6.6 |

Our Board has resolved that for the year ending December 31, 2018 and each year thereafter, we will limit the net margin after tax for our entire hardware business (including smartphone, IoT and lifestyle products), or the Margin, to a maximum of 5%. The Margin is calculated based on the following formula, or the Formula:

- the Margin = the net profits after tax relating to the sales of our entire hardware business based on our management accounts for a financial year, or the Net Profit / the revenue of the entire hardware business for the same financial year; and

- the Net Profit = (revenue from the entire hardware business – cost of goods sold relating to the entire hardware business – the selling and marketing expenses, research and development expenses and administrative expenses relating to the sales of the entire hardware business) x (1 – the Group's effective tax rate for the preceding financial year).

The expenses cited in the Formula exclude any expenses related to share-based compensation. If the actual Margin achieved for any financial year exceeds 5% calculated based on the Formula, we will distribute the amount of net profit earned exceeding 5% to our customers in general by way of reasonable means as our Board may determine from time to time.

In each of 2018 and 2019, our hardware business (including smartphones, IoT and lifestyle products) was profitable with a net margin after tax of less than 1.0%, fulfilling our pledge.

## NON-IFRS MEASURE: ADJUSTED NET PROFIT

To supplement our consolidated results which are prepared and presented in accordance with the IFRS, we utilize non-IFRS adjusted net profit, or Adjusted Net Profit, as an additional financial measure. We define Adjusted Net Profit as profit for the period, as adjusted by adding back (i) fair value changes of convertible redeemable preferred shares, (ii) share-based compensation, (iii) net fair value changes on investments, and (iv) amortization of intangible assets resulting from acquisitions, (v) changes of value of financial liabilities to fund investors, and (vi) income tax effects of Non-IFRS adjustments.

Adjusted Net Profit is not required by, or presented in accordance with, IFRS. We believe that the presentation of non-IFRS measures when shown in conjunction with the corresponding IFRS measures provides useful information to investors and management regarding financial and business trends in relation to our financial condition and results of operations, by eliminating any potential impact of items that our management does not consider to be indicative of our operating performance such as certain non-cash items and the impact of certain investment transactions. We also believe that the non-IFRS measures are appropriate for evaluating the Group's operating performance. However, the use of this particular non-IFRS measure has limitations as an analytical tool, and you should not consider it in isolation from, or as a substitute for analysis of, our results of operations or financial conditions as reported under IFRS. In addition, this non-IFRS financial measure may be defined differently from similar terms used by other companies and therefore may not be comparable to similar measures used by other companies.

The following tables set forth the reconciliations of our non-IFRS financial measure for the years ended December 31, 2017, 2018 and 2019 and the nine months ended September 30, 2020 to the nearest measures prepared in accordance with IFRS:

| | Nine Months Ended September 30, 2020 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | Adjustments | | | | | | |
| | As reported | Fair value changes of convertible redeemable preferred shares | Share-based compensation | Net fair value changes on investments[(1)] | Amortization of intangible assets resulting from acquisitions[(2)] | Changes of value of financial liabilities to fund investors[(3)] | Income tax effects[(4)] | Non-IFRS |
| | (RMB in thousands, unless specified) | | | | | | | |
| Profit for the period | 11,517,715 | – | 1,667,695 | (5,079,388) | 237 | 2,027,893 | (332,180) | 9,801,972 |
| Net margin | 6.6% | | | | | | | 5.6% |

| | Year Ended December 31, 2019 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | Adjustments | | | | | | |
| | As reported | Fair value changes of convertible redeemable preferred shares | Share-based compensation | Net fair value changes on investments[(1)] | Amortization of intangible assets resulting from acquisitions[(2)] | Changes of value of financial liabilities to fund investors[(3)] | Income tax effects[(4)] | Non-IFRS |
| | (RMB in thousands, unless specified) | | | | | | | |
| Profit for the year | 10,102,950 | – | 2,201,722 | (888,284) | 1,704 | 250,706 | (136,502) | 11,532,296 |
| Net margin | 4.9% | | | | | | | 5.6% |

| | Year Ended December 31, 2018 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | Adjustments | | | | | | |
| | As reported | Fair value changes of convertible redeemable preferred shares | Share-based compensation | Net fair value changes on investments(1) | Amortization of intangible assets resulting from acquisitions(2) | Changes of value of financial liabilities to fund investors(3) | Income tax effects(4) | Non-IFRS |
| | (RMB in thousands, unless specified) | | | | | | | |
| Profit for the year | 13,477,747 | (12,514,279) | 12,380,668 | (4,524,425) | 6,207 | 42,504 | (313,874) | 8,554,548 |
| Net margin | 7.7% | | | | | | | 4.9% |

| | Year Ended December 31, 2017 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | Adjustments | | | | | | |
| | As reported | Fair value changes of convertible redeemable preferred shares | Share-based compensation | Net fair value changes on investments(1) | Amortization of intangible assets resulting from acquisitions(2) | Changes of value of financial liabilities to fund investors(3) | Income tax effects(4) | Non-IFRS |
| | (RMB in thousands, unless specified) | | | | | | | |
| (Loss)/profit for the year | (43,889,115) | 54,071,603 | 909,155 | (6,350,022) | 3,179 | – | 617,076 | 5,361,876 |
| Net margin | -38.3% | | | | | | | 4.7% |

Notes:

(1) Includes fair value changes on equity investments and preferred shares investments deducting the cumulative fair value changes for investments (including the financial assets measured at fair value through profit or loss, or FAFVPL, and the investments using the equity method transferred from FAFVPL) disposed in the current period, the impairment provision for investments, re-measurement of loss of significant influence in an associate, re-measurement of investments transferring from FAFVPL to investments using the equity method, but excludes the equity pick up of share of (losses)/gains of investments accounted for using the equity method.

(2) Represents amortization of intangible assets resulting from acquisitions.

(3) Represent the change of value of the financial liabilities payable to the fund investors, as a result of the change of fair value of the fund.

(4) Income tax effects of Non-IFRS adjustments.

## PERIOD-TO-PERIOD COMPARISON OF RESULTS OF OPERATIONS

### Three months ended September 30, 2020 Compared to three months ended September 30, 2019

#### *Revenue*

Revenue increased on a year-over-year basis by 34.5% from RMB53.7 billion in the third quarter of 2019 to RMB72.2 billion in the third quarter of 2020.

*Smartphones*

Revenue from our smartphones segment increased by 47.5% from RMB32.3 billion in the third quarter of 2019 to RMB47.6 billion in the third quarter of 2020. Our smartphone shipments increased 45.3% from 32.1 million in the third quarter of 2019 to 46.6 million in the third quarter of 2020, mainly driven by the strong growth momentum in mainland China and overseas markets. The ASP of our smartphones was RMB1,022.3 per unit in the third quarter of 2020, compared with RMB1,006.5 per unit in the third quarter of 2019. The increase in ASP was primarily due to the increase in sales of our mid- to high-end smartphone models in the third quarter of 2020. The ASP in mainland China increased by 14.7% year-over-year, while the ASP in overseas markets decreased slightly by 1.5% due to our product launch schedule, with our entry-level smartphone Redmi 9 series receiving widespread popularity.

*IoT and lifestyle products*

Revenue from our IoT and lifestyle products segment increased by 16.1% from RMB15.6 billion in the third quarter of 2019 to RMB18.1 billion in the third quarter of 2020, primarily due to the growth in demand for certain IoT products, such as robot vacuum cleaners, smart TVs and electric scooters. Revenue from smart TVs and laptops increased by 2.6% from RMB5.8 billion in the third quarter of 2019 to RMB5.9 billion in the third quarter of 2020.

*Internet services*

Revenue from our internet services segment increased by 8.7% from RMB5.3 billion in the third quarter of 2019 to RMB5.8 billion in the third quarter of 2020, driven by the growth in our advertising and other value-added service businesses. Our MIUI MAU increased by 26.3% from 291.6 million in September 2019 to 368.2 million in September 2020.

*Others*

Other revenue increased by 39.9% from RMB477.3 million in the third quarter of 2019 to RMB667.8 million in the third quarter of 2020, primarily due to the increase in revenue from the installation services provided for certain IoT products.

***Cost of Sales***

Our cost of sales increased by 36.5% from RMB45.4 billion in the third quarter of 2019 to RMB62.0 billion in the third quarter of 2020.

*Smartphones*

Cost of sales related to our smartphones segment increased by 48.5% from RMB29.4 billion in the third quarter of 2019 to RMB43.6 billion in the third quarter of 2020, primarily due to the increased sales of our smartphones.

*IoT and lifestyle products*

Cost of sales related to our IoT and lifestyle products segment increased by 14.2% from RMB13.6 billion in the third quarter of 2019 to RMB15.5 billion in the third quarter of 2020, primarily due to the increased sales of our IoT and lifestyle products.

*Internet services*

Cost of sales related to our internet services segment increased by 16.1% from RMB2.0 billion in the third quarter of 2019 to RMB2.3 billion in the third quarter of 2020, primarily due to the increased cost of our advertising and other value-added service businesses.

*Others*

Cost of sales related to our others segment increased by 18.1% from RMB474.1 million in the third quarter of 2019 to RMB560.1 million in the third quarter of 2020, primarily due to the increase in cost from the installation services provided for certain IoT products.

***Gross Profit and Margin***

As a result of the foregoing, our gross profit increased by 23.4% from RMB8.2 billion in the third quarter of 2019 to RMB10.2 billion in the third quarter of 2020. The gross profit margin of our smartphones segment decreased from 9.0% in the third quarter of 2019 to 8.4% in the third quarter of 2020, mainly due to enhanced promotional efforts. The gross profit margin of our IoT and lifestyle products segment increased from 12.8% in the third quarter of 2019 to 14.2% in the third quarter of 2020, mainly due to the strong growth in our IoT products with higher gross profit margin and the improvement in gross profit margin of smart TVs. The gross profit margin of our internet services segment decreased from 62.9% in the third quarter of 2019 to 60.4% in the third quarter of 2020, mainly due to the decline of gross profit margin of our fintech and gaming businesses. As a result of the foregoing, together with the stronger growth of our smartphone business, our gross profit margin decreased from 15.3% in the third quarter of 2019 to 14.1% in the third quarter of 2020.

***Selling and Marketing Expenses***

Our selling and marketing expenses increased by 41.9% from RMB2.5 billion in the third quarter of 2019 to RMB3.6 billion in the third quarter of 2020, primarily due to the increase in promotion and advertising expenses, as well as packaging and transportation expenses. Promotion and advertising expenses increased by 52.4% from RMB849.9 million in the third quarter of 2019 to RMB1,295.2 million in the third quarter of 2020, primarily due to our marketing efforts for our premium smartphone models to increase brand awareness in overseas markets. Packaging and transportation expenses increased by 55.9% from RMB626.4 million in the third quarter of 2019 to RMB976.8 million in the third quarter of 2020, primarily due to the expansion of our overseas business.

***Administrative Expenses***

Our administrative expenses increased by 1.1% from RMB843.8 million in the third quarter of 2019 to RMB852.7 million in the third quarter of 2020.

***Research and Development Expenses***

Our research and development expenses increased by 14.2% from RMB2.0 billion in the third quarter of 2019 to RMB2.3 billion in the third quarter of 2020, primarily due to the increase in compensation for research and development personnel.

***Fair Value Changes on Investments Measured at Fair Value Through Profit or Loss***

Our fair value changes on investments measured at fair value through profit or loss increased from a gain of RMB32.5 million in the third quarter of 2019 to a gain of RMB3,417.9 million in the third quarter of 2020, primarily due to the increase in fair value gains of equity and preferred share investments in the third quarter of 2020.

***Share of Losses of Investments Accounted for Using the Equity Method***

Our share of losses of investments accounted for using the equity method decreased from net losses of RMB240.6 million in the third quarter of 2019 to net losses of RMB10.7 million in the third quarter of 2020, primarily due to the decrease in share of loss of iQIYI, Inc. (Nasdaq: IQ) in the third quarter of 2020.

***Other Income***

Our other income decreased by 68.9% from RMB448.4 million in the third quarter of 2019 to RMB139.3 million in the third quarter of 2020, due to lower dividend income received from our investee companies.

***Other (Losses)/Gains, Net***

Our other net (losses)/gains changed from net gains of RMB49.9 million in the third quarter of 2019 to net losses of RMB241.0 million in the third quarter of 2020. This was mainly due to the recognition of foreign exchange losses for the third quarter of 2020, compared to foreign exchange gains for the third quarter of 2019.

***Finance (Expenses)/Income, Net***

Our net finance (expenses)/income changed from net income of RMB182.1 million in the third quarter of 2019 to net expenses of RMB1,245.9 million in the third quarter of 2020, primarily due to the increase in changes of value of financial liabilities to fund investors.

***Income Tax Expenses***

Our income tax expenses decreased by 24.4% from RMB775.4 million in the third quarter of 2019 to RMB586.3 million in the third quarter of 2020, primarily due to the decrease of deferred tax expenses.

***Profit for the Period***

As a result of the foregoing, we had a profit of RMB2.5 billion and a profit of RMB4.9 billion in the third quarter of 2019 and the third quarter of 2020, respectively a year-over-year increase of 93.1%.

**Year Ended December 31, 2019 Compared to Year Ended December 31, 2018**

***Revenues***

Our revenue increased by 17.7% to RMB205.8 billion for the year ended December 31, 2019, compared to RMB174.9 billion for the year ended December 31, 2018. Our revenues in mainland China increased by 9.2% from RMB104.9 billion in 2018 to RMB114.6 billion in 2019, and our overseas revenues significantly increased by 30.4% from RMB70.0 billion in 2018 to RMB91.2 billion in 2019.

*Smartphones*

Revenue from our smartphones segment increased by 7.3% from RMB113.8 billion for the year ended December 31, 2018 to RMB122.1 billion for the year ended December 31, 2019, driven by growth in both sales volume and ASP. We sold 124.6 million smartphone units for the year ended December 31, 2019, compared to 118.7 million units for the year ended December 31, 2018. The ASP of our smartphones was RMB979.9 per unit for the year ended December 31, 2019, compared with RMB959.1 per unit for the year ended December 31, 2018. The increase in ASP was primarily due to the optimization of our product portfolio, shifting to higher ASP models in mainland China and some of overseas markets.

*IoT and lifestyle products*

Revenue from our IoT and lifestyle products segment increased by 41.7% from RMB43.8 billion for the year ended December 31, 2018 to RMB62.1 billion for the year ended December 31, 2019, primarily due to the strong growth in demand of our smart TVs, home appliances and other IoT products such as *Mi Band, Mi Electric Scooter* and *Mi Air Purifier*. Revenue from smart TVs and laptops increased by 33.1% from RMB18.2 billion for the year ended December 31, 2018 to RMB24.2 billion for the year ended December 31, 2019.

*Internet services*

Revenue from our internet services segment increased by 24.4% from RMB16.0 billion for the year ended December 31, 2018 to RMB19.8 billion for the year ended December 31, 2019. All of our major internet service businesses experienced solid revenue growth in 2019. Our MIUI MAU increased by 27.9% from 242.1 million in December 2018 to 309.6 million in December 2019.

*Others*

Other revenue increased by 35.1% from RMB1,342.5 million for the year ended December 31, 2018 to RMB1,814.2 million for the year ended December 31, 2019, primarily due to the increase in revenue from out-of-warranty services as a result of greater hardware sales as well as the increase in revenue from sale of materials.

***Cost of sales***

Our cost of sales increased by 16.1% from RMB152.7 billion for the year ended December 31, 2018 to RMB177.3 billion for the year ended December 31, 2019.

*Smartphones*

Cost of sales related to our smartphones segment increased by 6.2% from RMB106.8 billion for the year ended December 31, 2018 to RMB113.3 billion for the year ended December 31, 2019, mainly due to increased sales of our smartphones.

*IoT and lifestyle products*

Cost of sales related to our IoT and lifestyle products segment increased by 40.3% from RMB39.3 billion for the year ended December 31, 2018 to RMB55.1 billion for the year ended December 31, 2019, primarily due to the increased sales of our smart TVs and other IoT products.

*Internet services*

Cost of sales related to our internet services segment increased by 23.1% from RMB5.7 billion for the year ended December 31, 2018 to RMB7.0 billion for the year ended December 31, 2019, primarily due to the increase in sales of advertising and other internet value-added services.

*Others*

Cost of sales in our others segment increased by 86.1% from RMB976.4 million for the year ended December 31, 2018 to RMB1,816.7 million for the year ended December 31, 2019, primarily due to the increased costs of providing out-of-warranty services and the increased costs from sale of materials.

***Gross profit and gross margin***

As a result of the foregoing, our gross profit increased by 28.7% from RMB22.2 billion for the year ended December 31, 2018 to RMB28.6 billion for the year ended December 31, 2019. The gross profit margin from our smartphones segment increased from 6.2% for the year ended December 31, 2018 to 7.2% for the year ended December 31, 2019. The increase in gross margin mainly reflected the improvement of our product mix and more prudent operations during the early transition period from 4G to 5G technology in mainland China.

The gross profit margin from our IoT and lifestyle products segment increased from 10.3% for the year ended December 31, 2018 to 11.2% for the year ended December 31, 2019, mainly due to the increased gross profit margin from our smart TVs and laptops business. The gross profit margin from our internet services segment was 64.7% for the year ended December 31, 2019, compared with 64.4% for the year ended December 31, 2018. As a result of the foregoing, our gross margin increased from 12.7% for the year ended December 31, 2018 to 13.9% for the year ended December 31, 2019.

***Selling and marketing expenses***

Our selling and marketing expenses increased by 29.8% from RMB8.0 billion for the year ended December 31, 2018 to RMB10.4 billion for the year ended December 31, 2019, primarily due to increases in promotion and advertising expenses and packaging and transportation expenses. Promotion and advertising expenses increased 34.9% from RMB2.5 billion for the year ended December 31, 2018 to RMB3.4 billion for the year ended December 31, 2019, primarily due to our elevated overseas marketing efforts in 2019. Packaging and transportation expenses increased by 36.7% from RMB1.9 billion for the year ended December 31, 2018 to RMB2.6 billion for the year ended December 31, 2019, primarily due to the strong growth in our overseas business.

*Administrative expenses*

Our administrative expenses decreased by 74.3% from RMB12.1 billion for the year ended December 31, 2018 to RMB3.1 billion for the year ended December 31, 2019, as the Company recognized a one-off share-based compensation expense in 2018. Excluding the one-off share-based compensation, our administrative expenses increased from RMB2.2 billion for the year ended December 31, 2018 to RMB3.1 billion for the year ended December 31, 2019, primarily due to the increase of administrative personnel as a result of the increased headcount to accommodate our business growth.

*Research and development expenses*

Our research and development expenses increased by 29.7% from RMB5.8 billion for the year ended December 31, 2018 to RMB7.5 billion for the year ended December 31, 2019, primarily due to the increase in compensation expenses relating to our research and development personnel and the expansion of our development projects.

*Fair value changes on investments measured at fair value through profit or loss*

Our fair value changes on investments measured at fair value through profit or loss decreased by 13.9% from a gain of RMB4.4 billion for the year ended December 31, 2018 to a gain of RMB3.8 billion for the year ended December 31, 2019, primarily due to changes in fair value of our equity and preferred share investments for the year ended December 31, 2019.

*Share of losses of investments accounted for using the equity method*

Our share of losses of investments accounted for using the equity method increased by 9.3% from RMB614.9 million for the year ended December 31, 2018 to RMB671.8 million for the year ended December 31, 2019, primarily due to the increase in share of loss of RMB733.2 million of iQIYI, Inc (Nasdaq: IQ), partially offset by the increase in share of gains of other investments.

*Other income*

Our other income increased by 49.9% from RMB844.8 million for the year ended December 31, 2018 to RMB1,265.9 million for the year ended December 31, 2019, primarily due to increase in dividend income received from our investee companies.

*Other gains/(losses), net*

Our other gains/(losses), net decreased by 206.2% from net gains of RMB213.3 million for the year ended December 31, 2018 to net losses of RMB226.4 million for the year ended December 31, 2019. This is due to the costs resulting from our financial guarantee.

*Finance income, net*

Our net finance income increased by 86.0% from RMB216.3 million for the year ended December 31, 2018 to RMB402.4 million for the year ended December 31, 2019, primarily due to the increase in our interest income.

*Fair value changes of convertible redeemable preferred shares*

Changes in the fair value of our convertible redeemable preferred shares were recorded as fair value changes of convertible redeemable preferred shares. We did not incur fair value changes of convertible redeemable preferred shares for the year ended December 31, 2019, compared to a gain of RMB12.5 billion for the year ended December 31, 2018. After the completion of our initial public offering, all of our convertible redeemable preferred shares were automatically converted to the Class B Shares and thus we no longer incurred fair value changes of convertible redeemable preferred shares after the fourth quarter of 2018.

*Income tax expenses*

Our income tax expenses increased from an income tax expense of RMB0.4 billion for the year ended December 31, 2018 to an income tax expense of RMB2.1 billion for the year ended December 31, 2019, primarily due 1) to an increase of profit in mainland China for the year ended December 31, 2019 compared to the year ended December 31, 2018 and 2) the decrease of deferred tax assets.

*Profit for the year*

As a result of the foregoing, we had a profit of RMB10.1 billion for the year ended December 31, 2019 compared with a profit of RMB13.5 billion for the year ended December 31, 2018.

**Year Ended December 31, 2018 Compared to Year Ended December 31, 2017**

*Revenues*

Our revenue increased by 52.6% to RMB174.9 billion for the year ended December 31, 2018, compared to RMB114.6 billion for the year ended December 31, 2017.

*Smartphones*

Revenue from our smartphones segment increased by 41.3% from RMB80.6 billion for the year ended December 31, 2017 to RMB113.8 billion for the year ended December 31, 2018, driven by growth in both sales volume and ASP. We sold 118.7 million smartphone units for the year ended December 31, 2018, compared to 91.4 million units for the year ended December 31, 2017. The ASP of our smartphones was RMB959.1 per unit for the year ended December 31, 2018, compared with RMB881.3 per unit for the year ended December 31, 2017.

*IoT and lifestyle products*

Revenue from our IoT and lifestyle products segment increased by 86.9% from RMB23.4 billion for the year ended December 31, 2017 to RMB43.8 billion for the year ended December 31, 2018, primarily due to the rapid growth in demand of our smart TVs and several sought-after ecosystem products such as *Mi Band, Mi Electric Scooter and Mi Robot Vacuum Cleaner*. Revenue from smart TVs and laptops, increased by 118.4% from RMB8.3 billion for the year ended December 31, 2017 to RMB18.2 billion for the year ended December 31, 2018.

*Internet services*

Revenue from our internet services segment increased by 61.2% from RMB9.9 billion for the year ended December 31, 2017 to RMB16.0 billion for the year ended December 31, 2018, primarily due to growth in advertising and other internet value-added services. Our MIUI MAU increased by 41.7% from 170.8 million in December 2017 to 242.1 million in December 2018.

*Others*

Other revenue increased by 87.3% from RMB716.9 million for the year ended December 31, 2017 to RMB1,342.5 million for the year ended December 31, 2018, primarily due to an increase in out-of-warranty service revenue in-line with our increase in hardware sales.

*Cost of sales*

Our cost of sales increased by 53.5% from RMB99.5 billion for the year ended December 31, 2017 to RMB152.7 billion for the year ended December 31, 2018.

*Smartphones*

Cost of sales related to our smartphones segment increased by 45.3% from RMB73.5 billion for the year ended December 31, 2017 to RMB106.8 billion for the year ended December 31, 2018, mainly due to increased sales of our smartphones and the appreciation of the United States dollar against the RMB and Indian Rupee.

We reassessed warranty provision in the fourth quarter of 2018. Through our relentless efforts over the past years, in particular, the work conducted by the newly established group level Quality Committee, the quality of our products has greatly improved. The actual repair costs within the warranty period incurred has been consistently reducing and was lower than the warranty provisioned for the year ended December 31, 2018. Therefore, we revisited the warranty provision percentage to better reflect the actual business performance while ensuring that the warranty provision to cover future claims on products under warranty is adequate. This has taken into account the new 18-month long warranty program for some smartphone models. The warranty provision remained stable at RMB1.7 billion as of December 31, 2018, compared to RMB1.7 billion as of December 31, 2017. The warranty expenses recognized in the year ended December 31, 2018 was RMB1.1 billion, compared to RMB1.8 billion in the year ended December 31, 2017. In order to return some of the gains from quality improvement to our users, we reflected these factors in the pricing of smartphones and provided discounts to our users on certain existing smartphone models. Such promotions resulted in additional inventory provision for unsold smartphones.

Furthermore, in anticipation of the separation of Redmi brand and new Xiaomi smartphone product launches in the first quarter of 2019, we increased the provision for impairment of inventories. The provision for impairment on our balance sheet was RMB1.9 billion as of December 31, 2018, compared to RMB0.7 billion as of December 31, 2017. Such additional provision provides us with pricing flexibility to promote existing smartphone models after the launch of new smartphones in 2019.

*IoT and lifestyle products*

Cost of sales in our IoT and lifestyle products segment increased by 82.8% from RMB21.5 billion for the year ended December 31, 2017 to RMB39.3 billion for the year ended December 31, 2018, primarily due to increased sales of smart TVs and other IoT products.

*Internet services*

Cost of sales related to our internet services segment increased by 44.4% from RMB3.9 billion for the year ended December 31, 2017 to RMB5.7 billion for the year ended December 31, 2018, primarily due to increased infrastructure service spending resulting from higher user traffic and engagement.

*Others*

Cost of sales in our others segment increased by 69.6% from RMB575.6 million for the year ended December 31, 2017 to RMB976.4 million for the year ended December 31, 2018, primarily due to increased out-of-warranty service costs.

***Gross profit and gross margin***

Because of the above mentioned, our gross profit increased by 46.4% from RMB15.2 billion for the year ended December 31, 2017 to RMB22.2 billion for the year ended December 31, 2018. The gross profit margin from our smartphones segment decreased from 8.8% for the year ended December 31, 2017 to 6.2% for the year ended December 31, 2018. In order to lay the groundwork to capture long term value, we selectively prioritized higher growth to capture market share in key products over higher gross margins.

The gross profit margin from our IoT and lifestyle products segment increased from 8.3% for the year ended December 31, 2017 to 10.3% for the year ended December 31, 2018, mainly due to the improvement of gross margin in our smart TVs. The gross profit margin from our internet services segment increased from 60.2% for the year ended December 31, 2017 to 64.4% for the year ended December 31, 2018, as the percentage of revenue from higher margin advertising business was larger. As a result of the foregoing, our gross margin decreased from 13.2% for the year ended December 31, 2017 to 12.7% for the year ended December 31, 2018.

***Selling and marketing expenses***

Our selling and marketing expenses increased by 52.8% from RMB5.2 billion for the year ended December 31, 2017 to RMB8.0 billion for the year ended December 31, 2018, primarily due to higher packaging and transportation expenses, the compensations for our sales and marketing personnel, and increase of advertising expenses. Packaging and transportation expenses increased by 97.9% from RMB1.0 billion for the year ended December 31, 2017 to RMB1.9 billion for the year ended December 31, 2018, primarily due to rapid growth in our overseas IoT business. Advertising expenses increased primarily due to our enhanced marketing efforts, such as advertising in relation to the World Cup and several high profile TV shows during the year ended December 31, 2018.

***Administrative expenses***

Our administrative expenses increased from RMB1.2 billion for the year ended December 31, 2017 to RMB12.1 billion for the year ended December 31, 2018, primarily due to a one-off share-based compensation. Excluding the one-off share-based compensation relating to administrative expenses, our administrative expenses increased from RMB1.2 billion for the year ended December 31, 2017 to RMB2.2 billion for the year ended December 31, 2018, primarily due to the expansion of our administration departments. Compensation relating to our administrative personnel increased from RMB0.6 billion for the year ended December 31, 2017 to RMB1.3 billion for the year ended December 31, 2018, primarily due to the increased headcount to accommodate for the rapid growth of our business.

***Research and development expenses***

Our research and development expenses increased by 83.3% from RMB3.2 billion for the year ended December 31, 2017 to RMB5.8 billion for the year ended December 31, 2018, primarily due to the increase in total compensation relating to our research and development personnel and the expansion of our smartphones, AI, internet services and other research projects, reflecting our increased focus on research and development. Salaries and benefits relating to research and development personnel increased primarily due to increased headcount to accommodate the rapid growth of our business.

***Fair value changes on investments measured at fair value through profit or loss***

Our fair value changes on investments measured at fair value through profit or loss decreased by 30.5% from a gain of RMB6.4 billion for the year ended December 31, 2017 to a gain of RMB4.4 billion for the year ended December 31, 2018, primarily due to changes in fair value of our equity and preferred share investments for the year ended December 31, 2018.

***Share of losses of investments accounted for using the equity method***

Our share of losses of investments accounted for using the equity method increased by 165.6% from RMB231.5 million for the year ended December 31, 2017 to RMB614.9 million for the year ended December 31, 2018, primarily due to share of loss of iQIYI, Inc of RMB616.3 million (NASDAQ ticker: IQ) for the year ended December 31, 2018.

***Other income***

Our other income increased by 88.3% from RMB448.7 million for the year ended December 31, 2017 to RMB844.8 million for the year ended December 31, 2018, primarily due to increase of income from wealth management products.

***Other gains/(losses), net***

Our other gains/(losses), net increased by 196.1% from net gains of RMB72.0 million in the year ended December 31, 2017 to net gains of RMB213.3 million in the year ended December 31, 2018, primarily due to the recognition of foreign exchange losses of RMB14.6 million for the year ended December 31, 2018, compared to foreign exchange losses of RMB144.3 million for the year ended December 31, 2017. The decrease in foreign exchange losses primarily resulted from the increase in United States Dollar assets from the gross proceeds of our initial public offering.

*Finance income, net*

Our net finance income increased by 707.8% from RMB26.7 million in the year of 2017 to RMB216.3 million in the year of 2018, primarily due to increase in our interest income. Our interest income increased primarily due to more bank deposits which generated higher interest received.

***Fair value changes of convertible redeemable preferred shares***

Changes in the fair value of our convertible redeemable preferred shares were recorded as "fair value changes on convertible redeemable preferred shares". Fair value changes of convertible redeemable preferred shares changed from a loss of RMB54.1 billion for the year ended December 31, 2017 to a gain of RMB12.5 billion for the year ended December 31, 2018, primarily due to revaluation of equity value of the Company based on the offer price in our initial public offering. After the completion of our initial public offering, all our convertible redeemable preferred shares were automatically converted to the Class B Shares. The fair value of each of convertible redeemable preferred share is equivalent to the fair value of each of our Class B Shares on the conversion date, which is the offer price in the initial public offering.

***Income tax expenses***

Our income tax expenses decreased from RMB2.1 billion for the year ended December 31, 2017 to RMB0.4 billion for the year ended December 31, 2018, primarily due to (1) an increase of deferred tax assets, and (2) a subsidiary becoming qualified to enjoy a preferential income tax rate of 10%. This resulted in a reversal of over accrued income tax expense during the year ended December 31, 2018.

***(Loss)/profit for the year***

As a result of the above mentioned, we reached a profit of RMB13.5 billion for the year ended December 31, 2018, compared with a loss of RMB43.9 billion for the year ended December 31, 2017.

## LIQUIDITY AND CAPITAL RESOURCES

Other than our initial public offering in July 2018, we have historically funded our cash requirements principally from cash generated from operations, convertible redeemable preference shares, asset-backed securities, bonds and bank borrowings. We had cash and cash equivalents of RMB11.6 billion, RMB30.2 billion and RMB25.9 billion as of December 31, 2017, 2018 and 2019, respectively. As of September 30, 2020, we had cash and cash equivalents of RMB30.3 billion.

The following table sets forth our cash flows for the periods indicated:

| | For the year ended December 31, | | | | For the nine months ended September 30, | |
|---|---|---|---|---|---|---|
| | **2017** | **2018** | **2019** | | **2019** | **2020** |
| | **RMB** | **RMB** | **RMB** | **US$** | **RMB** | **RMB** |
| | | | | | **(Unaudited)** | **(Unaudited)** |
| | | | **(in millions)** | | | |
| Net cash (used in)/generated from operating activities | (995.7) | (1,414.6) | 23,810.4 | 3,420.1 | 13,908.0 | 8,351.0 |
| Net cash used in investing activities | (2,677.7) | (7,508.0) | (31,570.1) | (4,534.8) | (11,768.9) | (7,173.1) |
| Net cash generated from financing activities | 6,214.9 | 26,574.2 | 3,121.2 | 448.3 | 2,577.0 | 3,839.9 |
| Net increase/(decrease) in cash and cash equivalents | 2,541.5 | 17,651.6 | (4,638.5) | (666.4) | 4,716.1 | 5,017.8 |
| Cash and cash equivalents at beginning of the year/period | 9,230.3 | 11,563.3 | 30,230.1 | 4,342.3 | 30,230.1 | 25,919.9 |
| Effects of exchange rate changes on cash and cash equivalents | (208.5) | 1,015.2 | 328.3 | 47.3 | 593.0 | (680.0) |
| Cash and cash equivalents at end of the year/period | 11,563.3 | 30,230.1 | 25,919.9 | 3,723.2 | 35,539.2 | 30,257.7 |

***Net Cash (Used in)/Generated from Operating Activities***

Net cash (used in)/generated from operating activities represents cash generated from operations minus income tax paid. Cash generated from operations primarily comprise our (loss)/profit before income tax for the period adjusted by non-cash items and changes in working capital.

For the nine months ended September 30 of 2020, net cash generated from our operating activities amounted to RMB8.4 billion, representing cash generated from operations of RMB9.8 billion minus income tax paid of RMB1.4 billion. Cash generated from operations was primarily attributable to our profit before income tax of RMB12.8 billion, adjusted by an increase in trade payables of RMB3.9 billion, partially offset by an increase in trade receivables of RMB7.0 billion.

In 2019, net cash generated from operating activities amounted to RMB23.8 billion, representing cash generated from operations of RMB26.0 billion minus income tax paid of RMB2.2 billion. Cash generated from operations was primarily due to our profit before income tax of RMB12.2 billion, as adjusted by (i) the add-back of non-cash items, primarily comprising impairment provision for inventories of RMB3.9 billion and share-based compensation of RMB2.2 billion, partially offset by fair value gains on long-term investments measured at fair value through profit or loss of RMB3.8 billion, and (ii) changes in working capital, which primarily comprised an increase in trade payables of RMB13.5 billion, an increase in inventories of RMB7.0 billion, an increase in loan receivables of RMB3.4 billion and an increase in advance from customers of RMB3.8 billion.

In 2018, net cash used in operating activities amounted to RMB1.4 billion, representing cash generated from operations of RMB0.1 billion minus income tax paid of RMB1.5 billion. Cash generated from operations was primarily due to our profit before income tax of RMB13.9 billion, as adjusted by (i) the add-back of non-cash items, primarily comprising share-based compensation of RMB12.4 billion and impairment provision for inventories of RMB3.0 billion, partially offset by fair value changes of convertible redeemable preferred shares of RMB12.5 billion and fair value gains on long-term investments measured at fair value through profit or loss of RMB4.4 billion, and (ii) changes in working capital, which primarily comprised an increase in inventories of RMB16.1 billion, an increase in loan receivables of RMB2.8 billion, an increase in prepayments and other receivables of RMB9.5 billion and an increase in trade payables of RMB12.6 billion.

In 2017, net cash used in operating activities amounted to RMB1.0 billion, representing cash generated from operations of RMB0.5 billion minus income tax paid of RMB1.5 billion. Cash used in operations was primarily due to our loss before income tax of RMB41.8 billion, as adjusted by (i) the add-back of non-cash items, primarily comprising fair value changes of convertible redeemable preferred shares of RMB54.1 billion, partially offset by fair value gains on long-term investments measured at fair value through profit or loss of RMB6.4 billion, and (ii) changes in working capital, which primarily comprised an increase in inventories of RMB8.6 billion, an increase in loan receivables of RMB6.9 billion related to our fintech business, an increase in prepayments and other receivables of RMB6.6 billion and an increase in trade payables of RMB15.5 billion. The operating cash outflow in 2017 was primarily due to an increase in loan receivables, as a result of the nature of our fintech business, which did not constitute our core business in terms of revenue contribution. For 2017, excluding the increase in loan receivables mainly resulted from fintech business, we would record a positive operating cash flow of RMB5.9 billion.

***Net Cash Used in Investing Activities***

For the nine months ended September 30 of 2020, our net cash used in investing activities was RMB7.2 billion, which was primarily attributed to the net increase of short-term investments measured at fair value through profit or loss of RMB4.6 billion, the purchase of property, plant and equipment of RMB1.3 billion and the net increase of investments accounted for using the equity method of RMB1.2 billion.

In 2019, our net cash used in investing activities was RMB31.6 billion, which was mainly attributable to net cash used in the placement and withdrawal of short-term bank deposits of RMB20.2 billion and net cash used in purchase and settlement of short-term investments measured at fair value through profit or loss of RMB9.8 billion.

In 2018, our net cash used in investing activities was RMB7.5 billion, which was mainly attributable to capital expenditures of RMB3.8 billion, net cash used in the purchase and disposal of long-term investments measured at fair value through profit or loss of RMB1.7 billion, net cash used in the placement and withdrawal of short-term bank deposits of RMB1.2 billion, the net cash used in purchase and settlement of wealth management products (including short-term investments measured at fair value through profit or loss and short-term investments measured at amortized cost) of RMB1.0 billion.

In 2017, our net cash used in investing activities was RMB2.7 billion, which was mainly attributable to the net cash used in purchase and settlement of wealth management products (including short-term investments measured at fair value through profit or loss and short-term investments measured at amortized cost) of RMB1.7 billion, and capital expenditures of RMB1.2 billion.

***Net Cash Generated from Financing Activities***

For the nine months ended September 30 of 2020, our net cash generated from financing activities was RMB3.8 billion, which was primarily attributed to the proceeds from fund investors of RMB3.4 billion and the net decrease of borrowings of RMB1.3 billion.

In 2019, our net cash generated from financing activities was RMB3.1 billion, which was mainly attributable to net cash generated from proceeds and repayment of borrowings of RMB6.6 billion, partially offset by payments for shares repurchase of RMB2.9 billion. In the future, we may continue to conduct share repurchase activities from time to time.

In 2018, our net cash generated from financing activities was RMB26.6 billion, which was mainly attributable to net proceeds from issuance ordinary shares relating to the initial public offering of RMB23.2 billion, proceeds from fund investors of RMB2.8 billion and net cash generated from withdrawal and placement of restricted cash of RMB0.9 billion.

In 2017, our net cash generated from financing activities was RMB6.2 billion, which was mainly attributable to net cash generated from proceeds and repayment of borrowings of RMB6.6 billion.

## INDEBTEDNESS

For a summary of our material indebtedness, see "Description of Other Material Indebtedness."

## CAPITAL EXPENDITURES AND LONG-TERM INVESTMENTS MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS

The following table sets forth our capital expenditures and placement for long-term investments for the periods indicated:

| | For the year ended December 31, | | | | For the nine months ended September 30, | |
|---|---|---|---|---|---|---|
| | 2017 | 2018 | 2019 | | 2019 | 2020 |
| | RMB | RMB | RMB | US$ | RMB | RMB |
| | | | | | (Unaudited) | (Unaudited) |
| | (in millions) | | | | | |
| Capital expenditures | 1,217.8 | 3,785.3 | 3,405.2 | 489.1 | 2,328.7 | 1,515.4 |
| Placement for long-term investments(1) | 813.2 | 1,999.8 | 3,987.2 | 572.7 | 2,780.2 | 6,675.5 |
| **Total** | **2,031.0** | **5,785.1** | **7,392.4** | **1,061.8** | **5,108.9** | **8,190.9** |

Note:

(1) Placement for long-term investments represents equity investments and preferred share investments.

Our capital expenditure primarily included disbursement on property and equipment resulting from the construction of and improvements made to our office complex, as well as on our intangible assets. Our capital expenditure decreased by 10.0% from RMB3,785.3 million in 2018 to RMB3,405.2 million in 2019 and experienced a year-on-year decrease of 34.9% for the nine months ended September 30, 2020 to RMB1,515.4 million.

We believe that our existing cash and cash equivalents, cash flows from operations, term deposits will be sufficient to meet the anticipated cash needs for our operating activities and capital expenditures for at least the next 12 months.

## CONTRACTUAL OBLIGATIONS

Our commitments primarily comprise capital expenditure contracted for but not yet incurred during the periods, operating lease commitments and other commitments.

### *Capital Commitments*

The table below sets forth our capital commitments as of the dates indicated:

| | As of December 31, | | | | As of September 30, |
|---|---|---|---|---|---|
| | 2017 | 2018 | 2019 | | 2020 |
| | RMB | RMB | RMB | US$ | RMB |
| | | | | | (Unaudited) |
| | (in millions) | | | | |
| Property and equipment | 1,486.0 | 1,825.3 | 1,747.0 | 250.9 | 927.0 |
| Intangible assets | 112.9 | 57.8 | 28.8 | 4.1 | 33.7 |
| Investments | 198.8 | 137.2 | 217.5 | 31.2 | 95.4 |
| **Total** | **1,797.7** | **2,020.3** | **1,993.3** | **286.2** | **1,056.1** |

### *Operating Lease Commitments*

The table below sets forth our future aggregate minimum lease payments under non-cancellable operating leases:

| | As of December 31, | | | | As of September 30, |
|---|---|---|---|---|---|
| | 2017 | 2018 | 2019 | | 2020 |
| | RMB | RMB | RMB | US$ | RMB |
| | | | | | (Unaudited) |
| | (in millions) | | | | |
| Not later than 1 year | 258.2 | 560.9 | 305.2 | 43.8 | 622.5 |
| Later than 1 year and not later than 5 years | 280.6 | 385.0 | – | – | – |
| Later than 5 years | – | 83.3 | – | – | – |
| **Total** | **538.8** | **1,029.2** | **305.2** | **43.8** | **622.5** |

## OFF-BALANCE SHEET COMMITMENTS AND ARRANGEMENTS

As of September 30, 2020, except for financial guarantee contracts, we had not entered into any off-balance sheet arrangements.

## FINANCIAL RISK DISCLOSURE

Our activities expose us to a variety of financial risks: market risk (including foreign exchange risk, interest rate risk and price risk), credit risk and liquidity risk. Our overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on our financial performance. Risk management is carried out by our senior management. For more information on the financial risks, see note 3 to the consolidated financial statement included in this Offering Circular.

### Market Risk

#### *Foreign Exchange Risk*

Our transactions are denominated and settled in our functional currency, U.S. dollars. Our subsidiaries operate in mainland China and overseas and are exposed to foreign exchange risk arising from various currency exposures, primarily with respect to U.S. dollars and RMB. Therefore, foreign exchange risk primarily arose from recognized assets and liabilities in our subsidiaries in mainland China when receiving or to receive foreign currencies from, or paying or to pay foreign currencies to overseas business partner, and recognized assets and liabilities in the our overseas subsidiaries when receiving or to receive foreign currencies from, or paying or to pay foreign currencies to business partners in mainland China.

We will continue to monitor changes in currency exchange rates and will take necessary measures to mitigate exchange rate impact.

#### *Interest Rate Risk*

Our interest rate risk primarily arose from borrowings with floating and fixed rates, loan receivables, long-term bank deposits, short-term bank deposits and cash and cash equivalents. Those carried at floating rates expose us to cash flow interest rate risk whereas those carried at fixed rates expose the Group to fair value interest rate risk.

We regularly monitor our interest rate risk to ensure there is no undue exposure to significant interest rate movements.

#### *Price Risk*

We are exposed to price risk in respect of our long-term investments and short-term investments measured at fair value through profit or loss held by us. We are not exposed to commodity price risk. To manage our price risk arising from the investments, we diversify our portfolio. Each investment is managed by senior management on a case-by-case basis. The sensitivity analysis is performed by our management.

### Credit Risk

We are exposed to credit risk in relation to our cash and cash equivalents, short-term bank deposits, long-term deposits, restricted cash, short-term investments, loan receivables, trade receivables, other receivables and financial guarantee contracts. The carrying amounts of each class of the above financial assets represent our maximum exposure to credit risk in relation to financial assets.

To manage risk arising from cash and cash equivalents, short-term bank deposits, long-term deposits, restricted cash and short-term investments, we only transact with state-owned or reputable financial institutions in mainland China and reputable international financial institutions outside of mainland China. There has been no recent history of default in relation to these financial institutions.

To manage risk arising from trade receivables, we have policies in place to ensure that credit terms are made to counterparties with an appropriate credit history and our management performs ongoing credit evaluations of our counterparties. The credit period granted to our customers is usually no more than 180 days and the credit quality of these customers are assessed, which takes into account their financial position, past experience and other factors.

For other receivables, our management makes periodic collective assessments as well as individual assessment on the recoverability of other receivables based on historical settlement records and past experiences. In view of the history of cooperation with debtors and the sound collection history of receivables due from them, our management believes that the credit risk inherent in our outstanding other receivable balances due from them is not significant.

Financial guarantee contracts are contracts that require us to make specified payments to reimburse the creditors (i.e. banks and financial institutions) for a loss incurred if a specified debtor fails to make payments when due. For financial guarantee contracts, we have taken measures to manage credit risk, including credit examination, fraud examination and risk monitoring alert.

To manage risk arising from loan receivables, we perform standardized credit management procedures. For pre-approval investigation, we use our platform and systems using big data technology to optimize the review process, aspects including credit analysis, assessment of collectability of borrowers, and possibility of misconduct and fraudulent activities. In terms of credit examining management, we have established specific policies and procedures to assess loans offering. For subsequent monitoring, we implemented credit examination on each borrower every three months. For unqualified borrowers, credit facilities granted previously could be terminated immediately. Once the loan was issued, all borrowers would be assessed by fraud examination model to prevent fraudulent behaviors. In post-loan supervision, we have established risk monitoring alert system through periodical monitoring, system alert, and corresponding solutions to identify impaired loans. The estimation of credit exposure for risk management purposes is complex and requires the use of models, as the exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties. We measure credit risk using Probability of Default, Exposure at Default, and Loss Given Default. This is similar to the approach used for the purposes of measuring Expected Credit Loss under IFRS 9.

**Liquidity Risk**

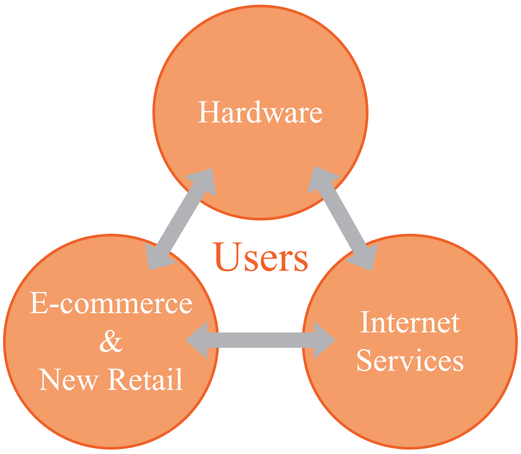
We aim to maintain sufficient cash and cash equivalents. Due to the dynamic nature of the underlying business, our policy is to regularly monitor our liquidity risk and to maintain adequate cash and cash equivalents or adjusted financing arrangements to meet our liquidity requirements.

Xiaomi is an internet company with smartphones and smart hardware connected by an IoT platform at its core.

**Our Business Model**

Our Company is built on innovation and efficiency. As a company founded by engineers and designers, we embrace a culture of bold innovation to push the boundaries of what technology can offer. A spirit of innovation permeates our Company and guides everything we do. In addition, we are relentless in our pursuit of efficiency. We strive to achieve cost savings to deliver value back to our users.

Our unique and powerful "triathlon" business model comprises three synergistic pillars of growth – (i) innovative, high quality and well-designed hardware focused on exceptional user experience, (ii) highly efficient new retail distribution platform allowing our products to be priced accessibly and (iii) engaging internet services.




*Hardware*

We offer a broad range of hardware products developed in-house or in collaboration with our ecosystem partners. Innovation, quality, design and user experience are ingrained in all of our products regardless of whether they are developed in-house or in collaboration with our partners. We strive to offer our products at price points that are accessible to the widest user base to enjoy broad adoption and high retention. For our core in-house products, we focus on designing and developing a range of cutting-edge hardware products including smartphones, laptops, smart TVs, AI speakers, smart routers, smart watches, smart refrigerators, smart washing machines and smart air conditioners.

We curate a wide range of additional products by investing in over 300 companies. This has enabled us to build one of the world's leading consumer IoT platforms. As of September 30, 2020, the number of connected IoT devices (excluding smartphones and laptops) on our AIoT platform reached 289.5 million, representing an increase of 35.8% year-over-year. This active and integrated suite of connected technology products enhances the lives of our users and constitutes a proprietary delivery platform for our internet services. We also curate a range of lifestyle products to further drive brand awareness and traffic to our sales points.

*New Retail*

Our highly efficient omni-channel new retail distribution platform is a core component of our growth strategy, allowing us to operate efficiently while simultaneously extending our user reach and enhancing our users' experience. Since inception, we have focused on direct online sales of our products to maximize efficiency and build a direct digital relationship with our users. We have continually expanded our direct offline retail network, for example, through our Mi Home stores. Moreover, to establish our offline new retail presence in lower-tier cities and rural areas of mainland China, we have built a sizable authorized store network. Our offline retail network allows us to broaden our reach and provide a richer user experience, while maintaining similar efficiency and the same product prices as our online channels. Our efficient omni-channel sales strategy enables us to provide our products at accessible price points to the largest user base.

*Internet Services*

We provide internet services to give our users a complete mobile internet experience. In September 2020, we had 368.2 million MAU on MIUI, our proprietary operating system built on the Android kernel. MIUI fully embraces the Android ecosystem, including all mobile apps. It functions as an open platform for us to deliver our wide range of internet services, such as content, entertainment, financial services and productivity tools. The connectivity between our devices and the seamless integration between smart hardware and internet services enable us to provide our users with better user experience. Furthermore, we have a proven track record of developing killer apps. Compared to other internet platforms that acquire new users at high costs, we leverage the sale of our hardware to acquire users at a profit.

*Network Effects*

Our unique and powerful triathlon business model comprises three synergistic pillars that are closely connected. We strive to offer killer products that are high quality, high performance, well designed and honestly priced. These products in turn bring additional traffic to our retail channels. We deliver our products to users at accessible prices through our highly efficient new retail channels such as our e-commerce platforms and our Mi Home stores. With our internet services, we closely engage and interact with users on our platform, thus increasing user stickiness and monetization opportunities.

This business model has led to powerful network effects across our platform, which enhances user experience, engagement and retention. As more of our products and services are connected, we are set to deliver better and richer user experience, which will, in turn, attract more users to our platform.

## OUR STRENGTHS

We believe that the following strengths contribute to our success and are differentiating factors that set us apart from our peers.

### 1. Triathlon Business Model

We believe the three components of our unique business model are complementary to each other, creating robust barriers to entry for potential competitors and enabling us to create a sustainable business model that cannot be easily replicated. The seamless integration of our smart hardware products, new retail and internet services has led to powerful network effects across our platform, which enhances user experience, engagement and retention. As more of our products and services are connected, we will deliver better and richer user experiences, which will, in turn, attract more users to our products and services.

Smartphones and IoT products form a valuable platform to attract new users. We are able to acquire users at a positive margin through the sale of our innovative, high-quality, well-designed and user-centric hardware products, which serve as the gateway to providing our users with internet services. Our killer products also bring additional traffic to our retail channels. In addition, our omni-channel retail strategy, comprised of highly efficient and complementary online and offline retail channels, enables us to sell our products at highly accessible prices, increasing our reach and depth of product distribution. This results in rapid expansion of our user base across different geographies. Having amassed a large and engaged user base through our innovative hardware and efficient new retail distribution channels, we monetize our users through our vast platform of internet services, which include our proprietary apps.

Leveraging our innovative hardware portfolio, superior user experience and efficient new retail channels, we have accumulated a large, active and loyal user base, which we can effectively monetize through advertising and internet value-added services. We continuously expand and enrich internet services offerings available to our users and strengthen monetization capabilities in domestic and key overseas markets. As a result of our business model, we have successfully diversified our revenue streams by boosting revenue contribution from sales of IoT and lifestyle products, as well as internet services, which has rich monetization potential with proven user stickiness and higher gross margins.

**2. Scale and Leadership**

As a testimony to the strength of our unique triathlon business model, we have experienced robust growth since our inception in 2010. Two years after our inception, our annual sales exceeded US$1.0 billion in 2012. In 2014, our annual sales exceeded US$10.0 billion, which, according to iResearch, made us the fastest company in history to achieve such milestone. Our growth momentum continued in recent years. Our total revenue increased by 52.6% from RMB114.6 billion in 2017 to RMB174.9 billion in 2018 and further increased by 17.7% to RMB205.8 billion in 2019. The total revenue increased on a year-over-year basis by 34.5% from RMB53.7 billion in the third quarter of 2019 to RMB72.2 billion in the third quarter of 2020.

We have achieved leading positions in our major products and services categories. According to Canalys, we ranked number three globally in terms of smartphone shipments in the third quarter of 2020. Epitomizing our success in global expansion, our global smartphone shipments ranked among the top five in 54 markets, top 3 in 36 markets and No. 1 in 10 markets in the third quarter in 2020, according to Canalys. We are also a global leader in the IoT sector and many specific product categories. As of September 30, 2020, the number of connected IoT devices (excluding smartphones and laptops) on our AIoT platform reached 289.5 million, representing an increase of 35.8% year-over-year. According to All View Cloud ("**AVC**"), in the third quarter of 2020, our TV shipments ranked No. 1 in mainland China for the seventh consecutive quarter, and maintained a top 5 position globally. According to Canalys, our Mi Band ranked number one by global shipments in the second quarter of 2020. Our MIUI system has also seen significant growth in recent years, with a user base of 368.2 million MAU in September 2020, representing a 26.3% year-over-year increase.

**3. Brand and Passionate Users**

We have created an internationally renowned brand through our dedication to providing our users with high-quality products and services, which has been recognized by many global honors and accolades. For example, August 2020 marked our second entry into the Fortune Global 500 list, ranking 422nd. In June 2020, we were included in BCG's "50 Most Innovative Companies 2020" list, ranking 24th. In August 2020, we were named in the "Derwent Top 100 Global Innovators 2020" list, being one of three mainland China companies to make the list. In November 2020, we were named among the "50 Smartest Companies" list by MIT Technology Review.

Leveraging our powerful brand value and reputation, we have amassed a large and rapidly growing user base. Our users are highly engaged and spend a significant amount of time interacting within the Xiaomi platform. We believe our users have a high level of trust in our brand. Within our user base, we have a highly dedicated and intensely loyal group of users who have nicknamed themselves Mi Fans. These fans are very passionate about Xiaomi and own many of our products. For example, as of September 30, 2020, over 5.6 million users had more than five devices (excluding smartphones and laptops) connected to our IoT platform. Furthermore, our Mi Fans actively follow and support the latest developments of our Company. This extends beyond mainland China to places such as India, Indonesia and Spain, where thousands of avid Mi Fans queued up for hours outside new flagship stores on their opening days. In addition, we also benefit from our enthusiastic Mi Fans through their passionate word-of-mouth marketing and their constructive product feedback, which helps us to constantly improve our products and services. We have continually developed innovative internet services to expand and enrich the experience of users and to enhance their loyalty to Xiaomi's online communities and increase their level of engagement.

**4. Innovation and Design**

We have amassed a strong track record in innovation and design.

We have achieved many technological breakthroughs, which have been consistently recognized. For example, in September 2019, we released our concept smartphone, Mi MIX Alpha, a futuristic

5G smartphone featuring the world's first surround display and a screen-to-body ratio of 180.6%, demonstrating the Company's continued efforts in exploring cutting-edge technology. Launched in February 2020, our Mi 10 Pro was ranked number one in the camera category by DXOMARK at the time of product debut, empowered by its state-of-the-art imaging technologies and AI algorithms. Mi 10 Pro has also received the highest rating in the audio category by DXOMARK at the time of launch. In August 2020, our Mi 10 Ultra was again ranked number one globally by DXOMARK camera score at the time of launch. Attributing to our proven track record in innovation, Clarivate Analytics listed Xiaomi among the Derwent Top 100 Global Innovators in February 2020 for the second year in a row.

Furthermore, we developed MIUI, our very own operating system built on the Android kernel. We have constantly improved the MIUI platform by incorporating direct feedback from our Mi Fans and updating the MIUI developer version on a regular basis. In addition, our ability to develop killer apps has been consistently demonstrated by a wide range of popular services, including Mi App Store, Mi Browser, Mi Video and Mi News Feed.

We leverage our in-house design capabilities and continuous feedback from our users and Mi Fans to develop high-quality products and services with advanced features and compelling aesthetic designs that are very user friendly. As of September 30, 2020, we have received numerous industrial design awards for our smartphones and IoT products, including the Red Dot: Best of the Best award, the iF Gold award, the International Design Excellence Award (IDEA) Gold award and the Good Design award. In 2019 alone, our products won more than 50 design awards around the world, including the iF Silver Award for our Mi Mix 3 smartphone. We continued to win accolades in 2020, including the iF Gold Award for our handheld wireless vacuum cleaner and Best of the Best of the Red Dot Design Award for our Mijia smart electric baseboard heater. These awards are further testaments to our industry-leading design capabilities and craftsmanship.

**5. 5G and AIoT**

We believe that we are well-positioned to capture the new opportunities in the 5G era by leveraging our strong capabilities in research and development as well as innovation. Following the granting of 5G business licenses in mainland China in 2019, 5G technology has officially started to be implemented for commercial use. We established a research and development team back in 2016 for advanced research on 5G technology and are well-prepared for the commercialization of 5G. Such commitment and preparedness have been proven by our introduction of a series of 5G smartphone models. We launched our first 5G model, Mi MIX 3 5G, in Europe in February 2019 and our first 5G model in mainland China, Mi 9 Pro 5G, in September 2019, marking milestones in our 5G technology development. In December 2019, the Redmi brand launched Redmi K30 5G, the world's first 5G smartphone priced below RMB2,000. In February 2020, we launched Mi 10 and Mi 10 Pro, our flagship 5G smartphones under the Xiaomi brand, further demonstrating our industry-leading 5G technology. In August 2020, our Xiaomi brand unveiled another premium 5G model, Mi 10 Ultra, sporting our most cutting-edge technologies with price starting from RMB5,299.

We continuously work to improve our AIoT platform, enhance the interconnectivity across our products, and optimize user experience. In the third quarter of 2020, we introduced Redmi Router AX6 with Wi-Fi 6 technology, featuring "Xiaomi Express Connect", that provides an array of functions and enables superior IoT connectivity, including automatic device discovery, one-click network configuration, and automatic password sync across all supporting devices. In addition, we introduced the revolutionary ultra-wideband (UWB) technology. With this technology, users' smartphones will be able to perceive signals from the smart devices in their surroundings and control the smart devices by simply pointing towards them. In addition, at the annual Mi Developer Conference (MIDC 2020) held in November 2020, we launched Xiaomi Vela, an IoT software platform that is built on the Nuttx open-source embedded operating system. This platform aims to enhance the interconnectivity across everyday scenarios to build out a thriving IoT ecosystem. At this event, we also introduced our next-generation AI Assistant "XiaoAi AI Assistant 5.0", offering full-scenario intelligent collaboration, conversational active intelligence, customized voice with emotions, multi-modal visual capabilities, and smart learning assistance.

The wide application of 5G technology will enable the connection of a significantly larger number of IoT devices, giving us a powerful boost in developing our AIoT platform. After years of efforts in product innovation and strategic investment, we have built a vibrant AIoT platform featuring a wide variety of AI enabled IoT products and empowered by strong device-to-device connectivity and compatibility. Each of our smartphones, smart TVs, AI speakers, and smart watches can act as a control hub for other connected smart devices on our AIoT platform, significantly improving our users' smart living experience. Laying a solid foundation for further development of our AIoT platform, we have achieved an extensive scale with 289.5 million connected devices (excluding smartphones and laptops) as of September 30, 2020. Our AI voice assistant had amassed 78.4 million MAU in September 2020, representing a 35.5% increase year-over-year. We are committed to continually developing and broadening our open AIoT platform to attract more partners and users to join our pursuit of smart living.

As an integral part of our efforts to enrich our AIoT platform's products and services, we continually make strategic investments in our ecosystem partners. We identify promising startups and founders that share the same core values as ours and support them with our brand, capital, supply chain, research and development capabilities, product design and management expertise, as well as access to our highly efficient retail network. We empower our ecosystem partners and accelerate their growth, which, in turn, strengthens our AIoT platform and creates a win-win scenario. We have invested in over 300 companies as of September 30, 2020. Many of our investments have since become remarkable successes in terms of both strategic and financial values.

### 6. Global

We have successfully expanded overseas in recent years. We generated 28.0%, 40.0%, 44.3% and 50.5% of our revenues in countries and regions outside mainland China in 2017, 2018, 2019 and for the nine months ended September 30, 2020, respectively. As of September 30, 2020, our products were sold in over 90 countries and regions around the world.

Our smartphones business has continued to make significant progress globally. In the third quarter of 2020, our global smartphone shipments achieved 46.6 million units. According to Canalys, we achieved the highest year-over-year smartphone shipments growth rate among the top five smartphone companies globally. Our global smartphone shipments rose to the third position in the third quarter of 2020, with an all-time high market share of 13.5%, according to Canalys.

Our overseas business continued to demonstrate robust growth momentum. Our revenue from overseas markets amounted to a record high of RMB39.8 billion in the third quarter of 2020, representing a year-over-year increase of 52.1%. According to Canalys, our smartphone shipments in Europe grew 90.7% year-over-year, achieving an 18.7% market share. We maintained top 3 position in terms of smartphone shipments for the 2$^{nd}$ consecutive quarter in Europe and reached top 3 position in the Western European market for the first time.

In the third quarter of 2020, our IoT business continued its strong growth trajectory in overseas markets. Revenue from IoT and lifestyle products in overseas markets increased by 56.2% year-over-year, reaching a historical high. In addition, overseas revenue from certain key categories surpassed that in mainland China in the same quarter, such as wearable bands, electric scooters, and robot vacuum cleaners. Given the huge growth potential, we intend to fully leverage our highly efficient new retail channels and large user base to introduce more popular IoT products into overseas markets.

### 7. Efficiency

We operate with a relentless focus on operational efficiency in order to realize overall cost savings, which we return to our users.

Our online sales channels are highly efficient, as evidenced by their low distribution costs. Leveraging the growth of e-commerce, we are able to capture more customers who prefer to purchase through our online channels. Mi Store and Youpin are our own direct e-commerce platforms. We also cooperate with third-party e-commerce platforms such as JD.com, Tmall, Flipkart and Amazon to leverage their localized sales and marketing expertise, logistics and payment infrastructure.

In addition to our online channels, we have built a complementary offline retail network. Our offline retail network is comprised of our Mi Home stores as well as third-party offline retail partners to whom we supply our products directly. Our Mi Home stores provide users an immersive opportunity to experience our products first-hand, which increases their propensity to purchase our products offline and online. Our superior offline experience also improves user loyalty and satisfaction. We have approached our offline retail strategy with a similar efficiency level as our online distribution.

Our operational efficiency also extends to our supply chain costs. Our economies of scale allow us to increase our leverage with our assembly and component third party partners, which in turn allows us to benefit from more beneficial pricing terms and optimize our cost structure.

### 8. Strong Financial Profile

We have demonstrated strong profitability and generate positive cash flows from our operations, with a negative cash conversion cycle. We had a profit of RMB11.5 billion and a non-IFRS Adjusted Net Profit of RMB9.8 billion for the nine months ended September 30, 2020. Our net margin and non-IFRS net margin for the nine months ended September 30, 2020 were 6.6% and 5.6%, respectively. We also had net cash generated from operating activities of RMB8.4 billion for the nine months ended September 30, 2020.

We have also maintained a strong and stable cash balance and have additional liquidity provided by equity investments. We had cash and cash equivalents of RMB30.3 billion as of September 30, 2020. Furthermore, we enjoy the additional liquidity provided by our investments. We had short-term investments measured at fair value through profit or loss of RMB21.1 billion for the nine months ended September 30, 2020.

### 9. Founders and Management Team

Xiaomi is led by our Founder, Chairman and Chief Executive Officer, Lei Jun, a highly respected entrepreneur with close to 30 years of industry experience. Mr. Lei previously co-founded successful internet companies such as Kingsoft (SEHK Stock Code: 3888) and Joyo.com (sold to Amazon in 2004) and was a key investor in leading internet companies such as JOYY Inc. (Nasdaq ticker: YY) and UCWeb (sold to Alibaba in 2014). Lei Jun's proven track record and extensive experience in software, e-commerce, investment and mobile internet services provide clear leadership and strong commitment to our mission and execution.

Mr. Lei's iconic leadership has been recognized globally. In 2013, Lei Jun was awarded the "China Economic Figures of the Year" award by China Central Television (CCTV). In 2015, Lei Jun was the only Chinese entrepreneur among the "World's 100 Most Influential People of the Year" selected by TIME Magazine. He also received the "Asia Game Changer Award" from the Asia Society in the same year. In November 2017, Lei Jun was elected Vice Chairman of the All-China Federation of Industry and Commerce. In December 2017, he was also elected Vice President of China Quality Association.

Our co-founders and other senior management are composed of engineers, designers or executives with decades of extensive experience and strong track record in the technology, internet, and mobile communication industries. They worked at prominent global technology companies, including Google, Qualcomm, Microsoft and Motorola, before joining Xiaomi. They have been instrumental in instilling a genuinely transparent, efficient, inclusive and accessible corporate culture. This culture is the powerful driving force behind our collective passion to deliver advancements in innovation, quality, design and user experience across all of our products and services.

## OUR STRATEGIES

### 1. Unwavering focus on innovation, quality, design and user experience

We will continue to pursue artisanal craftsmanship in all our products and relentlessly focus on technological innovation, quality and design, to drive high-quality user experience and grow our loyal and engaged user base. We will continue to invest in research and development and prudently manage our high-quality human capital to maintain our leadership position in innovation, quality, design and user experience. In particular, we will invest in research and development with a close focus on 5G and AIoT. We plan to invest RMB50.0 billion in these areas in the next five years.

**2. Smartphone x AIoT**

We will continue to pursue our core strategy of "Smartphone x AIoT" and drive synergies between the two business segments in various aspects spanning interconnectivity, product design and marketing strategy, further strengthening the moats for our business. We strive to connect all facets of our users' life and fortify our leading position in smart living. We will continue to expand our product portfolio by focusing on innovation and product design, offer more intelligent user experiences and application scenarios, and enhance the connectivity and compatibility of our devices across the platform. We will further promote our open AIoT platform to attract more users and collaborate with more partners, thereby further enhancing the products and services available on our AIoT platform.

**3. Maintain relentless efficiency**

Our highly efficient omni-channel new retail distribution platform is a core component of our strategy, which enables us to maintain high efficiencies while broadening the coverage of user base and enhancing user experience. We will continue to enhance our highly efficient online and offline retail channels, boost supply chain cost efficiencies and drive distribution efficiencies to ensure the continued price accessibility of our products and services to grow our user base.

**4. Enrich our internet services**

We will further develop and diversify our internet services offerings to enhance user engagement and improve user experience. We believe that internet services will enable us to continue to grow our user base and increase user monetization, which will boost our financial growth and profitability. We intend to leverage our advanced big data and artificial intelligence capabilities to analyze our proprietary data to improve user experience via smarter and more customized services. We have been diversifying our internet services revenue outside of gaming and advertising from Chinese smartphones in recent years, expanding our services including Youpin ecommerce, fintech business, TV and other IoT services, and overseas internet services. We will continue to diversify our internet service offerings to improve our monetization capabilities.

**5. Broaden our overseas expansion**

Overseas markets offer us tremendous room to grow. We intend to leverage our strong execution capabilities to continue to extend and localize our unique business model in order to grow our user base and increase user monetization. We will further boost our market share in places where we have already established a strong foothold, including India, Europe, Southeast Asia and Latin America. We will also actively explore opportunities in new regions.

**6. Invest in and expand our ecosystem**

We will continue to identify, invest in and incubate promising companies, primarily in the fields of AIoT and mobile internet services, in order to further expand our ecosystem. We aspire to strengthen our ecosystem partners and enable them to grow rapidly and develop innovative, high-quality, well-designed products and services with exceptional user experience for our users. By expanding our ecosystem, we can accelerate the rollout of new complementary products and services, enabling us to grow our user base in mainland China and globally.

**Our Business**

**Hardware**

Our product portfolio includes a wide range of products developed in-house or in collaboration with our ecosystem partners. We offer our full line-up of products to consumers in mainland China. In the rest of the world, the availability of our hardware products varies by country and region.

*Diverse products*. We design and develop a suite of core in-house products, including smartphones, laptops, smart TVs, AI speakers, smart routers, smart watches, smart refrigerators, smart washing machines and smart air conditioners. We also curate a wide range of additional products by investing in over 300 companies as of September 30, 2020. In collaboration with us and centered around our users, our ecosystem partners produce a wide range of IoT and lifestyle products, such as smart home appliances, wearable products and transportation devices. Regardless of whether the products are designed and produced in-house or in collaboration with our ecosystem partners, the products share the same philosophy and are distinguished by a unique combination of innovative technologies, high quality, aesthetically pleasing designs, user-oriented features and price accessibility.

*Innovative technologies and high-quality, artisanal craftsmanship*. We relentlessly pursue the latest technological innovations in the industry for each of our products. Our smartphones have been ranked 1st, three times in the camera category by DXOMARK, attributable to their state-of-the-art technologies and innovative algorithms. In September 2019, we released our concept smartphone, Mi MIX Alpha, a futuristic 5G smartphone featuring the world's first surround display and a screen-to-body ratio of 180.6%, demonstrating the Company's continued efforts in exploring cutting-edge technology. Launched in February 2020, our Mi 10 Pro was ranked number one in the camera category by DXOMARK at the time of product debut, empowered by its state-of-the-art imaging technologies and AI algorithms. Mi 10 Pro has also received the highest rating in the audio category by DXOMARK at the time of launch. We believe our brand series, primarily consisting of Mi, Redmi, Mi Home and Youpin, are synonymous with high quality and aesthetically pleasing products across all categories. We believe our users have confidence that they can expect the same high level of quality and artisanal craftsmanship from all our products. To reinforce this brand identity, we only work with hardware and lifestyle products partners who share our product and design philosophy.

*Exceptional user experience*. Our smartphones and smart TVs are designed for optimal integration with our MIUI operating system. Our IoT products are seamlessly integrated with our own Mi Home app and AI voice assistant, which allows us to tap into a wide variety of application scenarios. Our proprietary AI voice assistant can control a wide range of product models on our platform, including smart lamps, Mi TVs, Mi Air Purifiers and a variety of other connected smart home products. For example, when a user opens the door through a Mi Smart Door Lock, our AI voice assistant will welcome him/her home. At the same time, the Mi Air Purifier, Mi Air Conditioner and other smart devices could be switched on automatically. The Mi Smart Combo Washing Machine and Dryer Pro can be operated by the voice control function through our AI voice assistant and can also support automatic detergent dispensing functionality.

In the following sections, the suggested retail prices cited are suggested retail prices in mainland China. For markets outside of mainland China, suggested retail prices are similar to those in mainland China but are adjusted for local markets.

***Core In-House Products***

*Smartphones*

We have adopted a dual-brand strategy for our smartphones, since Xiaomi and Redmi became independent brands since January 2019. Xiaomi focuses on pioneering advanced technologies, establishing itself in the mid- to high-end markets, and building online and offline new retail channels, and Redmi brand is positioned to pursue the ultimate price-performance ratio and focuses on online channels.

Global shipments of our smartphones in the third quarter of 2020 reached 46.6 million units and smartphone revenue recorded RMB47.6 billion, representing a year-over-year increase of 45.3% and 47.5% respectively. According to Canalys, we achieved the highest year-over-year smartphone shipments growth rate among the top five smartphone companies globally and our global smartphone shipments rose to the 3rd position in the third quarter of 2020, with an all-time high market share of 13.5%.

Following the granting of 5G business licenses in mainland China, 5G technology has officially started to be implemented for commercial use. The commercialization of 5G technology could potentially lead to a new smartphone replacement cycle and boost the overall demand of the domestic market. We established a research and development team back in 2016 for advanced research on 5G technology and are now well-prepared for the commercialization of 5G. We launched our first 5G model, Mi MIX 3 5G, in Europe in February 2019 and our first 5G model in mainland China, Mi 9 Pro 5G, in September 2019, marking milestones in our 5G technology development. In December 2019, the Redmi brand launched Redmi K30 5G, the world's first 5G smartphone priced below RMB2,000. In February 2020, we launched Mi 10 and Mi 10 Pro, and in August 2020, we launched Mi 10 Ultra, our flagship 5G smartphone under the Xiaomi brand, further demonstrating our industry-leading 5G technology.

In the third quarter of 2020, we further expanded our smartphone business in mainland China, achieving growth in both volume and average selling price ("**ASP**"). According to Canalys, our smartphone shipments market share in mainland China climbed to 12.6% in the third quarter of 2020 from 9.0% in the same period of 2019, maintaining a top four position. Meanwhile, the ASP of our smartphones in mainland China increased by 14.7% year-over-year, driven by a higher percentage of sales from our premium smartphones. Our leading advantages in online channels also continued to expand. According to third-party data, our smartphone market share in terms of online shipments increased from 18.5% in the first quarter of 2020 to 25.7% in the third quarter of 2020. During the Singles' Day shopping festival in 2020, we ranked 1st in sales volume among Android smartphones on Tmall.com and JD.com.

Our overseas business continued to demonstrate robust growth momentum. According to Canalys, our smartphone shipments in Europe grew by 90.7% year-over-year, achieving an 18.7% market share. We maintained top 3 position in terms of smartphone shipments for the 2nd consecutive quarter in Europe and reached top 3 position in the Western European market for the first time. Below is a selected list of our recent smartphone models:

**Xiaomi Brand**

*Mi MIX Series*

*Mi MIX Alpha (RMB19,999)*

In September 2019, we released our concept smartphone, Mi MIX Alpha, a futuristic 5G smartphone featuring the world's first surround display and a screen-to-body ratio of 180.6%, demonstrating the Company's continued efforts in exploring cutting-edge technology. Mi MIX Alpha features a state-of-the-art 7.92-inch, 2,088 × 2,250 Super AMOLED display that wraps around the edges and nearly spans the entire width of both sides of the phone, rendering a seamless and multi-functional user experience. It also features Qualcomm Snapdragon™ 855+ processor, LPDDR4X and a triple camera setup capable of recording 8K videos.

*Mi Number Series*

*Mi 10 (RMB3,999 and above)/ Mi 10 Pro (RMB4,999 and above)/ Mi 10 Ultra (RMB5,299 and above)/ Mi 10T (EUR499 and above)/ Mi 10T Pro (EUR599 and above)*

In February 2020, we launched the latest flagship 5G smartphones of the Xiaomi brand – Mi 10 and Mi 10 Pro. Equipped with a Qualcomm Snapdragon™ 865 processor, Mi 10 and Mi 10 Pro are among the first smartphones in the industry to feature LDPDDR5, UFS3.0 and Wi-Fi 6 technologies, which have revolutionarily accelerated the speed of application loading, operation and text processing. Mi 10 Pro was ranked number one in the camera category by DXOMARK at the time of product debut, empowered by its state-of-the-art imaging technologies and AI algorithms. Mi 10 Pro has also received the highest rating in the audio category by DXOMARK at the time of launch. As part of our 10th anniversary promotional efforts, we also unveiled the Mi 10 Ultra in August 2020, sporting our most cutting-edge technologies, and it was again ranked number one globally by DXOMARK camera score at the time of launch. In September 2020, we launched the Mi 10T and Mi 10T Pro models targeting the overseas markets, featuring a Snapdragon 865 processor, a 144Hz refresh rate display and 64MP and 108MP high definition cameras.

*Mi CC Series*

*Mi CC9 Pro (RMB2,799 and above)/ Mi Note 10 (EUR549.9 and above)/ Mi Note 10 Pro (EUR649.9 and above)*

In November 2019, we launched Mi CC9 Pro in Beijing and its international version Mi Note 10 and Mi Note 10 Pro in Madrid, as the latest flagships from the Mi CC and Mi Note series. The models are equipped with industry-leading 108MP penta camera, with a single photo resolution of up to 12,032 x 9,024, 12 times as high as 4K resolution. The models also feature Qualcomm Snapdragon™ 730G, multi-functional near-field communication (NFC) system, and 3D curved AMOLED display.

**Redmi Brand**

*Redmi K Series*

*Redmi K30 4G (RMB1,599 and above)/ Redmi K30 5G (RMB1,999 and above)/ Redmi K30 Pro (RMB2,999 and above)/ Redmi K30 Ultra (RMB1,999 and above)/ Redmi K30S Ultra (RMB2,599 and above)*

In December 2019, we launched the dual mode 5G smartphone Redmi K30 5G under with attractive specifications including a Qualcomm Snapdragon™ 765G processor and a 64-megapixel main camera. As world's first 5G smartphone priced below RMB2,000, Redmi K30 5G has garnered global attention since its launch with its substantially more attractive price point compared to other 5G smartphones in the market. Redmi K30 5G marked the Redmi brand's first step as a pioneer in providing 5G smartphones with ultimate price-performance ratio to the mass market. We launched Redmi K30 Pro in March 2020, which is equipped with a suite of performance upgrades, including the Qualcomm Snapdragon™ 865, LPDDR5, and UFS 3.1 flash storage. It also features a pop-up selfie camera and ultra-slim bezels to achieve an incredible 92.7% screen-to-body ratio. In the third quarter of 2020, we unveiled the Redmi K30 Ultra and Redmi K30S Ultra to appeal to different market segments. The Redmi K30 Ultra is equipped with Dimensity 1000+ 5G flagship processor and features a 120 Hz AMOLED full screen display, while the Redmi K30S Ultra sports a Snapdragon 865 processor and a 144 Hz refresh rate display. According to Canalys, Redmi accounted for 3 of the world's top 10 best-selling smartphones in the third quarter of 2020.

*Redmi Note Series*

*Redmi Note 9 4G (RMB999 and above)/ Redmi Note 9 5G (RMB1,299 and above)/ Redmi Note 9 Pro 5G (RMB1,599 and above)*

In November 2020, we released three models in the Redmi Note 9 series in mainland China. Among them, Redmi Note 9 4G has 6,000mAh long battery life; Redmi Note 9 5G is equipped with Dimensity 800U processor and 48MP ultra-clear camera; Redmi Note 9 Pro 5G is not just the first smartphone with a Snapdragon 750G processor, but is also equipped with a 108MP camera and a 120 Hz refresh rate.

*Redmi X Series*

*Redmi 10X 4G (RMB999 and above)/ Redmi 10X 5G (RMB1,599 and above)/ Redmi 10X Pro 5G (RMB2,299 and above)*

In May 2020, we launched the Redmi 10X Series in Mainland China. Redmi 10X 4G carries 5,020mAh battery and 18W fast charging technology. Redmi 10X 5G and Redmi 10X Pro 5G are equipped with the MediaTek Dimensity 820 SoC and supports dual 5G standby, while also feature a Samsung AMOLED display and 30x digital zoom camera.

*Redmi Number Series*

*Redmi 9 (RMB799 and above)/ Redmi 9A (RMB599 and above)*

In June 2020, we released the highly cost-effective entry-level Redmi 9A series. Redmi 9A has a 5,000mAh long-life battery and a 6.53-inch large screen. In July 2020, we released the Redmi 9, equipped with a large 5,020mAh battery and a Helio G80 high performance processor.

*Smart TVs*

In the third quarter of 2020, our smart TV business maintained its leadership position and global shipments of our smart TVs reached 3.1 million units. According to All View Cloud ("**AVC**"), in the third quarter of 2020, our TV shipments ranked No. 1 in mainland China for the seventh consecutive quarter, and maintained a top five position globally. As a market leader in smart TVs, we further solidified our position in the premium market and introduced a number of flagship products within the Mi TV Master Series in the third quarter of 2020. Following the August debut of the Mi TV LUX Transparent Edition, the world's first mass-produced transparent TV, we launched the Mi TV LUX 82" and the Mi TV LUX 82" Pro in September 2020. Mi TV LUX 82" offers great price-to-performance ratio among 4K TVs, with prices starting from RMB9,999. Mi TV LUX 82" Pro introduced cutting-edge Mini LED backlight technology that enriches images with incredible layers of details and definitions, and is priced starting from RMB49,999.

*Laptops*

We design and develop our laptops with a focus on delivering lightweight, portable products equipped with comprehensive features to offer the best quality and price among all peer products with similar specifications. Our Mi series laptops consist of three lines – Mi Notebook Air, Mi Notebook Pro and Mi Gaming Laptop. Among the latest models, Mi Notebook Air 12.5" starts from RMB3,599, Mi Notebook Air 13.3" 2019 starts from RMB4,999, Mi Notebook Pro 15.6" starts from RMB5,599, and Mi Gaming Laptop 2019 starts from RMB7,499. We launched our Redmi series laptops in 2019. We have introduced a number of ultra-thin models with attractive prices, including RedmiBook 14 (including its variations 14 Pro and 14 Ryzen Edition) (RMB3,199 and above) and our "full-screen" laptop, RedmiBook 13 (RMB3,799 and above). In August 2020, we launched a 16.1-inch large screen Redmi G gaming laptop, equipped with a 144 Hz ultra-high refresh rate and surround sound, bringing users the ultimate gaming experience.

*AI Speakers*

We ranked third in mainland China and fifth globally in terms of smart speakers shipment in 2019, according to iResearch. Our AI speakers currently include a variety of models priced from RMB49 to RMB599. Our AI speakers feature high-end performance without compromising design and portability. Users can connect our voice-controlled AI speakers with our other smart hardware products via Wi-Fi and program customized voice commands. Our first speaker with a screen, Xiaomi Touch Screen Speaker, can be used not only to receive and make phone calls, view a variety of video content and watch over your front stoop when connected with our smart door bell. We launched our Redmi XiaoAI Touch Screen Speaker, in March 2020, which features an 8-inch HD full-fit screen to reduce reflection and a wide visual angle. Redmi XiaoAI Touch Screen Speaker gathers the content of a variety of popular online video platforms to provide an interactive and seamless entertainment experience to its users.

*Smart Routers*

Our smart routers offer superior-price performance ratio among major comparable products. At the launch of Mi 10 series, we also launched Mi AIoT Router AX3600 with high cost-effective Wi-Fi 6 standard, followed by the launch of Mi Router AX1800 in May 2020, which is powered by a quad-core Qualcomm APQ6000 chipset. In June 2020, we officially launched Redmi AX5 Wi-Fi 6 router, with four independent signal amplifier antennas, increasing the signal strength by 4dB and increases the coverage by 50%. In August 2020, we introduced Redmi Router AX6 with Wi-Fi 6 technology, featuring "Xiaomi Express Connect", which provides an array of functions and enables superior IoT connectivity, including automatic device discovery, one-click network configuration, and automatic password sync across all supporting devices.

*Smart Watches*

Launched in November 2019, Mi Watch is priced from RMB1,299 to RMB1,999. Mi Watch can support cellular connectivity (through an eSIM), Wi-Fi, GPS, Bluetooth and NFC. Mi Watch can precisely monitor the heart rate of users and work with professional sports analytics providers to closely track users' sleep quality, heart rate, physical energy, etc. Mi Watch provides a revolutionary user experience with the MIUI For Watch system, offering a variety of dial plate selections and the most used apps for downloading. Our AI voice assistant can be activated for users to easily use voice commands for music playback, phone calls and navigation.

In November 2020, we released the Redmi Watch (price starting from RMB299), which has a 1.4-inch high-definition large screen, supports multi-function NFC and 7-day long battery life.

*Smart Refrigerators*

We offer a variety of models of Mi Refrigerators priced from RMB1,099 to RMB3,299, including Mi 4-Door Side-by-Side Refrigerator 486L, Mi 2-Door Side-by-Side Refrigerator 483L, Mi 3-Door Refrigerator 210L, and Mi 2-Door Refrigerator 160L, providing a spectrum of appliance sizes, storage volumes and price ranges. A three-dimensional air circulation setting ensures an even temperature in the cabin and prevents cool air from blowing directly onto food so it remains fresh longer. Each refrigerator boasts a silent 39dB noise level, keeping sound at a minimal volume. Along with a smart control panel, Mi 4-Door Side-by-Side Refrigerator is also enabled with our AI voice assistant and Mi Home app. Through voice control over our AI voice assistant, users can effortlessly modify the temperature and cooling mode of the cabin to customize their favored food tastes.

*Smart Washing Machines*

We offer various models of MIJIA Smart Washing Machine with suggested retail prices ranging from RMB799 to RMB3,299. In September 2020, we launched the Mijia Internet Direct Drive Washing and Drying Machine, featuring a quiet washing function with the lowest volume of 50dB. The Mijia Internet Direct Drive Washing and Drying Machine uses the industry-leading DD direct drive motor with higher energy efficiency, lower noise and vibration levels and is able to be more precisely controlled compared to the BLDC variable frequency motor. It also has unique features such as the silver ion antibacterial function that has a sterilization rate of 99.9%.

*Smart Air Conditioners*

We offer various models of smart air conditioners with suggested retail prices ranging from RMB1,799 to RMB5,999. In September 2020, we launched the Mi Vertical Air Conditioner with 2hp capacity. It adopts a cylindrical compact body design, has a circulating air volume of 1000$m^3$/h, noise levels as low as 33dB, and supports our AI voice assistant as well as the Mijia application remote start function.

***Products Produced in Collaboration with Our Ecosystem Partners***

We work with our ecosystem partners to design and develop a rich portfolio of smart hardware products. We meet our users' daily needs with products integrated through our internet platform in order to provide them with a digital lifestyle. Regardless of whether the products are designed and produced in-house or in collaboration with our ecosystem partners, the products share the same philosophy and are distinguished by a unique combination of innovative technologies, high quality, aesthetically pleasing designs, user-oriented features and price accessibility.

To facilitate the integration of hardware products with our Mi Home app and AIoT platforms, we provide our ecosystem partners with hardware and software modules that could be seamlessly integrated into their devices. Instead of requiring our partners to invest significant resources in developing sophisticated integration software, our ecosystem partners can leverage our prepackaged modules with such software and only need to develop their communication protocols. We have robust safety standards to protect our internet and AIoT platforms in respect of the integration of our modules with hardware products.

Our products produced in collaboration with our ecosystem partners are primarily divided into three categories, including mobile peripherals, smart devices and lifestyle products.

*Selected Mobile Peripheral Products*

*Headphones*

We offer three types of headphones, namely wired, Bluetooth and true wireless stereo headphones, priced from RMB29 to RMB999. Our headphones are equipped with various features to cater to different needs and scenarios, such as making phone calls, sound quality optimization, noise reduction, portability and sports. All these headphones offer superior sound quality, aesthetically pleasing design and comfortable wearing experience. Our TWS devices include Mi True Wireless Earbuds Basic, Mi True Wireless Earbuds, and Mi True Wireless Earphones 2S, which features truly wire-free design, intuitive touch control and auto-connect functions. In addition, we released the Mi True Wireless Earphones Air 2 Pro in October 2020, which is equipped with 35dB broadband active noise reduction, introducing more quality options to the active noise reduction TWS earphones market.

*Power Banks*

Our Mi Power Bank comes in various capacities, such as 20,000mAh, 10,000mAh and 5,000mAh. For example, the 10,000mAh Mi Power Bank Pro is sleek and slim, and supports two-way fast charging. It is able to fully charge a 3,000mAh smartphone approximately 2.2 times in a single charge.

*Fitness Bands*

In June, 2020, we introduced Mi Smart Band 5, offering a host of upgrades from its predecessors. Mi Smart Band 5 boasts a larger 1.1-inch AMOLED dynamic display, improved fitness tracking accuracy, women's health tracking, stress assessment, remote shutter control, and more. According to Canalys, we ranked No. 1 in terms of global shipments of wearable bands in the 2$^{nd}$ quarter of 2020.

*Selected Smart Hardware Products*

*Air Purifiers*

We ranked first in terms of air purifier shipments in mainland China in 2019, according to iResearch. The current models of our air purifiers include Mi Air Purifier 2S (RMB899), 3 (RMB899), Pro (RMB1,499), Pro H (RMB1,699), X (RMB1,999) and MAX Pro (RMB2,199). Mi Air Purifier MAX Pro is a premium model that features an OLED display showing PM2.5 level, temperature and humidity. It has professional grade setting formaldehyde CADR as high as 400m$^3$/h, and is capable of removing 99.9% of virus and bacteria. It has particulate CADR of 700m$^3$/h and can cover an area as large as 84m$^2$. Mi Air Purifier MAX Pro also has advanced noise reduction technology and the noise under sleep mode is as low as 33.5dB. In August 2020, we launched the Mijia Fresh Air Blower C1 80, a portable wall-mounted fan which doubles as an air purifier. It has an ultra-thin body and occupies only 0.16 square meters of wall area. The air blower can filter the air of an area up to 28.6 square meters and can remove common allergens, second-hand smoke, sand, dust and other pollutants from the air, creating a clean living environment.

*Robot Vacuum Cleaners*

We ranked second in terms of robot vacuum cleaners shipments in mainland China in 2019, according to iResearch. We currently offer two models of Mi Robot Vacuum Cleaner priced from RMB1,699 to RMB1,999 and four models of 2 in 1 Sweeping and Wet Mopping Mi Robot Vacuum Cleaner priced from RMB999 to RMB2,299. With a Laser Distance Sensor (LDS) or Visual Simultaneous Localization and Mapping (VSLAM) navigation, all models of Mi Robot Vacuum Cleaner are able to scan its surroundings 360 degrees, map out how the home is laid out and calculate the best cleaning path. Equipped with 12 to 15 sensors and a host of advanced features, all models of Mi Robot Vacuum clean homes in a smart and efficient way. Integrated with the Mi Home app, it allows users to control Mi Robot Vacuum Cleaners remotely and set regular cleaning schedules.

*Scooter/Self-balancing Scooters*

We ranked first in terms of electric scooters shipment globally in 2019, according to iResearch. We currently offer two models of electric scooter in mainland China, Mi Electric Scooter and Mi Electric Scooter Pro priced at RMB1,999 and RMB2,799, respectively. Both models have an award-winning design and are easy to master. The Mi Electric Scooter Pro has a travel range of 45 kilometers on a single charge and weighs 14.2 kilograms, and comes with features such as an LED headlight and an energy recycling function. Users can control both models via our Mi Home app.

In August 2020, we teamed up with Lamborghini to launch the Ninebot GoKart Pro Lamborghini Edition. The car incorporates classic Lamborghini colors and stylistic elements, is equipped with top of the range hardware configuration, speakers which can mimic up to 4 different types of engines, with a maximum speed of 40 kilometers per hour. It can also be transformed into a self-balancing scooter, allowing the user more choices.

*Water Purifiers*

We ranked second in terms of water purifiers shipments in 2019 in China, according to iResearch. We offer ten models of Mi Water Purifier priced from RMB999 to RMB3,999, which are well-designed water purifiers featuring reverse osmosis (RO) technology, which applies pressure through a RO membrane to separate purified water from tap water. It employs a multi-step filtration process before ultimately producing clean purified water. With a high flow RO filter and an optimized water purification path that improves filtration efficiency, Mi Water Purifier is able to empower higher rate of water flow. Mi Water Purifier can be monitored via the Mi Home app, allowing users to check real-time filter effectiveness and be reminded to change filters. Users can purchase new filters simply by placing orders via the Mi Home app. Mi Water Purifiers are designed to allow users to change filters intuitively and easily.

*Smart Rice Cookers*

Our smart rice cookers come in four variants, including the Mi Induction Heating Pressure Rice Cooker 3L, Mi Induction Heating Rice Cooker 3L/4L, Mi Smart Rice Cooker 1.6L/4L, and Mi Rice Cooker C1 3L/4L/5L. Mi Rice Cooker employs a magnetic relief valve to precisely control the pressure inside the rice cooker to 1.2 times the atmospheric pressure, corresponding to an ideal boiling point of water at 105 degrees Celsius, which results in tastier rice. It also uses electromagnetic heating technology for higher thermal efficiency. To ensure even heating and strong thermal performance, it features a gray cast iron surface that has undergone a 69-step crafting process. Mi Rice Cooker is priced from RMB149 to RMB1,099.

*Home Security Cameras*

Our current models of home security cameras include Mi Home Security Camera Lite (RMB99), Mi Home Security Camera SE (RMB149), Mi Home Security Camera 360° (RMB199) and Mi Home Security Camera 360° Pro (RMB249). These home security cameras offer 1080P or 2K high resolution and internet connectivity for long-distance, real-time monitoring through the Mi Home app.

*Smart Door Locks*

We offer various types of smart door locks with retail prices ranging from RMB999 to RMB1,799. The latest model is Mi Automatic Smart Door Lock priced at RMB1,799. Mi Automatic Smart Door Lock supports 7-fold safety status detection, and is able to resist the small black box attack and other technical cracks. Mi Automatic Smart Door Lock can also be paired with other smart home devices, so that unlocking the door lock will automatically turn on the paired devices to create a seamless smart living experience.

***Lifestyle Products***

We offer high-quality and well-designed lifestyle products, including housewares and personal accessories, from our ecosystem partners through our new retail platform. These lifestyle product offerings reinforce our brand image and bring additional traffic to our platform. We carefully source and select the lifestyle products by upholding the same standards that we apply to our brand series products. These selected lifestyle products are meticulously designed and crafted with attention to detail.

***IoT Developer Platform***

Our IoT developer platform is open to not only our ecosystem partners but also to other developers who desire to connect their devices with other devices connected to our platform and ultimately reach more users through us. A developer can submit its application for connecting a device to our platform through our IoT developer online platform at any stage of the device's life cycle. Once a developer's device has completed our quality and compatibility test, the developer is able to enjoy our fully managed and integrated support and services as well as a wide range of basic and advanced developing capabilities, such as hardware connection, IoT modules, cloud platform and storage, app remote control, voice control and content sharing.

***Value Proposition to Ecosystem partners***

*Minority capital investment*. We invest in the success of our ecosystem partners by providing early stage capital support and obtain minority equity interests in these partners.

*Incubation support*. We provide incubation support, including human resources and other administrative support and assistance to our ecosystem partners in their early stages of development.

*Product design and development support*. We bring our renowned industrial design prowess and technological expertise to the development of ecosystem hardware products and require our partners to follow our strict design and quality protocols and standards for products associated with our brands.

*Supply chain management support*. Through our know-how and our relationships with raw materials and component suppliers, we assist our partners in securing quality materials on preferential terms. Furthermore, we share our expertise in operational efficiency with our partners to help them manage their production-related costs.

*Brand, marketing and retail support*. Through our brand recognition and efficient new retail platform, we consistently offer highly popular IoT and lifestyle products to our users at accessible price points, thereby raising the profile, industry standing and sales volume of our ecosystem partners.

**New Retail**

Through our new retail strategy, we closely integrate online and offline sales channels to minimize layers of middlemen, achieve greater efficiency and provide the same products at the same accessible price points to our users.

***Online***

Leveraging our online expertise, we reach a wide group of customers across the entire e-commerce space in mainland China, in particular through our Mi Store and Youpin platforms.

During the first few years of our operations, we exclusively sold our products through our self-owned online distribution channels. Capitalizing on the growing trend of e-commerce and its distribution efficiency, we expanded our online distribution channels through cooperation with leading third-party online e-commerce partners to capture more customers. As a result, we believe we have established a strong online retail presence in our core markets. Our online approach provides significant advantages, including lower distribution costs.

*Direct Online Retail*

Currently our direct online retail channels include our Mi Store, our Youpin platform and our flagship store on Tmall, all of which enable us to efficiently sell our products and services to our customers at accessible price points.

Mi Store

Mi Store, available in mobile app and Mi.com, offers the full line-up of our products directly to our users. In mainland China and many overseas markets, users can purchase our products directly from local Mi Store apps and websites. For other overseas markets, Mi Store serves as the centralized platform for users to learn about our products and services. Mi Store creates a curated shopping experience for our users through personalized product recommendations and insightful product descriptions.

Our Mi Store mobile app allows customers to quickly and efficiently discover, review, select and purchase our products. We strive to provide customers with a customized shopping experience through analyzing and understanding their transaction histories and browsing patterns on our mobile apps in order to increase customer stickiness and enhance cross-selling opportunities. We continuously develop additional features to enhance user experience.

Youpin

Youpin is an e-commerce marketplace that we created not only to sell our Mi-branded products but also to sell high-quality products that are not associated with Xiaomi but curated and sourced by us. Youpin's e-commerce platform complements our existing business model by offering a wider set of popular high-quality products. Youpin, which includes the Youpin mobile app and the xiaomiyoupin.com website, stands for good taste and premium quality, which is also the Chinese meaning of the name.

We distinguish ourselves from other e-commerce players through our careful selection of a limited set of SKUs within each category, focusing on products that can become "killer products." The platform currently offers a variety of categories, including home, transportation, electronics, entertainment, apparel, sporting goods and personal care. We have strict requirements and high standards for all merchandise listed on Youpin. We offer our customers an experience of unique brand identity, premium quality and high value, as well as a simple sleek look that shares a similar design philosophy to our own brand series products. Youpin product placement is acknowledged as a validation of quality and style. As a result, our merchants know that placing products on Youpin will improve brand recognition and likely increase sales.

*Third-party Online Distribution Partners*

We sell our products through a global online distribution network comprising of third-party e-commerce partners. In mainland China, we cooperate with major e-commerce players such as JD.com who directly purchase our products and subsequently distribute the products to end users. In overseas markets, the third-party e-commerce marketplaces on which our products are sold include Flipkart and Amazon. We believe that the online distribution of our products through these leading e-commerce players enables us to take advantage of their established customer base and brand recognition and helps us reach a wide group of customers in a variety of global markets.

***Offline***

For offline, we primarily sell our products through our own retail stores, Mi Homes, directly to our users and through a third-party distribution network comprising of (i) cellular network carriers in mainland China, (ii) retail chains and local authorized stores in mainland China, and (iii) overseas distributors, including wholesale distributors, cellular network carriers, and authorized stores. As a key part of our offline retail strategy, we endeavor to work with no more than one distribution intermediary to ensure distribution efficiency, competitive retail pricing and great user experience.

*Direct Offline Retail*

As an integral part of our new retail strategy and to ensure a consistent satisfactory shopping experience for our products, we have built a large network of offline retail stores called Mi Homes. In mainland China, our Mi Homes footprint covers substantially all provinces and municipalities. We typically operate our Mi Homes in large cities in mainland China.

Our Mi Homes are typically located at high-traffic locations in quality shopping malls and urban shopping districts. The stores are designed to enhance the presentation and marketing of our products and services. Our in-store personnel are well-trained and knowledgeable on our products. Also, we believe that direct interaction with our targeted customers is an effective way to demonstrate the advantages of our products. To enhance customer experience and our operational efficiency, we do not incentivize or encourage our in-store personnel to promote our products or services to potential customers in an unsolicited manner.

*Third-Party Offline Distribution Network*

We distribute our products through cellular network carriers in mainland China, including China Mobile, China Unicom and China Telecom. In a number of European countries and other overseas markets, we have also partnered with local cellular network carriers to distribute our products.

In addition, we collaborate with consumer electronics retail chains and local authorized stores to distribute our products. Our retail chain partners include leading national brands and regional players, and we typically enter into a non-exclusive framework agreement with each retailer and sell our products to retailers on a per-order basis.

We do not commit to repurchase our products from the retailers or local authorized store owners. We recommend a minimum price on the resale of our products. Our retailers and local authorized store partners are our customers rather than agents, because once we have sold and delivered our products to them, they bear the risks of damage and obsolescence and they may not return the products unless they are defective according to the relevant applicable laws.

For selected international markets, our wholesale distribution partners distribute our products to other sub-distributors and retailers only within certain designated territories, and those sub-distributors and retailers will subsequently sell our products to end users. Our wholesale distributors are typically specialized in the distribution of smart hardware and operate well-established local distribution networks.

**Internet Services**

Given our vast, diverse and highly engaged user base, we are well positioned to broaden our services. Since our inception, we have focused on improving the integration of our products and internet services and the connectivity between our devices in order to provide a better user experience. As a result, we have achieved a high level of user engagement and retention. In addition to MIUI, we also provide internet services to users on other operating systems. These services include Mi Store, Youpin, Mi Home and Mi Fit. By offering these internet services, we expand our user base and enrich our entire ecosystem.

***MIUI***

MIUI is our proprietary operating system built on the Android kernel, which fully embraces and is compatible with the Android ecosystem. All Android apps are compatible with MIUI.

We developed the first version of MIUI based on the Android operating system in 2010 with significant customization and localization to adapt to consumers' user habits. Since then, MIUI has achieved high popularity among users attributable to its intuitive, fast and stable features. We made beta versions available to users every week to gather feedback and recommendations ahead of stable version updates, based on which we analyze and improve the system and have developed numerous features and optimizations to enhance its basic framework, usability and user experience. As a result, MIUI has attracted a massive user base with active user engagement.

MIUI supports a comprehensive suite of functionalities for our smartphones and provides a wide array of customized services to our users and developers to address their needs. For example, Mi Push is a stable, reliable and efficient notification service that provides a system-level message notification solution for users and developers not only on MIUI but also on other Android- and iOS-based platforms.

MIUI pre-installed on our smartphones shipped internationally may vary from our domestic versions, with system framework, design and customization catered to the local markets.

***Mi Cloud***

Mi Cloud is our cloud storage and cloud computing service that provides users with a one-stop solution to address the needs of personal data storage and backup. Seamlessly integrated with our products such as our smartphones, Mi Cloud offers a comprehensive and convenient storage service for user data, including data in a user's contacts, messages, photos, videos and documents. Mi Cloud synchronizes each individual user's data on different devices and keeps the data updated across all devices through a unified online account. Any changes to the stored data are automatically synchronized regardless of the device on which the change is made, making data migration easier. Mi Cloud backs up scalable user data automatically when a device is connected to Wi-Fi, and it possesses a broad set of features that enable multiple devices to operate faster, more securely, and save substantial costs.

***Mi App Store***

Mi App Store is our distribution platform for Android-based mobile apps. Mi App Store allows users to browse, search and obtain various mobile applications for mobile devices, and through these applications access the mobile internet on a secure and user-friendly platform. Through various apps, users can conveniently obtain internet content such as video, music, games and e-books. We leverage our proprietary development skills and technologies and have established strong relationships with app developers and content providers to provide a large quantity of mobile apps and other content on our Mi App Store.

***Mi Browser***

Our Mi Browser provides our users with a fast and secure browsing experience. Mi Browser can automatically block malicious websites, identify them among search results and scan files downloaded through the browser for security threats. Mi Browser also offers a "private browsing" option to allow users to surf the internet without leaving historical access records. Mi Browser features user-friendly user interface and functions. For example, users can store their bookmarks on our Mi Cloud and access the bookmarks whenever they want and wherever they are through a mobile device. Also, Mi Browser offers password managers to help users easily access multiple personal accounts on different online services through a secure cloud-based system.

***Mi News Feed***

Mi News Feed is a comprehensive content distribution platform, providing our smartphone users with high-quality, timely and customized streams of news articles and short videos. Mi News Feed operates through easily accessible portals including the mobile web browser and content center installed on our smartphones. In cooperation with leading providers of content providers to ensure high-quality user experience, Mi News Feed provides tailored content delivery services based on AI-powered analytics of our users' content consumption habits.

***Mi Security***

Mi Security is an internet security application that we offer our users for free. It incorporates anti-virus, anti-malware, anti-phishing, malicious website blocking and secure online shopping functions in a single lightweight installation package and leverages the power of our cloud-based data analytics engines to protect our users against security threats and malicious applications. The app can perform periodic or on-demand scan of program files on our users' devices and test them against our cloud-based security threats database.

***Mi Game Center***

We seek to cooperate with leading game producers as well as individual developers to provide our users with the broadest selection of games. Users can find the latest action blockbusters as well as popular leisure games. We customize the display of the homepage and ranking of the games based a variety of factors, including each user's individual taste and preference by leveraging our big data analytics capabilities. Therefore, users get a curated selection of games and individualized gaming experience. In addition, we offer live streaming services designed for gamers to create, share and discover a broad range of mobile game-related content. Users can interact with live streaming hosts by commenting on the content or by sending virtual gifts.

***Mi Video***

Mi Video is our main video content distribution platform on smartphones, with content sourced from third parties. We have been expanding and diversifying our content library to make premium content available to our users, achieved through partnership with major content providers. Mi Video is a one-stop portal for users to access both trending and recommended content. Leveraging our big data analytics, we analyze user browsing behavior to understand their tastes and preference, and dynamically update the content shown on the home page to offer users with the most desirable content. Our interface offers comprehensive viewing functions designed to enhance user experience. Our membership services generally provide paid subscribing members with a superior entertainment experience that is embodied in various membership privileges.

***Mi Music***

Our music distribution platform features large selections from popular artists and albums sourced from third parties. Our users have access to a vast array of music from both popular Chinese and international artists. Our music library spans across all major music genres such as pop, R&B, classical and traditional Chinese. We also offer podcasts and talk shows that users can subscribe to. Mi Music caters to diverse listening needs through improved search functions and AI-enabled personalized recommendations. We suggest playlists based on a variety of factors, including users' previous music selections and listening habits, time of the year or holidays and location.

***Our finance related business***

We commenced our internet finance business in 2015. Since then, we have developed innovative financial products and internet payment platforms to meet our users' diverse financial needs. Our loan products include installment purchase loans, which allow users to finance purchases of our hardware, and consumer loans, which allow users to satisfy their other financial needs. We distributed our loan products mainly through our Airstar Finance, Airstar Wallet and Airstar Loans mobile apps. In addition to our loan products, Airstar Wallet has mobile wallet and payment functions such as money transfer and bill payment functions. In addition, we provide supply chain financing services to our ecosystem partners as well as our upstream partners. On October 18, 2020, we rebranded our fintech business as "Airstar Digital Technology". It focuses on three main areas: Supply Chain Finance, Retail Finance, and Financial Technology. Drawing on our technological capabilities in big data and AI, Airstar Digital Technology will provide financial services to an increasing base of companies and retail consumers, and empower digital transformation of financial institutions.

***Monetization***

Currently we monetize our internet services primarily in mainland China and focus on advertising and internet value-added services. We have been building internet service monetization capabilities in overseas markets. Our monetization approach is to emphasize long-term sustainable monetization capabilities without compromising our exceptional user experience. With our continuous efforts to diversify our internet services business, our internet services revenue outside of advertising and gaming from mainland China smartphones, including those generated from the Youpin e-commerce platform, fintech business, TV internet services and overseas internet services, increased by 39.5% year-over-year and accounted for 39.0% of our total internet services revenue in the second quarter of 2020.

Our hardware creates a platform for users to engage with our internet services, which in turn we monetize through advertising and a wide range of internet value-added services. We use our proprietary technologies and big data analytical capabilities to offer comprehensive and innovative services to our business partners and users.

*Advertising*

Our advertising distribution channels primarily include our mobile apps and smart TVs. We offer diverse types of advertising formats to our advertising customers, such as display and performance-based advertising, to suit their particular business needs and marketing goals. Utilizing our robust big data analytics and AI capabilities, we customize the look, feel and timing of the display of the marketing messages to allow their seamless integration into content without compromising user experience. Our advertising customers cover diverse industries, ranging from auto and consumer goods to internet services and financial services, and they place advertisements directly with us or by engaging advertising agencies and resellers that in turn enter into contracts with us. We generate advertising revenue from this marketing distribution channel primarily by offering display-based and performance-based advertisement services. For display-based advertising services, we typically charge advertising customers based on the length of time during which the advertisements are displayed on our internet platform. For performance-based advertising services, we typically charge advertising customers on a per-click basis when the users click on the content, on a per-impression basis when the advertising content is displayed to users, or on a per-download basis, when the third-party app is downloaded by users. Our other advertising services primarily include pre-installation of mobile apps from third-party app developers on our smartphones. Our automated marketing functionalities for advertisers empower performance-based marketing throughout our mobile apps. We offer a suite of analytical tools to help our advertising customers to evaluate the performance of their ads and improve key metrics such as click-through rate. We allow e-commerce advertising customers to integrate their catalog into our platform, leading to more precise targeting and pushing of their products. Our big data technologies enable a real-time and dynamic bidding process by analyzing bidding price and click-through rates of the advertisements, which facilitate market making and improve monetization. Through the use of aggregated behavioral targeting data and analytics, we continually improve the effectiveness of our online marketing services for our advertising customers. Our overseas advertising business has also been rapidly developing, as we expanded our advertiser base and attracted increasing advertising budgets, with support of our strong smartphone shipments abroad.

*Gaming*

A sizable portion of our internet value-added service revenues was derived from online games. We offer streamlined digital sales, distribution and operational support services to third-party game developers. We offer a broad range of operational support to our third-party game developers, in a joint effort to enhance user engagement and increase monetization. For example, we closely monitor and analyze the key performance metrics of a game, including daily active users, average daily time online, paying user conversion rate and retention rate. Based on these metrics and leveraging our big data capabilities, our games operation team actively identifies areas for improvement and offers diagnostic advice to game developers. We also design promotional activities to help game developers gain more exposure and improve performance. We seek to maintain close and mutually beneficial relationships with key game publishers. Most of the games on our platform are free-to-play. We primarily generate revenue from sales of virtual currency that can be spent on the purchase of virtual items for use in the games we operate, which is subject to revenue-sharing arrangements with third-party game developers.

*Other Value-added Services*

We have made solid progress in recent years in developing other diverse forms of monetization for our internet value-added services, which primarily include our fintech business, paid subscription by users of premium entertainment content (such as online videos) and Youpin e-commerce platform. In January 2020, we successfully obtained a consumer finance license from the China Banking and Insurance Regulatory Commission. On October 18, 2020, we rebranded our fintech business as "Airstar Digital Technology". Our TV internet services also has maintained strong traction, driven by the solid performance of our subscription business. The Youpin e-commerce business has also grown robustly, as we have enlarged our merchandise portfolio, insisted on selecting high quality goods that appeal to our customers and increased our efforts in new customer acquisition.

## Global Operations

As of September 30, 2020, we have sold our products in over 90 countries and regions across five continents. Geographically, we generated 28.0%, 40.0%, 44.3% and 50.5% of our revenues in overseas markets in 2017, 2018, 2019 and for the nine months ended September 30, 2020. In the third quarter of 2020, our revenue from overseas markets increased 52.1% year-over-year to RMB39.8 billion. This marks a record high quarterly overseas revenue and overseas revenue contribution to our total revenue.

In the third quarter of 2020, we achieved strong growth in major markets across the globe. According to Canalys, in the third quarter, our smartphone shipments in Western Europe increased 107.3% year-over-year, achieving a market share of 13.3%, and ranked top 3 in the region for the first time. In particular, we retained the top spot in Spain in smartphone shipments for the 3rd consecutive quarter with a 33.9% market share. We also increased our smartphone shipments by over 100% year-over-year in France, Italy and Germany. Additionally, we accounted for 26.9% of the smartphone shipments in Central and Eastern Europe in the third quarter of 2020, attaining the 2nd position in the region. In particular, we ranked 1st in Poland and Ukraine and 2nd in Russia in terms of smartphone shipments. Moreover, we realized rapid growth in various other markets around the world. According to Canalys, we ranked 3rd globally in terms of smartphone shipments in the third quarter of 2020.

According to Canalys, in Latin America, our smartphone shipments jumped 471.4% year-over-year, attaining the 4th position with a 9.0% market share; in the Middle East, our smartphone shipments advanced by 156.7% year-over-year, ranking us 3rd with a 17.4% market share; in Africa, our smartphone shipments surged 197.5% year-over-year, and achieved the 3rd position with a market share of 10.7%. Furthermore, in the third quarter of 2020, we maintained our number 1 position in India, capturing a market share of 26.1% by smartphone shipments, according to Canalys.

We strengthened our existing channel networks and made significant progress in cellular carrier channels. As of September 30, 2020, we established partnerships with more than 50 carriers, covering over 100 sub-networks in 50 countries. In the first 9 months of 2020, our smartphone shipments via carrier channels grew by over 200% year-over-year. According to Canalys, our carrier channel market share in Western Europe increased from 2.3% in the third quarter of 2019 to 4.6% in the third quarter of 2020. With the growing penetration rate of e-commerce in overseas markets, our long-standing advantages in e-commerce channels also continued to expand. In the first 9 months of 2020, we shipped over 10 million smartphones to overseas markets excluding India via e-commerce channels.

As overseas markets are a strong growth driver for us, we will continue to invest heavily in them, expand our sales channels through strengthening our cooperation with local partners, and export our competitive products and services to more countries and regions. For risks relating to our overseas operations, see "*Risk Factors – Risks Relating to Our Business and Industry – Our business is subject to the risks of overseas operations*."

## Customer Service

Providing great customer service is a high priority for us. Our commitment to users is reflected in the high levels of service provided by our customer service staff as well as in our product return and exchange policies. We operate customer service centers around world, handling user queries and complaints regarding our products and services. Users can make queries on our products and ordering process and file complaints around the clock by various means, such as online chatting, a customer service hotline, online written instant messages through Xiaomi official accounts in WeChat and Weibo, and emails.

## Marketing and User Engagement

### *Branding and Endorsements*

Since our inception we have emphasized the value of customer feedback and direct communication with our users. We do not have very large selling and marketing expenses for a company of our size. Instead, we rely on word-of-mouth marketing through continual offering of killer products. We have fostered a large, active and loyal user base. In order to reach a wider customer base, we engage popular celebrities as brand ambassadors for our products and sponsor popular variety shows.

***Community and Engagement***

We have a close-knit user community that shares our core values. They actively participate in our Mi Community, MIUI forum, various other social media platforms, our research and development initiatives and offline activities. We cultivate and support the growth of our user community through close interaction with our users, especially Mi Fans, and actively listening to their feedback. We have adopted a user-centric research and development approach. Mi Fans can directly provide our engineers and developers with valuable suggestions and insights, which enables us to capture user demand and market trends in a timely and precise fashion.

Mi Community and MIUI forum are our official online discussion forums where users can share thoughts and experience, discover new functionalities and make recommendations for improvements for our products and services. Our engineers regularly participate in our online discussion forums to respond to users' queries and understand users' evolving needs. We also maintain various official social media accounts to actively engage with the users by addressing their questions and concerns. Our news channel on Mi Community publishes the latest news and updates about our Company and products. Our users also engage with us through other social media platforms.

Our offline events are nicknamed "Mi Pop." These events range from Mi Fan meet-ups to sporting events to dinner parties with our management teams. Mi Fans often take the initiative in planning and organizing these events to promote Mi Fan pride. Our close-knit and vibrant Mi Fan community is highly visible. Such events generate significant buzz on social media. We greatly benefit from word-of-mouth marketing and referrals by our passionate Mi Fans.

**Data Privacy and Protection**

We are committed to protecting our users' personal information and privacy. We believe it is crucial that our users understand how we handle their information so that they can make informed choices in deciding how such information is used and shared. To this end, we collect personal information and data from users only with their prior consent, and we offer our users opt-out or opt-in options.

We have established a strict company-wide policy on data collection and processing and have implemented a network of process and software controls to preserve individual personal information and privacy. We prioritize user data security and privacy by strictly following our defined policy.

**Technology and IT Infrastructure**

***5G and Technology Development***

We formed the Standards and Advanced Technology Department in 2015 to participate in the formulation of international, domestic and enterprise standards that are important to our businesses.

We are one of the few smartphone companies with 5G simulation capability in the industry. We actively participate in the formulation of 5G and 5G-related telecommunication standards, and have also participated in the research of 6G technology. We are a member of many important international standardization organizations including but not limited to GSMA, WPC, IEEE and 3GPP, with our experts holding leadership positions in many of these organizations. We have submitted a large number of research papers to these organizations to share our technological breakthroughs and industry insight.

***Cloud Computing***

Our sophisticated and strong cloud computing capability empowers us to provide differentiated services to our users and supports our continuous data analytic efforts. For individual users who grant consent to us, we leverage our cloud computing technology to store and analyze user data and provide tailored services to our users to enhance user experience. Through its capability to gather and analyze user data and user behaviors, our cloud computing technology serves as a universal analytics and processing engine that optimizes the functionality of our products in frequent and important user scenarios, thus enhancing the competitiveness of our products. For example, we design and develop customized optimization of our products for users in various countries and regions based on their different photo-shooting habits.

In addition, our cloud computing technology enables our ecosystem partners to conduct their business operation with security. Connecting to our enterprise cloud helps our partners achieve real-time storage and data backup and enables high-capacity and scalable data processing in an efficient, cost-effective and flexible manner. Our cloud computing also supports emerging applications so that IoT hardware can compute locally at the edge, while leveraging the cloud for global collaboration and machine learning at scale.

***Big Data***

Our data scientists specialize in data pre-processing, data modeling and data mining, as well as the creation of customized data analysis. Our big data processing and advanced algorithm capability enables us to analyze massive amount of data, based on which we design and tailor more innovative products and services to better serve and create value for our users. With prior user consent, we collect various types of data, such as logs, user behaviors and patterns, from products and services across our platform. All data is pooled into one platform for ease of analysis and is further categorized into multiple layers, each requiring different level of access authority. Our different operational departments can access the data on an as-needed and real-time basis with user consent, and utilize the data to improve their respective function and performance.

***Artificial Intelligence***

Our AI technology team is responsible for developing and refining our proprietary computational algorithms and machine learning capabilities, and applying the latest AI technology in our products and services. Our engineers incorporate open source software with our robust proprietary technology to form an enterprise-grade platform to deliver an integrated suite of capabilities for data management, machine learning and advanced analytics. We have successfully applied our advanced AI capabilities in various aspects of our business to improve both user experience and monetization opportunities.

*Computer Vision*

Our computer vision technology uses advanced algorithms and precisely detects, identifies and recognizes objects, scenes, images and faces, providing users with functionalities such as face detection and photo classification. Our facial recognition technology, the core of our computer vision technology, forms a positive feedback loop with our users' activities such that an increasing amount of user data further improves the precision and efficiency of our algorithm. The entire process is based solely on collected user behavioral statistics and does not involve users' data privacy.

Our face detection technology accurately and rapidly detects the location and the number of faces in photos. Our facial point detection technology can quickly and precisely locate key facial features and compositions. We have also developed advanced capabilities in facial boundary detection, face color optimization, portrait segmentation and white-balance optimization. These technologies enable our smartphones to take portrait photos with bokeh effects even with one single camera. Our visual recognition app is capable of recognizing and identifying different real-life objects, such as flowers, plants, vehicles, foods, celebrities, animals, arts and posters, and facilitating our users to acquire relevant information or image or to browse similar commercial products related to the objects identified. Our image understanding algorithm applies deep learning to classify and segment image content, thereby providing users a variety of powerful tools, such as sky replacement, portrait retention, etc.

*Speech Recognition and Natural Language Processing*

We develop our leading speech recognition and natural language processing (NLP) technologies under our proprietary testing standards and certification system. Our speech recognition capabilities feature highly accurate and speedy recognition and translation of spoken language into text, which builds the bedrock for further processing and analysis. Our machine translation system is trained on massive parallel corpus and achieves high accuracy for languages pairs. With sophisticated algorithms applied to a variety of daily user scenarios, we continuously improve and expand the application of voice control, both by our own team and third-party developers.

Our AI voice assistant is able to adapt to users' individual language usages, searches, and preferences and carry on conversations intelligently with users and respond to a range of customized queries. As a virtual assistant, it is able to recognize user voice and possesses contextual knowledge of user information to complete a variety of daily tasks assigned by users. Connected through our AI platform, our AI speaker can also interact with our apps and third-party apps to provide services such as navigating and ordering products from Mi Store. Our cloud-based open platform enables third-party developers to code and program new voice-controlled software and skills for our voice-enabled AI speaker. Our AI voice assistant has been built into multiple devices including smartphones, smart speakers, smart TVs, smart watches, and smart alarm clocks. Our AI voice assistant is capable to perform a wide range of functions from turning on lights, adjusting temperature of the air conditioner, controlling vacuum cleaners, checking weather condition, playing music, to telling children's stories. At the annual Mi Developer Conference (MIDC 2020) held in November 2020, we introduced our latest "XiaoAi AI Assistant 5.0", offering full-scenario intelligent collaboration, conversational active intelligence, customized voice with emotions, multi-modal visual capabilities, and smart learning assistance.

*Search and Recommendation*

Leveraging our AI technology, we have developed a high-quality search and personalized recommendation system for our internet services, allowing users to access what they need anytime, anywhere, including information, applications, games, music, videos and merchandises. Through machine learning techniques, our system is able to better understand content and extract semantic tags, which provide more relevant search results to our users. For example, when our user searches for certain content, our system first identifies the query intent based on the searched term, and then matches and returns the content that best meets the user's intention through search sorting algorithms. When the user does not have a clear search intention, our system predicts the content that the user may be most interested in based on user profile and previous search history. Currently our search and personalized recommendation system powers our various internet services.

***IT Infrastructure***

Our network infrastructure is designed to satisfy the requirements of our operations, to support the growth of our business and to ensure the stability of our operations as well as the security of information on our internet platform. We continuously develop our platform to offer users an effortless and seamless experience across all of our internet services, while at the same time enhancing the reliability and scalability of our internet platform.

*Cloud Services*

We use virtual machines, computing, storage, network and other infrastructure services in cooperation with a number of major public cloud service providers to ensure smooth business operations. Our system infrastructure is hosted in data centers in scattered regions with backup storage provided by databases of our cloud service providers. We have implemented multiple layers of redundancy to ensure network reliability and a working data redundancy model to conduct daily complete database backup. Our data storage services can be efficiently switched between multiple cloud providers across regions.

*Information Security*

We are committed to maintaining a secure platform and protecting our users' information security. We have established an information security management system in line with ISO27001 international information security standards, and manage the company's information security from various aspects including security organization, security policies, and technical control. We have also established company-wide privacy protection system in accordance with ISO29151 and ISO27018 international privacy standards, safeguarding data security for our users on various respects such as privacy policies, privacy assessments, and privacy protection technologies. We have established an information security and privacy committee responsible for formulating our security and privacy policies.

We have a dedicated security and privacy team to provide technical support for the security and privacy protection functions of our products and services. Our network and application systems use defense-in-depth security system, which features network isolation, network boundary access control, remote access multi-factor authorization, security protocol transmission for application programs and cloud server application. We have also implemented security baseline check, strict password enforcement policies, and regular review mechanism. Our multi-layer security technology automatically defends against malicious attacks every day and secures the security of our users' data in various scenarios. In terms of privacy protection, we use a privacy white paper for our products and services to maintain records of personal data processing and use an automated privacy compliance testing platform.

**Research and Development**

As the industry which we compete in is characterized by rapid technological advances, our ability to compete successfully depends on our ability to develop and introduce new products, services and technologies to the market. We are passionate about developing innovative technologies and continuous upgrading and improving the functionality and features of our technology infrastructure to enhance existing products and services and expanding the range of our offerings through in-house research and development, licensing of third-party intellectual property and acquisition of third-party businesses and technology.

In August 2020, we unveiled the 3$^{rd}$ Generation Under-screen Camera Technology. The smartphones equipped with this new camera technology have front-facing camera under the screen, providing a perfect full-screen design and ensuring a superior selfie experience. In October 2020, we debuted our 80W Mi Wireless Charging Technology that enables full wireless charging of a 4,000mAh battery in 19 minutes. This cutting edge technology again spearheads the wireless charging solutions in the industry.

In November 2020, we introduced the Retractable Wide-aperture Lens Technology, which features a retractable optical structure allowing a larger aperture to increase the amount of light intake by 300%. This complements the new anti-shake technology that provides a more stable image display with a 20% increase in definition and clarity.

As of September 30, 2020, our research and development personnel, totaling 10,480 employees, were staffed across our various departments. Our research and development team comprises industrial design engineers, electrical engineers, mechanical engineers, computer scientists, software engineers and mobile app developers. In 2021, we will continue to advance our investment and recruit more engineers to strengthen our R&D capabilities. We look to further broaden Xiaomi's technological frontier across key areas, including camera imaging, screen display, fast charging/wireless charging, audio, IoT platform and connectivity, AI and voice interaction, 5G/6G, Big Data and cloud-based services, digitalization and workflow management system, and smart manufacturing.

**Intellectual Property**

Intellectual property rights are fundamental to our business, and we devote significant time and resources to their development and protection. We currently hold a broad collection of intellectual property rights relating to certain aspects of our in-house designed and ecosystem hardware products, software and internet services. Such rights include trademarks, copyrights, domain names, trade names, trade secrets, patents and other proprietary rights in mainland China and a number of overseas jurisdictions. For ecosystem hardware products, we typically exclusively hold the intellectual property rights relating to the design of such products and hold joint ownership over the intellectual property rights relating to the technology arising from the joint research and development of such products with our ecosystem partners. With our prior written consent, our ecosystem partners are allowed to license jointly-owned intellectual property rights to a third party, and use such intellectual property rights to develop and manufacture products of their own brands with features that can be easily differentiated from ours. We have entered into worldwide intellectual property cross license agreements with a number of global technology leaders in the mobile telecommunications market. See "*Risk Factors – Risks Relating to Our Business and Industry – We rely on access to third-party intellectual property, which may not be available to us on commercially reasonable terms or at all.*"

***Intellectual Property Protection***

The protection of our trademarks, copyrights, domain names, trade names, trade secrets, patents and other proprietary rights is a strategic priority for the sustainable development and growth of our business. We regularly file patent and other proprietary rights applications to protect innovations arising from our research, development and design, and are currently pursuing thousands of intellectual property applications around the world. In particular, we have accumulated a large portfolio of issued patents, including utility patents, design patents and others, in mainland China and various countries and jurisdictions internationally.

We rely on a combination of patent, trademark, copyright and other intellectual property protection laws in mainland China and other jurisdictions, fair trade practice, as well as confidentiality procedures and contractual provisions to protect our intellectual property. In general, our employees must enter into a standard employment contract that includes a clause acknowledging that all inventions, trade secrets, developments and other processes generated by them on our behalf are our property, and assigning to us any ownership rights that they may claim in those works. Despite our precautions, third parties may infringe our intellectual property rights. Unauthorized use of our intellectual property by third parties and the expenses that may incur in protecting our intellectual property rights from such unauthorized use may adversely affect our business and results of operations. See "*Risk Factors – Risks Relating to Our Business and Industry – We may not be able to prevent others from unauthorized use of our intellectual property, which could harm our business and competitive position.*"

**Suppliers of Raw Materials, Components, Finished Products and Internet Services**

***Procurement***

We procure raw materials and components from top-tier suppliers for the production of our in-house products based upon a forecasted production plan and outsource the assembly of our in-house designed products to our outsourcing partners. We closely collaborate with our ecosystem partners to jointly design and develop hardware products, and our ecosystem partners supply finished products to us for sale and distribution to our customers.

Although most raw materials and components essential to our in-house products are generally available from multiple sources, a few components are currently sourced from a single or limited number of high quality suppliers in the industry. Therefore, many raw materials and components used by us, including those that are available from multiple sources, may at times be subject to industry-wide shortage and significant pricing fluctuations. See "*Risk Factors – Risks Relating to Our Business and Industry – Future operating results depend upon our ability to obtain raw materials, components and products in sufficient quantities on commercially reasonable terms.*"

We use certain custom components for our in-house designed products that are not commonly used by our competitors, and new products introduced by us often source custom components available from only a single or limited number of suppliers. When a component or product uses new technologies, initial capacity constraints may exist until a supplier's yields have matured or manufacturing capacity has increased. Continued availability of these raw materials and components at acceptable prices, or at all, may be affected if those suppliers decide to concentrate on the production of common components instead of components customized to meet our requirements.

**Assembly**

A substantial majority of our in-house products are currently assembled by our outsourcing partners in mainland China, and some of such products are assembled in India and Indonesia in compliance with the relevant local regulations. Our outsourcing partners produce our products using design specifications and standards established by us. We possess the key patents and technologies in relation to our hardware production. Our partners specialize in the assembling of electronic devices, and we believe they are experienced and well-positioned to meet our volume, cost and strict quality requirements.

Our outsourcing partners assemble hardware devices using components and raw materials primarily sourced and procured by us. Our engineers and other quality assurance professionals monitor the assembling process and compliance with all of our protocols. We believe that outsourcing assembling affords us greater scalability and flexibility than establishing and maintaining our own assembling facilities. We periodically evaluate the necessity and benefit of working with additional outsourcing partners to support our operations.

In August 2020, we introduced our smart factory in Beijing. Through our smart factory, Xiaomi has developed advanced manufacturing equipment, including automated high-end smartphone production lines, and successfully mass produced Mi 10 Ultra Transparent Edition. Our smart factory serves to provide three key functions, namely (1) a smart factory with an annual production capacity of one million high-end smartphones; (2) a mega laboratory that engages in the research and development of new materials and cutting-edge technologies; and (3) an experimental base for the next-generation manufacturing equipment and automated production lines. The smart factory enables us to enhance control over the full production cycle across research and development, technology implementation, and manufacturing processes, fortifying our technological leadership.

**Strategic Investments**

Our success is based on our ability to create new and compelling products, services, and experiences for our users, to embrace disruptive technology trends, to enter new geographic markets, and to drive broad adoption of our products and services. Our investment strategy is (i) to deepen strategic cooperation with partners through investing and becoming active shareholders and (ii) to apply financial investment rigor and invest in only our best-in-class partners.

After years of effort, we have established a unique ecosystem business model for strategic investment. Leveraging our strong capabilities in R&D and product design, as well as our superior brand and sales networks, we empower our ecosystem partners and accelerate their growth, creating a win-win scenario. As of September 30, 2020, the Company had invested in more than 300 companies with an aggregated book value of RMB39.5 billion, an increase of 37.5% year-over-year. We believe our strategic investments have not only allowed us to forge close partnerships with investee companies to create synergies across our ecosystem, but have also provided us with stable and recurring investment income.

**Competition**

The markets for our products and services are highly competitive and we are confronted by aggressive competition in all areas of our business. These markets are characterized by frequent product introductions and rapid technological advances that have substantially increased the capabilities and use of mobile communication and media devices, laptops and other smart devices. We generally compete with other internet companies for user time spent. Principal competitive factors important to us include product features, relative price and performance, product quality and reliability, design innovation, software integration and user experience, marketing and distribution capability, service and support and corporate reputation. Our main competitors include domestic and global internet industry leaders, as well as major producers of smart devices.

We experience significant competition for highly skilled personnel, including management, engineers, designers and product managers. Our growth depends in part on our ability to retain our existing personnel and recruit highly skilled employees.

**Employees**

As of September 30, 2020, we had 20,881 full-time employees, 19,319 of whom were based in mainland China, primarily at our headquarters in Beijing, with the rest primarily based in India and Indonesia. We expect to continue to increase our headcount in mainland China and our key target global markets. As of September 30, 2020, our research and development personnel, totaling 10,480 employees, were staffed across our various departments.

Our success depends on our ability to attract, retain and motivate qualified personnel. As part of our human resources strategy, we offer employees competitive compensation packages. As of September 30, 2020, 15,846 employees held share-based awards. The total remuneration expenses, including share-based compensation expense, for the years ended December 31, 2017, 2018, 2019 and the three months ended September 30, 2020 were RMB4.1 billion, RMB17.1 billion, RMB8.3 billion and RMB2.5 billion, respectively.

As required under the regulations of the mainland China, we participate in various employee social security insurance programs that are organized by applicable local municipal and provincial governments, including housing, pension, medical, work-related injury and unemployment benefit insurance, under which we make contributions at specified percentages of the salaries of our employees.

**Insurance**

We maintain various insurance policies to safeguard against risks and unexpected events. We have purchased property insurance covering all risks of physical loss, destruction or damage to the inventory of our products and our fixed assets. We also maintain public liability insurance for our Mi Homes in mainland China to protect against a variety of claims, including bodily injury, property damage and personal injury, that may arise from the business operations of our Mi Homes. In addition, we have purchased construction all risks insurance for our Mi Homes under construction, which provides coverage for property damage and third-party injury or damage claims that may arise from the construction projects. We maintain product liability insurance for our ecosystem hardware products sold in North America. We also maintain trade insurance for our overseas transactions in certain other markets.

In line with general market practice, we do not maintain sufficient business interruption insurance, which is not mandatory under the relevant laws of the mainland China. We do not maintain sufficient key-man life insurance or insurance policies covering damages to our IT infrastructure or information technology systems. See "*Risk Factors – Risks Relating to Our Business and Industry – We have limited insurance coverage which could expose us to significant costs and business disruption.*"

**Properties**

We operate our businesses through our leased properties and owned properties in many countries and regions, including but not limited to mainland China, India, Indonesia, Russia, Hong Kong, Japan, Thailand, Vietnam, the Philippines, Bangladesh, Malaysia, Mexico, Spain, Poland, Italy, Germany, the Netherlands, UK, Finland, USA and UAE. Our leased and owned properties serve as our offices, Mi Home stores, research and development centers, customer service centers and other operational facilities. We have acquired land use rights for the construction of our office buildings in favorable locations in a number of cities in mainland China, including but not limited to Beijing, Guangzhou, Wuhan and Nanjing. We believe that we will be able to obtain adequate facilities, principally through the leasing of appropriate properties, to accommodate our future expansion plans.

**Legal Proceedings**

As of the date of this Offering Circular, we are not a party to any material legal or administrative proceedings. We have in the past and may from time to time be subject to various legal or administrative claims and proceedings arising in the ordinary course of our business. The majority of the legal proceedings involve intellectual property claims initiated by us to protect intellectual properties owned by or licensed to us. The legal proceedings against us include claims brought by other technology companies and smartphone manufacturers relating to intellectual property infringement. See the section headed "*Risk Factors – Risks Relating to Our Business and Industry – We could be impacted by unfavorable results of legal and administrative proceedings, such as being found to have infringed on intellectual property rights.*"

The following discussion summarizes certain aspects of mainland China, Hong Kong and Cayman law and regulations, which are relevant to our operations and business.

## REGULATIONS RELATING TO VALUE-ADDED TELECOMMUNICATION SERVICES

### Licenses for Value-Added Telecommunication Services

The Telecommunications Regulations of the People's Republic of China, or the Telecommunications Regulations, promulgated by the State Council on September 25, 2000 and last amended on February 6, 2016, provide a regulatory framework for telecommunications services providers in mainland China. The Telecommunications Regulations require telecommunications services providers to obtain an operating license prior to the commencement of their operations. The Telecommunications Regulations categorize telecommunications businesses into basic telecommunications businesses and value-added telecommunications businesses. According to the Catalog of Telecommunications Business, attached to the Telecommunications Regulations and last amended by the Ministry of Industry and Information Technology, or MIIT, on June 6, 2019, information services provided via fixed network, mobile network and Internet fall within value-added telecommunications services.

The Administrative Measures on Internet Information Services, or the Internet Measures, which was promulgated by the State Council on September 25, 2000 and amended on January 8, 2011, set out guidelines on the provision of internet information services. The Internet Measures classified internet information services into commercial internet information services and non-commercial internet information services, and a commercial operator of internet content provision services must obtain an ICP License for the provision of internet information services from the appropriate telecommunications authorities. The Administrative Measures for Telecommunications Businesses Operating Licensing, which was promulgated by MIIT on July 3, 2017 and became effective on September 1, 2017, provides that a commercial operator of value-added telecommunications services must first obtain an ICP License, from MIIT or its provincial level counterparts. In addition, in the first quarter of every year while the operator is holding the license, it must report information such as business performance and service quality to the issuing authorities.

### Restrictions on Foreign Investment

Foreign direct investment in telecommunications companies in mainland China is governed by the Regulations for the Administration of Foreign-Invested Telecommunications Enterprises, which was promulgated by the State Council on December 11, 2001 and amended on September 10, 2008 and February 6, 2016, respectively. The regulations require foreign-invested value-added telecommunications enterprises in mainland China to be established as Sino-foreign equity joint ventures, which the foreign investors may acquire up to 50% of the equity interests of such enterprise. In addition, the main foreign investor who invests in a foreign-invested value-added telecommunications enterprises operating the value-added telecommunications business in mainland China must demonstrate a good track record and experience in operating a value-added telecommunications business; the main foreign investor is defined as the one who makes the largest contribution among all foreign investors and has a share of 30% or more of the total amount invested by all foreign investors. Moreover, foreign investors that meet these requirements must obtain approvals from MIIT and MOFCOM, or their authorized local counterparts, which retain considerable discretion in granting approvals, for the commencement of that investor of value-added telecommunication business in mainland China.

In July 2006, the Ministry of Information Industry, or the MII, which is the predecessor of MIIT, released the Notice on Strengthening the Administration of Foreign Investment in and Operation of Value-added Telecommunications Business, or the MII Notice, pursuant to which, domestic telecommunications enterprises were prohibited to rent, transfer or sell a telecommunications business operation license to foreign investors in any form, or provide any resources, premises, facilities and other assistance in any form to foreign investors for their illegal operation of any telecommunications business in mainland China. In addition, under the MII Notice, the internet domain names and registered trademarks used by a foreign-invested value-added telecommunication service operator shall be legally owned by that operator (or its shareholders).

Investment activities in mainland China by foreign investors are mainly governed by the Special Administrative Measures for Access of Foreign Investment (Negative List) (2020 Edition), or the Negative List, which was promulgated jointly by MOFCOM and the NDRC on June 23, 2020 and became effective on July 23, 2020. Foreign investors shall not invest in any of the prohibited sectors specified in the Negative List; they must obtain the permit for access of foreign investments if they intend to invest in other sectors that are not prohibited; if they intend to invest in sectors subject to limits on the proportion of foreign investment, they are not allowed to establish foreign-invested partnerships. According to the Negative List, Telecommunications companies are limited to investment in the telecommunications business opened according to China's WTO accession commitments; the proportion of foreign investment in a value-added telecommunications business (excluding e-commerce business, domestic multi-party communications, store-and-forward and call center) shall not exceed 50 percent, and investment in internet news services, online publishing services, online audio-visual program services, internet culture operation (excluding music), and internet public-oriented information releasing services (excluding content of the abovementioned services that is permitted under China's WTO accession commitments) is prohibited.

## REGULATIONS RELATING TO MANUFACTURE AND SALE OF MOBILE PHONES

### General Administration of Manufacturing and Selling Mobile Phones

According to the Administrative Regulations for Compulsory Product Certification, which was promulgated by the General Administration of Quality Supervision, Inspection and Quarantine P.R.C., or the AQSIQ (which has merged into the State Administration for Market Regulation) on July 3, 2009, products specified by the state shall not be delivered, sold, imported or used in other business activities until they are certified, or the Compulsory Product Certification, and labeled with China Compulsory Certification mark. For products that are subject to Compulsory Product Certification, the state implements unified product catalogs, or the 3C Catalog, unified compulsory requirements, standards and compliance assessment procedures in technical specification, unified certification marks and unified charging standards. Pursuant to the First Batch Compulsory Product Certification Product Catalog, the First Batch 3C Product Catalog, by the AQSIQ and the Certification and Accreditation Administration of the People's Republic of China, or the CNCA, on December 3, 2001, mobile user terminals and CDMA digital cellular mobile station are required to obtain the Compulsory Product Certification in order to be delivered, sold, imported or used.

Besides the Compulsory Product Certification, the seller of radio component products in mainland China is required to obtain the Radio Transmission Equipment Type Approval Certificate in accordance with the Radio Regulation of the People's Republic of China, which was promulgated by the State Council, Central Military Commission on September 11, 1993, and amended on November 11, 2016, and the Administrative Regulations on Manufacturing of Radio Transmission Equipment, promulgated by the State Radio Regulation Committee, or the SRRC, and the State Bureau of Technical Supervision, or the SBTS, the predecessor of the AQSIQ on October 7, 1997.

In addition, the Administrative Measures for the Network Access of Telecommunications Equipment, which was promulgated by the MII on May 10, 2001 and revised by the MIIT on September 23, 2014 provide that the State applies the network access permit system to the telecommunications terminal equipment, radio communications equipment, and equipment relating to network interconnection that is connected to public telecommunications networks. The telecommunications equipment subject to the network access permit system shall obtain the Telecommunications Equipment Network Access Permit issued by the MIIT, or the Network Access Permit. Without the Network Access Permit, no telecommunications equipment is allowed to be connected to the public telecommunications networks for use nor sold on the domestic market. In the event of an application for the Network Access Permit, a production enterprise shall submit a testing report issued by a telecommunications equipment testing institution or a Compulsory Product Certification. In the event of an application for the network access permit for radio transmission equipment, a Radio Transmission Equipment Type Approval Certificate issued by the MIIT shall also be submitted.

**Regulations on Product Quality**

Products made in mainland China are subject to the Product Quality Law of the People's Republic of China, or the Product Quality Law, which was promulgated on February 22, 1993, amended on July 8, 2000, August 27, 2009 and December 29, 2018. According to the Product Quality Law, a manufacturer of a product is responsible to compensate for the damages to any person or property caused by the defect of such a product, unless the manufacturer is able to prove that: (i) it has not circulated the product; (ii) the defect did not exist at the time when the product was circulated; or (iii) scientific or technological knowledge at the time when the product was circulated was not such that it allowed the defect to be discovered.

The Consumer Rights and Interests Protection Law of the People's Republic of China, or the Consumers Protection Law, was promulgated on October 31, 1993 and became effective on January 1, 1994. The Consumers Protection Law has been further revised on August 27, 2009 and October 25, 2013. According to the Consumers Protection Law, unless otherwise provided by this law, an operator that provides products or services may bear civil liability in accordance with the Product Quality Law and other relevant laws and regulations. The Tort Law of the People's Republic of China, promulgated on December 26, 2009 and came into force on July 1, 2010, provides that in the event of damage arising from a defective product, the victim may seek compensation from either the manufacturer or seller of such a product. If the defect is caused by the seller, the manufacturer shall be entitled to seek reimbursement from the seller upon compensation to the victim. If the defect is caused by the manufacturer, the seller shall be entitled to seek reimbursement from the manufacturer upon compensation to the victim.

**Registration for Import and Export Goods**

Pursuant to the Customs Law of the People's Republic of China promulgated by the Standing Committee of the National People's Congress, or SCNPC on January 22, 1987 and amended on July 8, 2000, June 29, 2013, December 28, 2013, November 7, 2016 and November 4, 2017 unless otherwise stipulated, the declaration of import and export goods may be made by consignees and consignors themselves, and such formalities may also be completed by their entrusted customs brokers that have registered with the Customs. The consignees and consignors for import or export of goods and the customs brokers engaged in customs declaration shall register with the Customs in accordance with the laws.

Pursuant to the Administrative Provisions of the Customs of the People's Republic of China on the Registration of Customs Declaration Entities promulgated by the General Administration of Customs on March 13, 2014 and amended on December 20, 2017, coming into force on March 13, 2014, the registration of customs declaration entities comprises the registration of the customs declaration enterprise and the registration of the consignor or consignee of imported and exported goods. The consignor or consignee of imported and exported goods shall register with local customs in accordance with the laws.

## REGULATIONS RELATING TO MOBILE INTERNET APPLICATIONS INFORMATION SERVICES

Mobile internet application is governed by the Provisions on the Administration of Mobile Internet Applications Information Services, or Provisions on Administration of Application, promulgated by the Cyberspace Administration of China, or the CAC on June 28, 2016 and became effective on August 1, 2016.

Pursuant to the Provisions on Administration of Application, application information service providers shall obtain the relevant qualifications prescribed by laws and regulations, strictly implement their information security management responsibilities, and carry out the duties including to establish and complete user information security protection mechanism, to establish and complete information content inspection and management mechanisms, to protect users' right to know and right to choose in the process of usage, and to record users' daily information and preserve it for 60 days. Application store services providers shall, within 30 days of the business going online and starting operations, conduct filing procedures with the local cybersecurity and informatization department. Furthermore, internet application store service providers and internet application information service providers shall sign service agreements to determinate both sides' rights and obligations.

## REGULATIONS RELATING TO INFORMATION SECURITY AND CENSORSHIP

Internet content in mainland China is regulated and restricted from a state security standpoint. SCNPC enacted the Decisions on the Maintenance of Internet Security on December 28, 2000, which was amended on August 27, 2009, that may subject persons to criminal liabilities in mainland China for any attempt to: (i) gain improper entry to a computer or system of strategic importance; (ii) disseminate politically disruptive information; (iii) leak state secrets; (iv) spread false commercial information or (v) infringe intellectual property rights. In 1997, the Ministry of Public Security issued the Administration Measures on the Security Protection of Computer Information Network with International Connections, which were amended by the State Council on January 8, 2011 and prohibit using the internet in ways which, among others, result in a leakage of state secrets or a spread of socially destabilizing content. The Ministry of Public Security has supervision and inspection powers in this regard, and relevant local security bureaus may also have jurisdiction. If an ICP License holder violates these measures, the government of the People's Republic of China may revoke its ICP License and shut down its websites.

On November 7, 2016, the SCNPC promulgated the Cyber Security Law of the People's Republic of China, which became effective on June 1, 2017, pursuant to which, network operators shall comply with laws and regulations and fulfill their obligations to safeguard security of the network when conducting business and providing services. Those who provide services through networks shall take technical measures and other necessary measures pursuant to laws, regulations and compulsory national requirements to safeguard the safe and stable operation of the networks, respond to network security incidents effectively, prevent illegal and criminal activities, and maintain the integrity, confidentiality and usability of network data, and the network operator shall not collect the personal information irrelevant to the services it provides or collect or use the personal information in violation of the provisions of laws or agreements between both parties, and network operators of key information infrastructure shall store within the territory of mainland China all the personal information and important data collected and produced within the territory of mainland China. The purchase of network products and services that may affect national security shall be subject to national cyber security review. On May 2, 2017, the CAC issued a trial version of the Measures for the Security Review of Network Products and Services (Trial), which took effect on June 1, 2017, to provide for more detailed rules regarding cyber security review requirements.

## REGULATIONS RELATING TO PRIVACY PROTECTION

On December 13, 2005, the Ministry of Public Security issued the Regulations on Technological Measures for Internet Security Protection, or the Internet Protection Measures, which took effect on March 1, 2006. The Internet Protection Measures require internet service providers to take proper measures including anti-virus, data back-up and other related measures, and to keep records of certain information about their users (including user registration information, log-in and log-out time, IP address, content and time of posts by users) for at least 60 days, and detect illegal information, stop transmission of such information, and keep relevant records. In December 2012, the SCNPC promulgated the Decision on Strengthening Network Information Protection to enhance the legal protection of information security and privacy on the internet. In July 2013, the MIIT promulgated the Provisions on Protection of Personal Information of Telecommunication and Internet Users to regulate the collection and use of users' personal information in the provision of telecommunication services and internet information services in mainland China and the personal information includes a user's name, birth date, identification card number, address, phone number, account name, password and other information that can be used for identifying a user. On December 29, 2011, the MIIT promulgated the Several Provisions on Regulation of the Order of Internet Information Service Market, which became effective on March 15, 2012. The Provisions stipulate that without the consent of users, internet information service providers shall not collect information relevant to the users that can lead to the recognition of the identity of the users independently or in combination with other information, nor shall they provide personal information of users to others, unless otherwise provided by laws and administrative regulations. On May 8, 2017, the Supreme People's Court and the Supreme People's Procuratorate released the Interpretations of the Supreme People's Court and the Supreme People's Procuratorate on Several Issues Concerning the Application of Law in the Handling of Criminal Cases Involving Infringement of Citizens' Personal Information, which clarifies several concepts regarding the crime of "infringement of citizens' personal information" stipulated by Article 253A of the Criminal Law of the People's Republic of China, including "citizen's personal information," "provision," and "unlawful acquisition." Also, it specifies the standards for determining "serious circumstances" and "particularly serious circumstances" of this crime.

## REGULATIONS RELATING TO ONLINE GAMES

### General Administration of Online Games

The Notice on Interpretation of the State Commission Office for Public Sector Reform on Several Provisions relating to Animation, Online Game and Comprehensive Law Enforcement in Culture Market in the 'Three Provisions' jointly promulgated by the Ministry of Culture (which has merged into the Ministry of Culture and Tourism), the State Administration of Radio, Film, and Television, or SARFT (which has merged into SAPPRFT) and the General Administration of Press and Publication, or the GAPP, which was issued by the State Commission Office for Public Sector Reform (a division of the State Council) and became effective on September 7, 2009, provides that the GAPP will be responsible for the examination and approval of online games to be uploaded on the internet and that, after such upload, online games will be administered by the Ministry of Culture.

The Interim Measures for the Administration of Internet Games, the Internet Game Measures, issued by the Ministry of Culture on June 3, 2010, amended on December 15, 2017, regulate a broad range of activities related to the internet game business, including the development and production of internet games, the operation of internet games, the issuance of virtual currencies used for internet games, and virtual currency trading services. The Internet Game Measures provides that any entity that is engaged in internet game operations must obtain an online culture operating permit, and require the content of an imported internet game to be examined and approved by the Ministry of Culture prior to the launch of the game and the content of a domestic internet game must be filed within 30 days of its launch with the Ministry of Culture. The Internet Game Measures also request internet game operators to protect the interests of online players and specify certain terms that must be included in the service agreements between internet game operators and the players of their internet games. The Notice of the Ministry of Culture on the Implementation of the Interim Measure for the Administration of Online Games issued by the Ministry of Culture and which took effect on July 29, 2010 specifies entities regulated by the Online Game Measures and procedures related to the review of the Ministry of Culture of the content of online games, emphasizes the importance of protecting minors playing online games and requests online game operators to promote real-name registration by their players.

On May 24, 2016, SAPPRFT promulgated the Notice on the Administration over Mobile Game Publishing Services, which became effective as of July 1, 2016. The Notice provides that game publishing service entities shall be responsible for examining the contents of their games and applying for game publication numbers. On December 1, 2016, the Ministry of Culture promulgated the Circular of the Ministry of Culture on Regulating the Operation of Online Games and Strengthening the Interim and Ex Post Supervision, which became effective on May 1, 2017. The Circular sets requirements in relation to the following aspects of online games: (i) clarifying the scope of online game operation; (ii) regulating services for issuance of virtual props of online games; (iii) strengthening the protection of the rights and interests of online game users; (iv) strengthening the interim and ex post supervision of online game operation; and (v) seriously investigating and punishing illegal operating activities.

### Regulations on Anti-fatigue Compliance System and Real-name Registration

On April 15, 2007, in order to curb addictive online game-playing by minors, eight government authorities of the People's Republic of China, including the GAPP, the Ministry of Education, the Ministry of Public Security and the MIIT, jointly issued the Notice on Protecting Minors Mental and Physical health and Implementation of Online Game Anti-fatigue System requiring the implementation of an anti-fatigue compliance system and a real-name registration system by all Chinese online game operators. Under the anti-fatigue compliance system, three hours or less of continuous playing by minors, defined as game players under 18 years of age, is considered to be "healthy," three to five hours is deemed "fatiguing," and five hours or more is deemed "unhealthy." Game operators are required to reduce the value of in-game benefits to a game player by half if it discovers that the amount of time a game player spends online has reached the “fatiguing” level, and to zero in the case of the “unhealthy” level. To identify whether a game player is a minor and thus subject to the anti-fatigue compliance system, a real-name registration system should be adopted to require online game players to register their real identity information before playing online games.

**Regulations on Virtual Currency**

On June 4, 2009, the Ministry of Culture and MOFCOM jointly issued the Notice on Strengthening the Administration of Online Game Virtual Currency, or the Virtual Currency Notice. The Virtual Currency Notice requires businesses that (a) issue online game virtual currency (in the form of prepaid cards and/or pre-payment or prepaid card points), or (b) offer online game virtual currency transaction services to apply for approval from the Ministry of Culture through its provincial branches within three months after the issuance of the notice. The Virtual Currency Notice prohibits businesses that issue online game virtual currency from providing services that would enable the trading of such virtual currency. Any business that fails to submit the requisite application will be subject to sanctions, including, without limitation, mandatory corrective measures and fines.

**Restrictions on Foreign Investment**

The Notice Regarding the Consistent Implementation of the “Regulation on Three Provisions” of the State Council and the Relevant Interpretations of the State Commission Office for Public Sector Reform and the Further Strengthening of the Administration of Pre-examination and Approval of Online Games and the Examination and Approval of Imported Online Games, or the GAPP Notice, promulgated by the GAPP, together with the National Copyright Administration and the Office of the National Working Group for Crackdown on Pornographic and Illegal Publications, on September 28, 2009, provides, among other things, that foreign investors are not permitted to invest or engage in online game operations in mainland China through wholly-owned subsidiaries, equity joint ventures or cooperative joint ventures, and expressly prohibits foreign investors from gaining control over or participating in domestic online game operations indirectly by establishing other joint venture companies, establishing contractual agreements or providing technical support. Serious violation of the GAPP Notice will result in suspension or revocation of relevant licenses and registrations. On June 30, 2019, MOFCOM and the NDRC jointly issued the “Special Administrative Measures (Negative List) for Foreign Investment Access (2019 Version)”, according to which, foreign investment in telecommunications carriers are limited to the telecommunications services in the commitments made by China upon WTO accession. The foreign stake in a value-added telecommunications service may not exceed 50% (except e-commerce, domestic conferencing, store-and-forward, and call center services), and the Chinese party shall be a controlling stakeholder in basic telecommunications business.

## REGULATIONS RELATING TO INTERNET PUBLICATION

**License for Internet Publication**

On February 4, 2016, the GAPP and the MIIT jointly issued the Regulations on Administration of Internet Publication Services, the Internet Publication Regulations, which became effective on March 10, 2016. The Internet Publication Regulations imposed a license requirement, or the Internet Publishing Service License, for internet publishing activities.

**Restrictions on Internet Content**

The content of the internet information is also highly regulated in mainland China. On February 16, 2007, the GAPP promulgated the Notice of the General Administration of Press and Publication on Strengthening Review Work of Audio-visual Products and Electronic Publication Items and Internet Publication Items, pursuant to which GAPP shall strengthen the review of internet publication items, including

(i) annual topic plan review for those unpublished video and audio products and electronic publication,

(ii) special review and daily review for published video and audio products and electronic publication; and

(iii) regulation of internet publication content. According to the Internet Measures, violators who provide prohibited internet content may be subject to penalties, including criminal sanctions, operation suspension and rectification, or even revoking ICP Licenses.

Internet information service providers are also required to monitor their websites. Pursuant to the Internet Publication Regulations, the entities providing internet publication services shall adopt a system of responsibility for examination of the content of publications, an editor responsibility system, a proofreader responsibility system, and other management systems to ensure the quality of its web publications.

**Restrictions on Foreign Investment**

Investment activities in mainland China by foreign investors are mainly governed by the Catalog, which was promulgated jointly by MOFCOM and the NDRC on June 28, 2017 and became effective on July 28, 2017. The Catalog divides industries into four categories in terms of foreign investment. Those categories are: "encouraged," "restricted," "prohibited" and all industries not listed under one of these categories are deemed to be "permitted." According to the Catalog, the internet information services that the Company's subsidiaries in mainland China currently offer falls within the scope of value-added telecommunications services (except for e-commerce) and internet cultural businesses (except for music), which are under the "restricted" categories and "prohibited" categories, respectively. "Book editing" is under the "prohibited" categories as a newly added item.

**REGULATIONS RELATING TO INTELLECTUAL PROPERTY**

**The Copyright Law**

China has enacted various laws and regulations relating to the protection of copyright. China is a signatory to some major international conventions on protection of copyright and became a member of the Berne Convention for the Protection of Literary and Artistic Works in October 1992, the Universal Copyright Convention in October 1992, and the Agreement on Trade-Related Aspects of Intellectual Property Rights upon its accession to the World Trade Organization in December 2001.

The Copyright Law of the People's Republic of China (Revised in 2010), or the Copyright Law, provides that Chinese citizens, legal persons, or other organizations shall, whether published or not, enjoy copyright in their works, which include, among others, works of literature, art, natural science, social science, engineering technology and computer software. The purpose of the Copyright Law aims to encourage the creation and dissemination of works which is beneficial for the construction of socialist spiritual civilization and material civilization and promote the development and prosperity of Chinese culture.

Under the Regulation on Protection of the Right to Network Dissemination of Information that took effect on July 1, 2006 and was amended on January 30, 2013, it is further provided that an internet information service provider may be held liable under various situations, including if it knows or should reasonably have known a copyright infringement through the internet and the service provider fails to take measures to remove or block or disconnects links to the relevant content, or, although not aware of the infringement, the internet information service provider fails to take such measures upon receipt of the copyright holder's notice of infringement.

The Circular on Strengthening the Copyright Administration of Internet Literary Works promulgated by National Copyright Administration, or the NCA**,** on November 4, 2016 and effective from November 4, 2016 provides that internet service providers who provide literary works through information networks and render relevant network services shall strengthen the copyright supervision and administration, establish a sound infringing works handling mechanism, and fulfill the obligation to protect the copyright of internet literary works according to the law, shall fulfill the obligation to review the copyright of literary works disseminated and exercise their duty of care according to the law. Except as otherwise provided by laws and regulations, without the permission of right holders, the dissemination of their literary works shall be prohibited and shall establish a copyright complaint mechanism, actively accept complaints from right holders, and resolve the legitimate demands of right holders in a timely manner according to the law.

Measures on Administrative Protection of Internet Copyright, that were promulgated by the MII and NCA and took effect on May 30, 2005, provided that an internet information service provider shall take measures to remove the relevant contents, record relevant information after receiving the notice from the copyright owner that some content communicated through internet infringes upon his/its copyright and preserve the copyright owner's notice for 6 months. Where an internet information service provider clearly knows an internet content provider's tortious act of infringing upon another's copyright through internet, or fails to take measures to remove relevant contents after receipt of the copyright owner's notice although it does not know it clearly, and meanwhile damages public benefits, the infringer shall be ordered to stop the tortious act, and may be imposed of confiscation of the illegal proceeds and a fine of not more than 3 times the illegal business amount; if the illegal business amount is difficult to be calculated, a fine of not more than RMB100,000 may be imposed.

The Notice on Regulating Copyright Order of Internet Reproduction issued by the NCA in 2015 includes the following four major points: (i) clarify certain important issues related to internet copyrights in existing laws and regulations, including the definition of news, clarify statutory licenses that are not applicable to internet copyrights and prohibit the distortion of title and work intent; (ii) guide the press and media to further improve the internal management of copyrights, especially requesting the press to clarify the copyright sources of their content; (iii) encourage the press and internet media to actively carry out copyright cooperation; and (iv) ask the copyright administrations at all levels to strictly implement copyright supervision.

The Computer Software Copyright Registration Measures, or the Software Copyright Measures, promulgated by the National Copyright Administration on February 20, 2002, regulate registrations of software copyright, exclusive licensing contracts for software copyright and transfer contracts. The National Copyright Administration of China shall be the competent authority for the nationwide administration of software copyright registration and the Copyright Protection Center of China, or the CPCC, is designated as the software registration authority. The CPCC shall grant registration certificates to the Computer Software Copyrights applicants which conforms to the provisions of both the Software Copyright Measures and the Computer Software Protection Regulations.

**The Trademark Law**

Trademarks are protected by the Trademark Law of the People's Republic of China, which was promulgated on August 23, 1982 and subsequently amended on February 22, 1993, October 27, 2001, August 30, 2013 and April 23, 2019 respectively as well as the Implementation Regulation of the Trademark Law of the People's Republic of China (Revised in 2014) adopted by the State Council on August 3, 2002. In mainland China, registered trademarks include commodity trademarks, service trademarks, collective marks and certification marks.

The Trademark Office under the State Administration for Industry and Commerce, or SAIC (which has merged into the State Administration for Market Regulation), handles trademark registrations and grants a term of ten years to registered trademarks. Trademarks are renewable every ten years where a registered trademark needs to be used after the expiration of its validity term. A registration renewal application shall be filed within twelve months prior to the expiration of the term. A trademark registrant may license its registered trademark to another party by entering into a trademark license contract. Trademark license agreements must be filed with the Trademark Office to be recorded. The licensor shall supervise the quality of the commodities on which the trademark is used, and the licensee shall guarantee the quality of such commodities. As for trademarks, the Trademark Law of the People's Republic of China has adopted a "first come, first file" principle with respect to trademark registration. Where trademark for which a registration application has been made is identical or similar to another trademark which has already been registered or been subject to a preliminary examination and approval for use on the same kind of or similar commodities or services, the application for registration of such trademark may be rejected. Any person applying for the registration of a trademark may not prejudice the existing right first obtained by others, nor may any person register in advance a trademark that has already been used by another party and has already gained a "sufficient degree of reputation" through such party's use.

**Domain Names**

Internet domain name registration and related matters are primarily regulated by China Internet Network Information Center, or CNNIC Implementing Rules of Domain Name Registration issued by China Internet Network Information Center, or the CNNIC, the domain name registrar of mainland China, which became effective on May 29, 2012, the Administrative Measures for Internet Domain Names, issued by MIIT on August 24, 2017 and effective as of November 1, 2017, and the Measures on Domain Name Disputes Resolution issued by CNNIC which became effective on September 1, 2014. Domain name registrations are handled through domain name service agencies established under the relevant regulations, and the applicants become domain name holders upon successful registration.

**Patent Law**

According to the Patent Law of the People's Republic of China amended on December 27, 2008 and the Detailed Rule for the Implementation of Patent Law amended on January 9, 2010, patent is divided into three categories: invention patent, utility model patent, and design patent.

Invention patent is intended to protect new technical solution for a product. The applicant for invention patent must prove that the subject matter product possesses novelty, creativity and practical applicability. The grant of invention patent is subject to disclosure and publication. Normally, the patent administrative authority publishes the application within 18 months after it is filed and if it meets the requirements of this Law in its preliminary review, which may be shortened upon request by the applicant. The patent administrative authority conducts a substantive review within three years from the date the application is filed. The term of protection is 20 years from the date of application. Once the invention patent right is granted, unless otherwise permitted by law, no individuals or entities are permitted to engage in the manufacture, use, offering for sale, sale or import of the patented product, or use the patented method or otherwise engage in the use, offering for sale, sale or import of the product directly derived from applying the patented method, without the licensing of the patent holder.

Utility model patent is intended to protect new technical solution in relation to a product's shape, structure or a combination thereof, which is fit for practical use. The applicant for utility model patent must prove that the subject matter product possesses novelty, creativity and practical applicability. Utility patent is granted and registered upon application unless there are reasons for the patent administrative authority to reject the application after its preliminary review. The utility model patent is subject to the disclosure and publication upon application. The term of protection is 10 years from the date of application. Once the utility patent right is granted, unless otherwise permitted by law, no individuals or entities are permitted to engage in the manufacture, use, offering for sale, sale or import of the patented product, or use the patented method or otherwise engage in use, offering for sale, sale or import of the product directly derived from applying the patented method, without the licensing of the patent holder.

Design patent is intended to protect new design of a product's shape, pattern or a combination thereof as well as its combination with the color and the shape or pattern of a product, which creates an aesthetic feeling and is fit for industrial application. The applicant for design patent protection must prove that the subject that for matter product is not identical to a prior design. The application procedure and term of protection is the same as that for utility patent. Once a design patent is granted, no individuals or entities are permitted to engage in the manufacture, offering for sale, sale or import of the product protected by such design patent, without the licensing of the patent holder.

**REGULATIONS RELATING TO FINANCIAL BUSINESS**

**Regulations on Micro Lending Business**

Pursuant to the Guiding Opinions on the Pilot Operation of Micro Lending Companies promulgated by the China Banking Regulatory Commission, or CBRC, which has been merged into the China Banking and

Insurance Regulatory Commission) and the People's Bank of China, or PBOC, on May 4, 2008, to apply for setting up a micro lending company, the applicant shall file an application in due form with the competent department of the provincial government, and, upon approval, it shall apply to the local administrative department for industry and commerce for handling the registration formalities and get the business license. The major sources of funds of a micro lending company shall be the capital paid by shareholders, donated capital and the capital borrowed from at most two banking financial institutions. The balance of the capital borrowed from banking financial institutions shall not exceed 50% of the net capital within the scope as prescribed by laws and regulations. The loan interest ceiling shall be left open but below the ceiling determined by the judicial department, and the floor interest rate shall be 0.9 times the base rate published by PBOC.

CBRC together with other 14 ministries and commissions promulgated the Implementation Plan for the Special Rectification of Risks concerning Online Peer-to-Peer Lending on April 13, 2016, which aims to maintain the economic and financial order and social stability. The priorities of the special rectification are to rectify and ban online and offline P2P lending business conducted by internet enterprises in violation of the regulations or beyond scope, and illegal and irregular activities such as illegal fund-raising in the name of P2P lending.

According to the Notice on Standardization and Rectification of "Cash Loan" Business issued jointly by the CBRC and the PBOC on December 1, 2017 ("**Circular 141**"), online micro lending business should be strictly managed and without obtaining the qualifications for the lending business according to the law, no organization or individual may engage in the lending business. Circular 141 also stipulates that the overall costs charged by various lending institutions, including the annualized interest and all applicable service fees, must be capped at a rate in line with the opinions of the Supreme People's Court.

On September 7, 2020, CBIRC issued Notice of Strengthening the Supervision and Administration of Small Loans Companies ("**Circular 86**") in order to strengthen the supervision and administration, regulate the business operation behaviors, prevent and mitigate risks, and advance the regulated and sound development of the industry of small loan companies. Circular 86 points out that small loan companies should strengthen fund management, improve the business operation systems, regulate debt collection and improve information disclosure. Meanwhile, Circular 86 also stress that relevant authorities should intensify support to small loan companies and create a favorable environment.

**Regulations on Payment Business**

Pursuant to the Administrative Measures for the Payment Services Provided by Non-financial Institutions promulgated by the PBOC on May 19, 2010, and was revised on April 29, 2020 to provide payment services, a non-financial institution shall obtain a Payment Business Permit and become a payment institution. An applicant for a Payment Business Permit a limited liability company or joint-stock company legally formed inside the People's Republic of China and it is the corporate body of a non-financial institution. A payment institution shall file the statistical statements, financial accounting report and other relevant materials on its payment business with the local branch of the PBOC as required, and the proportion of its paid-in monetary capital against its daily average balance of clients' deposits shall not be lower than 10%. Where any payment institution continues to operate the payment business after its Payment Business Permit has expired, the PBOC or the branch thereof shall order it to terminate the payment business. On January 13, 2017, the PBOC promulgated the Notice on Matters concerning Implementing the Centralized Deposit of the Funds of Pending Payments of Clients of Payment Institutions. According to which, beginning on April 17, 2017, a payment institution shall deposit a certain percentage of the funds of pending payments of its clients in a special deposit account with a designated institution, and there is no interest on the funds in such an account for the time being. The percentage was adjusted by PBOC on December 29, 2017 in the Notice on Adjusting the Centralized Deposit Percentage of the Funds of Pending Payments of Clients of Payment Institutions, which requires the centralized deposit percentage to be raised by 10% on a monthly basis from February to April 2018.

### Regulations on Commercial Factoring

The commercial factoring is a relatively new business model in mainland China, MOFCOM had issued circulars to promote commercial factoring in the specific regions. Pursuant to the Circular on the Pilot Work of Commercial Factoring, which was promulgated by MOFCOM on June 27, 2012, a trial implementation of commercial factoring pilot work was permitted in Tianjin Binhai New Area and Shanghai Pudong New Area to explore the approaches to develop the commercial factoring and to better utilize its role in expanding the export and promoting the development of small and medium enterprises. Later in December 2012, the said trial implementation of commercial factoring pilot work was extended to Guangzhou and Shenzhen, which allowed qualified investors from Hong Kong and Macau to establish commercial factoring company in the said cities. Pursuant to the Reply of the Ministry of Commerce on Launching Pilot Commercial Factoring Business in the Chongqing Liang Jiang New Area, the Sunan Modernization Development Demonstration Zone and the Suzhou Industrial Park, released by MOFCOM on August 26, 2013, and amended on October 28, 2015, the trial implementation of commercial factoring was extended to Chongqing Liangjiang New Area, Sunan Modernization Development Demonstration Zone, and the Suzhou Industrial Park.

## REGULATIONS RELATING TO FOREIGN EXCHANGE

### General Administration of Foreign Exchange

Under the Foreign Exchange Administration Rules of the People’s Republic of China, promulgated on January 29, 1996 and last amended on August 5, 2008, and various regulations issued by the State Administration of Foreign Exchange, or SAFE, and other relevant government authorities, Renminbi is convertible into other currencies for the purpose of current account items, such as trade related receipts and payments, payment of interest and dividends. The conversion of Renminbi into other currencies and remittance of the converted foreign currency outside China for the purpose of capital account items, such as direct equity investments, loans and repatriation of investment, requires the prior approval from SAFE or its local office. Payments for transactions that take place within mainland China must be made in Renminbi. Unless otherwise required by SAFE, Chinese companies may repatriate foreign currency payments received from abroad or retain the same abroad. Foreign-invested enterprises may retain foreign exchange in accounts with designated foreign exchange banks under the current account items subject to a cap set by SAFE or its local office. Foreign exchange proceeds under the current accounts may be either retained or sold to a financial institution engaging in settlement and sale of foreign exchange pursuant to relevant rules and regulations of the State. For foreign exchange proceeds under the capital accounts, approval from SAFE is required for its retention or sale to a financial institution engaging in settlement and sale of foreign exchange, except where such approval is not required under the relevant rules and regulations of mainland China.

Pursuant to the Notice of the SAFE on Further Improving and Adjusting Foreign Exchange Administration Policies for Direct Investment, or the SAFE Circular No. 59, promulgated by SAFE on November 19, 2012, that became effective on December 17, 2012 and was further amended on May 4, 2015, approval is not required for the opening of an account entry in foreign exchange accounts under direct investment. SAFE Notice No. 59 also simplified the capital verification and confirmation formalities for foreign invested entities, the foreign capital and foreign exchange registration formalities required for the foreign investors to acquire equities from Chinese party, and further improved the administration on exchange settlement of foreign exchange capital of foreign invested entities.

On July 4, 2014, SAFE promulgated the Notice on Relevant Issues Relating to Domestic Residents’ Investment and Financing and Round-Trip Investment through Special Purpose Vehicles, or the Circular No. 37, effective as of July 4, 2014. Under Circular No. 37, (1) a resident in mainland China must register with the local SAFE branch before he or she contributes assets or equity interests in an overseas special purpose vehicle, or an Overseas SPV, that is directly established or indirectly controlled by the Chinese resident for the purpose of conducting investment or financing; and (2) following the initial registration, the Chinese resident is also required to register with the local SAFE branch for any major change, in respect of the Overseas SPV, including, among other things, a change in the Overseas SPV’s resident shareholder in mainland China, name of the Overseas SPV, term of operation, or any increase or reduction of the contributions by the Chinese resident, share transfer or swap, and merger or division. Additionally, pursuant to the Notice of SAFE on Further Simplifying and Improving the Direct Investment related Foreign Exchange Administration Policies, or SAFE Notice No. 13, which was promulgated on February 13, 2015 and became effective on June 1, 2015, the aforesaid registration shall be directly reviewed and handled by qualified banks in accordance with SAFE Notice No. 13, and SAFE and its branches shall perform indirect regulation over the foreign exchange registration via qualified banks.

The Circular on Reforming the Administration Measures on Conversion of Foreign Exchange Registered Capital of Foreign-invested Enterprises, or Circular 19, was promulgated on March 30, 2015 and became effective on June 1, 2015. According to SAFE Notice No. 19, a foreign-invested enterprise may, in response to its actual business needs, settle with a bank the portion of the foreign exchange capital in its capital account for which the relevant foreign exchange bureau has confirmed monetary contribution rights and interests (or for which the bank has registered the account-crediting of monetary contribution). For the time being, foreign-invested enterprises are allowed to settle 100% of their foreign exchange capitals on a discretionary basis; a foreign-invested enterprise shall truthfully use its capital for its own operational purposes within the scope of business; where an ordinary foreign-invested enterprise makes domestic equity investment with the amount of foreign exchanges settled, the invested enterprise shall first go through domestic re-investment registration and open a corresponding Account for Foreign Exchange Settlement Pending Payment with the foreign exchange bureau (bank) at the place of registration. The Notice of the SAFE on Reforming and Regulating Policies on the Control over Foreign Exchange Settlement of Capital Accounts, or SAFE Notice No. 16, was promulgated and became effective on June 9, 2016. According to SAFE Notice No. 16, enterprises registered in mainland China may also convert their foreign debts from foreign currency into Renminbi on self-discretionary basis. SAFE Notice No. 16 provides an integrated standard for conversion of foreign exchange under capital account items (including but not limited to foreign currency capital and foreign debts) on self-discretionary basis, which applies to all enterprises registered in mainland China. SAFE Notice No. 16 reiterates the principle that Renminbi converted from foreign currency-denominated capital of a company may not be directly or indirectly used for purposes beyond its business scope and may not be used for investments in securities or other investment with the exception of bank financial products that can guarantee the principal within mainland China unless otherwise specifically provided. Besides, the converted Renminbi shall not be used to make loans for unrelated enterprises unless it is within the business scope or to build or to purchase any real estate that is not for the enterprise own use with the exception for the real estate enterprise.

In February 2012, SAFE promulgated the Notices on Issues Concerning the Foreign Exchange Administration for Domestic Individuals Participating in Stock Incentive Plan of Overseas Publicly-Listed Company, or the Stock Option Rules, individuals participating in any stock incentive plan of any overseas publicly listed company who are Chinese citizens or foreign citizens who reside in mainland China for a continuous period of not less than one year, subject to a few exceptions are required to register with SAFE or its local branches and complete certain other procedures through a domestic qualified agent, which could be a Chinese subsidiary of such overseas listed company, and complete certain other procedures. The participants must also retain an overseas entrusted institution to handle matters in connection with their exercise of stock options, the purchase and sale of corresponding stocks or interests and fund transfers. In addition, the agent in mainland China is required to amend the SAFE registration with respect to the stock incentive plan if there is any material change to the stock incentive plan, the mainland Chinese agent or the overseas entrusted institution or other material changes. The mainland Chinese agents must, on behalf of the mainland Chinese residents who have the right to exercise the employee share options, apply to SAFE or its local branches for an annual quota for the payment of foreign currencies in connection with the mainland Chinese residents' exercise of the employee share options. The foreign exchange proceeds received by the mainland Chinese residents from the sale of shares under the stock incentive plans granted and dividends distributed by the overseas listed companies must be remitted into the bank accounts in mainland China opened by the mainland Chinese agents before distribution to such mainland Chinese residents. Under the Circular of the State Administration of Taxation on Issues Concerning Individual Income Tax in Relation to Equity Incentives promulgated by the SAT and effective from August 24, 2009, listed companies and their domestic organizations shall, according to the individual income tax calculation methods for "wage and salary income" and stock option income, lawfully withhold and pay individual income tax on such income.

## REGULATIONS RELATING TO DIVIDEND DISTRIBUTION

The principal laws regulating the dividend distribution of dividends by foreign-invested enterprises in mainland China is the Company Law of the People's Republic of China, as amended in 2005, 2013 and 2018. A mainland Chinese company is required to set aside as general reserves at least 10% of its after-tax profit, until the cumulative amount of such reserves reaches 50% of its registered capital unless the provisions of laws regarding foreign investment otherwise provided. A mainland Chinese company shall not distribute any profits until any losses from prior fiscal years have been offset. Profits retained from prior fiscal years may be distributed together with distributable profits from the current fiscal year.

## REGULATIONS RELATING TO LOANS BETWEEN FOREIGN COMPANY AND ITS CHINESE SUBSIDIARIES

A loan made by foreign investors as shareholders in a foreign invested enterprise is considered to be foreign debt in mainland China and is regulated by various laws and regulations, including the Regulation of the People's Republic of China on Foreign Exchange Administration promulgated by the State Council, the Interim Provisions on the Management of Foreign Debts promulgated by SAFE, the NDRC and the Ministry of Finance and executed on March 1, 2003, the Statistical Monitoring of Foreign Debts Tentative Provisions promulgated by SAFE on August 27, 1987, the Detailed Rules for the Implementation of Provisional Regulations on Statistics and Supervision of External Debt effective on January 1, 1998, the Regulations on Foreign Exchange Sale, Purchase and Payment promulgated by the PBOC on 1996 and the Administrative Measures for Registration of Foreign Debts promulgated by SAFE on April 28, 2013.

Under these rules and regulations, a shareholder loan in the form of foreign debt made to a Chinese entity does not require the prior approval of SAFE. However, such foreign debt must be registered with and recorded by SAFE or its local branches. According to the Law of the People's Republic of China on Enterprise Income Tax, any interest payments, if any, on the loans are subject to a 10% withholding tax unless any such foreign shareholder's jurisdiction of incorporation has a tax treaty with China that provides for a different withholding arrangement. Pursuant to the Interim Provisions of the State Administration for Industry and Commerce on the Ratio of the Registered Capital to the Total Investment of a Sino-Foreign Equity Joint Venture Enterprise, promulgated by SAIC on February 17, 1987, if the amount of foreign exchange debt of a foreign invested enterprise exceeds its borrowing limits, the enterprise is required to apply to the relevant Chinese regulatory authorities to increase the total investment amount and registered capital to allow the excess foreign exchange debt to be registered with SAFE.

## REGULATIONS RELATING TO M&A AND OVERSEAS LISTING

On August 8, 2006, six Chinese governmental and regulatory agencies, including MOFCOM and CSRC, promulgated the Rules on Acquisition of Domestic Enterprises by Foreign Investors, or the M&A Rules, a new regulation with respect to the mergers and acquisitions of domestic enterprises by foreign investors that became effective on September 8, 2006 and revised on June 22, 2009. Foreign investors should comply with the M&A Rules when they purchase equity interests of a domestic company or subscribe the increased capital of a domestic company, and thus changing the nature of the domestic company into a foreign-invested enterprise; or when the foreign investors establish a foreign-invested enterprise in mainland China, purchase the assets of a domestic company and operate the asset; or when the foreign investors purchase the asset of a domestic company, establish a foreign-invested enterprise by injecting such assets, and operate the assets. The M&A Rules, among other things, purport to require that an offshore special vehicle, or a special purpose vehicle, formed for listing purposes and controlled directly or indirectly by mainland Chinese companies or individuals, shall obtain the approval of the CSRC prior to the listing and trading of such special purpose vehicle's securities on an overseas stock exchange.

## REGULATIONS RELATING TO EMPLOYMENT AND SOCIAL WELFARE

### The Labor Contract Law

The Labor Contract Law of the People's Republic of China, or the Labor Contract Law, which was implemented on January 1, 2008 and amended on December 28, 2012, is primarily aimed at regulating employee/employer rights and obligations, including matters with respect to the establishment, performance and termination of labor contracts. Pursuant to the Labor Contract Law, labor contracts shall be concluded in writing if labor relationships are to be or have been established between enterprises or institutions and the laborers. Enterprises and institutions are forbidden to force laborers to work beyond the time limit and employers shall pay laborers for overtime work in accordance with national regulations. In addition, labor wages shall not be lower than local standards on minimum wages and shall be paid to laborers in a timely manner. In addition, according to the Labor Contract Law: (i) employers must pay laborers double income in circumstances where within one year an employer fails to enter into an employment contract that is more than a month but less than a year from the date of employment and if such period exceeds one year, the parties are deemed to have entered into a labor contract with an "unfixed term"; (ii) employees who fulfill certain criteria, including having worked for the same employer continuously for ten years or more, may demand that the employer execute a labor contract with them with an unfixed term; (iii) employees must adhere to regulations in the labor contracts concerning commercial confidentiality and non-competition; (iv) if an employer pays for an employee professional training, the labor contract may specify a term of service, but an upper limit not exceeding the cost of training supplied to the employee has been set as the amount of compensation an employer may seek for an employee's breach of the provisions concerning term of services in the labor contract; (v) employees may terminate their employment contracts with their employers if their employers fail to make social insurance contributions in accordance with the law; (vi) employers who demand money or property from employees as guarantee or otherwise may be subject to a fine of more than RMB500 but less than RMB2,000 per employee; and (vii) employers who intentionally deprive employees of any part of their salary must, in addition to their full salary, pay such employees compensation ranging from 50% to 100% of the amount of salary so deprived if they fail to pay the salary deprived within ascertain period by the labor administration authorities.

According to the Labor Law of the People's Republic of China promulgated on July 5, 1994 and became effective on January 1, 1995 and last amended on December 29, 2018, enterprises and institutions shall establish and improve their system of workplace safety and sanitation, strictly abide by state rules and standards on workplace safety, educate laborers in labor safety and sanitation in mainland China. Labor safety and sanitation facilities shall comply with state-fixed standards. Enterprises and institutions shall provide laborers with a safe workplace and sanitation conditions which are in compliance with state stipulations and the relevant articles of labor protection.

**Social Insurance and Housing Fund**

As required under the Regulation of Insurance for Labor Injury implemented on January 1, 2004 and amended in 2010, the Provisional Measures for Maternity Insurance of Employees of Corporations implemented on January 1, 1995, the Decisions on the Establishment of a Unified Program for Basic Old-Aged Pension Insurance of the State Council issued on July 16, 1997, the Decisions on the Establishment of the Medical Insurance Program for Urban Workers of the State Council promulgated on December 14, 1998, The Unemployment Insurance Measures promulgated on January 22, 1999, the Interim Regulations Concerning the Collection and Payment of Social Insurance Premiums implemented on January 22, 1999 and the Social Insurance Law of the People's Republic of China implemented on December 29, 2018, enterprises are obliged to provide their employees in mainland China with welfare schemes covering pension insurance, unemployment insurance, maternity insurance, labor injury insurance and medical insurance. These payments are made to local administrative authorities and any employer that fails to contribute may be fined and ordered to make up within a prescribed time limit.

In accordance with the Regulations on the Management of Housing Funds which was promulgated by the State Council in 1999 and last amended in 2019, enterprises must register at the competent managing center for housing funds and upon the examination by such managing center of housing funds, these enterprises shall complete procedures for opening an account at the relevant bank for the deposit of employees' housing funds. Enterprises are also required to pay and deposit housing funds on behalf of their employees in full and in a timely manner.

## REGULATIONS RELATING TO TAX

### Enterprise Income Tax

On March 16, 2007, the National People's Congress promulgated the Law of the People's Republic of China on Enterprise Income Tax which was amended on February 24, 2017, and on December 6, 2007, the State Council enacted The Regulations for the Implementation of the Law on Enterprise Income Tax of the People's Republic of China, or, collectively, the EIT Law. The EIT Law came into effect on January 1, 2008. According to the EIT Law, taxpayers consist of resident enterprises and non-resident enterprises. Under the EIT Law and relevant implementing regulations, a uniform corporate income tax rate of 25% is applicable. However, if non-resident enterprises have not formed permanent establishments or premises in mainland China, or if they have formed permanent establishment institutions or premises in mainland China but there is no actual relationship between the relevant income derived in mainland China and the established institutions or premises set up by them, the enterprise income tax is, in that case, set at the rate of 10% for their income sourced from inside mainland China.

The Notice Regarding the Determination of Chinese-Controlled Offshore Incorporated Enterprises as Chinese Tax Resident Enterprises on the Basis of De Facto Management Bodies promulgated by the State Administration of Taxation, or SAT, on April 22, 2009 and amended on January 29, 2014 sets out the standards and procedures for determining whether the "de facto management body" of an enterprise registered outside of mainland China and controlled by mainland Chinese enterprises or mainland Chinese enterprise groups is located within mainland China.

The EIT Law provide that an income tax rate of 10% will normally be applicable to dividends payable to investors that are "non-resident enterprises," and gains derived by such investors, which (a) do not have an establishment or place of business in mainland China or (b) have an establishment or place of business in mainland China, but the relevant income is not effectively connected with the establishment or place of business to the extent such dividends and gains are derived from sources within mainland China. Such income tax on the dividends may be reduced pursuant to a tax treaty between China and the jurisdictions in which our foreign shareholders reside. Pursuant to the Arrangement between the Mainland of China and the Hong Kong Special Administrative Region for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income, or the Double Tax Avoidance Arrangement, and other applicable mainland Chinese laws, if a Hong Kong resident enterprise is determined by the competent tax authority in mainland China to have satisfied the relevant conditions and requirements under such Double Tax Avoidance Arrangement and other applicable laws, the 10% withholding tax on the dividends the Hong Kong resident enterprise receives from a mainland China resident enterprise may be reduced to 5% upon receiving approval from in-charge tax authority. However, based on the Notice on Certain Issues with Respect to the Enforcement of Dividend Provisions in Tax Treaties, or the Notice No. 81, issued on February 20, 2009 by the SAT, if the relevant Chinese tax authorities determine, in their discretion, that a company benefits from such reduced income tax rate due to a structure or arrangement that is primarily tax-driven, such Chinese tax authorities may adjust the preferential tax treatment; and based on the Notice on the Interpretation and Recognition of Beneficial Owners in Tax Treaties, which was issued on October 27, 2009 by the SAT, and the Announcement on the Recognition of Beneficial Owners in Tax Treaties, which was issued on June 29, 2012 by the SAT, conduit companies, which are established for the purpose of evading or reducing tax, or transferring or accumulating profits, shall not be recognized as beneficial owners and thus will not be entitled to the above-mentioned reduced income tax rate of 5% under the Double Tax Avoidance Arrangement.

According to the EIT Law, the EIT tax rate of a high and new technology enterprise is 15%. Pursuant to the Administrative Measures for the Recognition of High and New Technology Enterprises, effected on January 1, 2008 and amended on January 29, 2016, the certificate of a high and new technology enterprise is valid for three years.

### Value-added Tax

The Provisional Regulations of the People's Republic of China on Value-added Tax were promulgated by the State Council on December 13, 1993 and came into effect on January 1, 1994 which were subsequently amended on November 5, 2008 and came into effect on January 1, 2009 and subsequently amended on February 6, 2016 and November 19, 2017. The Detailed Rules for the Implementation of the Provisional Regulations of the People's Republic of China on Value-added Tax (Revised in 2011) were promulgated by the Ministry of Finance and the SAT on December 18, 2008 which were subsequently amended on October 28, 2011 and came into effect on November 1, 2011, or, collectively, the VAT Law. According to the VAT Law, all enterprises and individuals engaged in the sale of goods, the provision of processing, repair and replacement services, and the importation of goods within the territory of mainland China must pay value-added tax. For general VAT taxpayers selling or importing goods other than those specifically listed in the VAT Law, the value-added tax rate is 17%. On April 4, 2018, the Ministry of Finance and the SAT promulgated the Notice on Adjusting Value-added Tax Rate, which reduced the tax rates for sale, import, and export of goods, as well as the deduction rate for taxpayer's purchase of agricultural products.

On March 23, 2016, the Ministry of Finance and the SAT jointly issued the Circular of Full Implementation of Business Tax to Value-added Tax Reform, or the Circular 36, which confirms that business tax would be completely replaced by VAT from May 1, 2016.

Announcement of the State Administration of Taxation on Promulgating the Administrative Measures for the Exemption of Value-added Tax on Cross-border Taxable Activities under the Collection of Value-added Tax in Lieu of Business Tax (for Trial Implementation), which was promulgated on May 6, 2016 by the SAT, provides that if a domestic enterprise provides cross-border taxable services such as technology transfer, technical consulting, software service etc., the above mentioned cross-border taxable services shall be exempt from the value-added tax.

**Dividend Withholding Tax**

The EIT Law provides that since January 1, 2008, an income tax rate of 10% will normally be applicable to dividends declared to foreign resident investors who do not have an establishment or place of business in mainland China, or which have such establishment or place of business but the relevant income is not effectively connected with the establishment or place of business, to the extent such dividends are derived from sources within mainland China.

Pursuant to the Double Tax Avoidance Arrangement, and other applicable Chinese laws, if a Hong Kong resident enterprise is determined by the competent mainland China tax authority to have satisfied the relevant conditions and requirements under such Double Tax Avoidance Arrangement and other applicable laws, the 10% withholding tax on the dividends the Hong Kong resident enterprise receives from a mainland China resident enterprise may be reduced to 5%. However, based on the Notice No. 81, if the relevant mainland China tax authorities determine, in their discretion, that a company benefits from such reduced income tax rate due to a structure or arrangement that is primarily tax-driven, such mainland China tax authorities may adjust the preferential tax treatment; and based on the Notice on How to Interpret and Recognize the "Beneficial Owner" in Tax Treaties, issued on October 27, 2009 by the SAT, conduit companies, which are established for the purpose of evading or reducing tax, or transferring or accumulating profits, shall not be recognized as beneficial owners and thus are not entitled to the above-mentioned reduced income tax rate of 5% under the Double Tax Avoidance Arrangement.

## HONG KONG LAWS AND REGULATIONS RELATING TO OUR BUSINESS

**Telecommunications Ordinance**

We import and sell our smartphones and other consumer electronics with radiocommunication functions in Hong Kong, which is regulated by the Telecommunications Ordinance (Chapter 106 of the Laws of Hong Kong), or the TO. Under the TO, a radio dealers license (unrestricted) is required for dealing in the course of trade or business (i) in apparatus or material for radiocommunications or in any component part of any such apparatus, or (ii) in apparatus of any kind that generates and emits radio waves, whether or not the apparatus is intended, or capable of being used, for radiocommunications. A radio dealers license (unrestricted) is also required for the import into Hong Kong or export therefrom of any radiocommunications transmitting apparatus unless otherwise permitted by the Communications Authority.

Under the Telecommunications (Telecommunications Apparatus) (Exemption from Licensing) Order (Chapter 106Z of the Laws of Hong Kong), a radio dealers license (unrestricted) is not required for importing or exporting telecommunications apparatus meeting prescribed specifications.

A person without the required license is liable, on summary conviction, for a fine of HK$50,000 and imprisonment for two years. A radio dealers license (unrestricted) is generally valid for 12 months, and is renewable on payment of a prescribed fee.

**Sale of Goods Ordinance**

Contracts for the sale of goods are mainly governed by the Sale of Goods Ordinance (Chapter 26 of the Laws of Hong Kong), or the SGO. The SGO provides that there are implied obligations owed by the seller towards the buyer, including: (i) where the goods are sold in the course of business and the buyer, expressly or by implication, makes known to the seller any particular purpose for which the goods are being bought, the goods supplied shall be reasonably fit for the purposes made known; (ii) goods must correspond to any description provided; and (iii) the goods meet the standard that a reasonable person would regard as satisfactory.

**Consumer Goods Safety Ordinance**

The Consumer Goods Safety Ordinance (Chapter 456 of the Laws of Hong Kong), or the CGSO, imposes a duty on manufacturers to ensure that the consumer goods they supply are reasonably safe. Under the CGSO, all products manufactured for consumption in Hong Kong must satisfy the general safety requirements. Criminal sanctions are imposed for violations of CGSO unless a due diligence defense can be successfully established. Any person who commits an offense shall be liable, on first conviction for a fine of HK$100,000 and imprisonment for one year, and on subsequent conviction for a fine of HK$500,000 and two years of imprisonment. A continuing offense will result in an additional fine of HK$1,000 per day during the relevant period. The Commissioner of Customs and Excise has the power to serve a recall notice requiring the immediate withdrawal of a mobile phone or consumer electronic product which is believed to be of significant risk and may cause a serious injury.

**Trade Descriptions Ordinance**

The Trade Descriptions Ordinance (Chapter 362 of the Laws of Hong Kong), or the TDO, regulates trade descriptions and statements made in respect of mobile phones and consumer electronic products offered in the course of trade. The TDO provides that no person shall, in the course of trade or business, apply a false trade description or trade mark to any good. Further, selling, importing or exporting a good with a false description or trade mark is prohibited. When dealing with a consumer, a trader must not engage in conduct that: (i) is a misleading omission; (ii) is aggressive; (iii) constitutes bait advertising; (iv) constitutes a bait and switch; or (v) constitutes wrongly accepting payment. A person who commits an offense under the TDO faces a potential fine of up to HK$500,000 and imprisonment for five years.

**The Inland Revenue Ordinance**

Section 20(2) of the Inland Revenue Ordinance (Chapter 112 of the Laws of Hong Kong), or the IRO, provides that where a resident person conducts transactions with a "closely connected" non-resident person in such a way that if the profits arising in Hong Kong are less than the ordinary profits that might be expected to arise, the business performed by the non-resident person in pursuance of his or her connection with the resident person shall be deemed to be carried on in Hong Kong, and the non-resident person shall be assessable and chargeable with tax in respect of his or her profits from such business in the name of the resident person. Section 20A of the IRO gives the Inland Revenue Department, or the IRD, wide powers to collect tax due from non-residents.

The IRD may also make transfer pricing adjustments by disallowing expenses incurred by the Hong Kong resident under sections 16(1), 17(1)(b) and 17(1)(c) of the IRO and challenging the entire arrangement under general anti-avoidance provisions such as sections 61 and 61A of the IRO.

Section 20 of the IRO was repealed in July 2008 with the enactment of the Inland Revenue (Amendment) No. 6 Ordinance 2018, or the Amendment Bill, which introduced a legislative framework on transfer pricing. The Amendment Bill codified international transfer pricing principles including, amongst others, the arm's length principle for provision between associated persons, the separate enterprises principle for attributing income or loss of non-Hong Kong resident person, and the three-tier transfer pricing documentation requirements relating to master file, local file and country-by-country report. Based on the Amendment Bill, a person who would have a Hong Kong tax advantage if taxed on the basis of a non-arm's length provision will instead have their income adjusted upwards or loss adjusted downwards as if arm's length provision had been made or imposed instead of the actual provision. This rule applies retrospectively to year of assessment on or after April 1, 2018.

**Cayman Islands Data Protection**

The Issuer has certain duties under the Data Protection Act, 2017 of the Cayman Islands (the "**DPL**") based on internationally accepted principles of data privacy.

Prospective investors should note that, by virtue of making investments in the Bonds and the associated interactions with the Issuer and its affiliates and/or delegates, or by virtue of providing the Issuer with personal information on individuals connected with the investor (for example directors, trustees, employees, representatives, shareholders, investors, clients, beneficial owners or agents) such individuals will be providing the Issuer and its affiliates and/or delegates (including, without limitation, the Administrator) with certain personal information which constitutes personal data within the meaning of the DPL. The Issuer shall act as a data controller in respect of this personal data and its affiliates and/or delegates, such as the Administrator, may act as data processors (or data controllers in their own right in some circumstances).

By investing in the Bonds, the Bondholders shall be deemed to acknowledge that they have read in detail and understood the Privacy Notice set out below and that such Privacy Notice provides an outline of their data protection rights and obligations as they relate to the investment in the Bonds.

Oversight of the DPL is the responsibility of the Ombudsman's office of the Cayman Islands. Breach of the DPL by the Issuer could lead to enforcement action by the Ombudsman, including the imposition of remediation orders, monetary penalties or referral for criminal prosecution.

**Privacy Notice**

**Introduction**

The purpose of this notice is to provide Bondholders with information on the Issuer's use of their personal data in accordance with the DPL.

In the following discussion, "Issuer" refers to the Issuer, the Administrator and its or their affiliates and/or delegates, except where the context requires otherwise.

**Investor Data**

By virtue of making an investment in the Issuer and a Bondholder's associated interactions with the Issuer (including any subscription (whether past, present of future), including the recording of electronic communications or phone calls where applicable) or by virtue of a Bondholder otherwise providing the Issuer with personal information on individuals connected with the Bondholder as an investor (for example directors, trustees, employees, representatives, shareholders, investors, clients, beneficial owners or agents), the Bondholder will provide the Issuer with certain personal information which constitutes personal data within the meaning of the DPL ("**Investor Data**"). The Issuer may also obtain Investor Data from other public sources. Investor Data includes, without limitation, the following information relating to a Bondholder and/or any individuals connected with a Bondholder as an investor: name, residential address, email address, contact details, corporate contact information, signature, nationality, place of birth, date of birth, tax identification, credit history, correspondence records, passport number, bank account details, source of funds details and details relating to the Bondholder's investment activity.

In the Issuer's use of Investor Data, the Issuer will be characterized as a "data controller" for the purposes of the DPL. The Issuer's affiliates and delegates may act as "data processors" for the purposes of the DPL.

**Who this Affects**

If a Bondholder is a natural person, this will affect such Bondholder directly. If a Bondholder is a corporate investor (including, for these purposes, legal arrangements such as trusts or exempted limited partnerships) that provides the Issuer with Investor Data on individuals connected to such Bondholder for any reason in relation to such Bondholder's investment with the Issuer, this will be relevant for those individuals and such Bondholder should transmit the content of this Privacy Notice to such individuals or otherwise advise them of its content.

**How the Issuer May Use a Bondholder's Personal Data**

The Issuer, as the data controller, may collect, store and use Investor Data for lawful purposes, including, in particular:

(i) where this is necessary for the performance of the Issuer's rights and obligations under any subscription agreements or purchase agreements;

(ii) where this is necessary for compliance with a legal and regulatory obligation to which the Issuer is subject (such as compliance with anti-money laundering and FATCA/CRS requirements); and/or

(iii) where this is necessary for the purposes of the Issuer's legitimate interests and such interests are not overridden by the Bondholder's interests, fundamental rights or freedoms.

Additionally, the Administrator may use Investor Data, for example to provide its services to the Issuer or to discharge the legal or regulatory requirements that apply directly to it or in respect of which the Issuer relies upon the Administrator, but such use of Investor Data by the Administrator will always be compatible with at least one of the aforementioned purposes for which we process Investor Data.

Should the Issuer wish to use Investor Data for other specific purposes (including, if applicable, any purpose that requires a Bondholder's consent), the Issuer will contact the applicable Bondholders.

**Why the Issuer May Transfer a Bondholder's Personal Data**

In certain circumstances the Issuer and/or its authorized affiliates or delegates may be legally obliged to share Investor Data and other information with respect to a Bondholder's interest in the Issuer with the relevant regulatory authorities such as the Cayman Islands Monetary Authority or the Tax Information Authority. They, in turn, may exchange this information with foreign authorities, including tax authorities.

The Issuer anticipates disclosing Investor Data to the Administrator and others who provide services to the Issuer and their respective affiliates (which may include certain entities located outside the Cayman Islands or the European Economic Area), who will process a Bondholder's personal data on the Issuer's behalf.

**The Data Protection Measures the Issuer Takes**

Any transfer of Investor Data by the Issuer or its duly authorized affiliates and/or delegates outside of the Cayman Islands shall be in accordance with the requirements of the DPL.

The Issuer and its duly authorized affiliates and/or delegates shall apply appropriate technical and organizational information security measures designed to protect against unauthorized or unlawful processing of Investor Data, and against accidental loss or destruction of, or damage to, Investor Data.

The Issuer shall notify a Bondholder of any Investor Data breach that is reasonably likely to result in a risk to the interests, fundamental rights or freedoms of either such Bondholder or those data subjects to whom the relevant Investor Data relates.

## DIRECTORS AND SENIOR MANAGEMENT

### Directors

Our board of directors currently consists of seven directors, comprising three executive directors, one non-executive director and three independent non-executive directors. The following table sets out the name, age and position of our directors as of the date of this Offering Circular:

| Name | Age | Position |
|---|---|---|
| Lei Jun | 50 | Executive Director, Founder, Chairman and CEO |
| Lin Bin | 52 | Executive Director, Vice Chairman and Co-founder |
| Chew Shou Zi | 38 | Executive Director, Partner, Senior Vice President and President of International |
| Liu Qin | 47 | Non-executive Director |
| Chen Dongsheng | 62 | Independent Non-executive Director |
| Tong Wai Cheung Timothy | 67 | Independent Non-executive Director |
| Wong Shun Tak | 59 | Independent Non-executive Director |

### Executive Directors

**Lei Jun** (雷軍), aged 50, is an executive Director, the Founder, the Chairman and the CEO of the Company. He is also a member of the Remuneration Committee. Lei Jun is overall responsible for the Company's strategy, company culture and key products. He oversees the senior management team. Lei Jun currently holds directorships in various subsidiaries, Consolidated Affiliated Entities and operating entities of the Group.

Lei Jun is a renowned angel investor in mainland China. Lei Jun joined Kingsoft Corporation Limited (SEHK Stock Code: 3888) in 1992 and has held various senior positions in Kingsoft, including as the chairman of the board since July 2011, non-executive director since August 2008 and the chief executive officer between 1998 and December 2007. From July 2011 to March 2018, Lei Jun was the chairman of Cheetah Mobile Inc. (NYSE ticker: CMCM). From July 2011 to August 2016, Lei Jun was the chairman of JOYY Inc. (NASDAQ ticker: YY).

Lei Jun received a Bachelor's degree in Computer Science from Wuhan University (武漢大學) on July 1, 1991. He has been a member of the board of Wuhan University since November 2003. Lei Jun has also been serving as vice chairman of All-China Federation of Industry and Commerce (中華全國工商業聯合會) since November 2017 and vice president of China Quality Association (中國質量協會) since December 2017.

Lei Jun was elected as one of the 2017 Top 10 Economic Personages of China, and one of 100 outstanding private entrepreneurs at the 40th anniversary of the China's reform and opening-up. In 2019, Lei Jun was honored with the title of "Outstanding Builders of Socialism with Chinese Characteristics" by the United Front Work Department of CPC Central Committee, the Ministry of Industry and Information Technology of People's Republic of China, the Ministry of Human Resources and Social Security of the People's Republic of China, the State Administration for Market Regulation and All-China Federation of Industry and Commerce, and was rewarded with the Fudan Outstanding Contribution Award of Business Management.

**Lin Bin** (林斌), aged 52, is an executive Director, Vice Chairman and Co-founder of the Board. He is also a member of the Nomination Committee. Lin Bin currently holds directorships in various major subsidiaries of the Group.

Before joining the Group in 2010, Lin Bin had served as an engineering director at Google Inc. between 2006 and 2010. Before this, he had worked at Microsoft Corporation from 1995 to 2006, including as an engineering director at Microsoft (China) Limited from 2003 to 2006. Prior to this, Lin Bin worked as a Network Engineer at ADP Inc. since May 1993.

Lin Bin has held numerous visiting and adjunct professorships, including visiting professor at Zhejiang University (浙江大學) in 2002, visiting professor at Tongji University (同濟大學) in 2002, adjunct professor at Nankai University (南開大學) from 2002 to 2005 and adjunct professor at Sun Yat-sen University (中山大學) from 2005 to 2008. He currently sits on the Board of Advisors of the Tufts University School of Engineering.

Lin Bin received a Bachelor of Science in Radio Electronics from Sun Yat-sen University (中山大學) in July 1990, and a Master of Science from Drexel University in June 1992.

**Chew Shou Zi** (周受資) (alias: Zhou Shouzi), aged 38, is an executive Director, a Partner, a Senior Vice President and President of International of the Company. He is responsible for the Group's international business. Chew Shou Zi served as the CFO of the Company from August 2015 to April 2020 and became an executive Director of the Company in October 2019, and currently holds directorships in multiple member companies of the Group. He is also a director of Kingsoft Cloud Holdings Limited (NASDAQ ticker: KC), a subsidiary of Kingsoft Corporation Limited (SEHK Stock Code: 3888).

Before joining the Group in July 2015, Chew Shou Zi was a partner at DST Investment Management Ltd. and worked there from August 2011 to June 2015. Prior to DST Investment Management Ltd., he worked at Goldman Sachs International from July 2006 to July 2008.

Chew Shou Zi received a Bachelor of Science in Economics from University College London in August 2006 and a Master of Business Administration from Harvard Business School in 2011.

**Non-executive Director**

**Liu Qin** (劉芹), former name: Liu Ya (劉雅), aged 47, is a non-executive Director and a member of the Audit Committee. Liu Qin became a Director of the Company in May 2010, and he currently holds directorships in various major subsidiaries of the Company. Liu Qin co-founded and has served as managing director of 5Y Capital (formerly known as Morningside Venture Capital Limited) since June 2007. The funds under 5Y Capital's management had been the earliest investors of the Group. Before co-founding 5Y Capital, Liu Qin served various roles including as a business development director for investment at Morningside IT Management Services (Shanghai) Co. Ltd. (晨興信息科技諮詢(上海)有限公司) from July 2000 to November 2008. He also served as a director of Xunlei Limited (NASDAQ ticker: XNET) from September 2005 to April 2020. Liu Qin has been a director of JOYY Inc. (NASDAQ ticker: YY) since June 2008.

Liu Qin received a Bachelor's degree in Industrial Electrical Automation from University of Science and Technology Beijing (北京科技大學) in July 1993, and a Master of Business Administration from China Europe International Business School (中歐國際工商學院) on April 22, 2000.

**Independent Non-Executive Directors**

**Chen Dongsheng** (陳東升), aged 62, has served as an independent non-executive Director since June 2018. He also currently serves as the chairman of both the Remuneration Committee and the Corporate Governance Committee, and a member of the Audit Committee. Chen Dongsheng has served as the chairman of Taikang Insurance Group Inc. (泰康保險集團股份有限公司) (formerly known as Taikang Life Insurance Co., Ltd (泰康人壽保險股份有限公司)) ("**Taikang**") since July 1996. He is currently the CEO of Taikang and holds various directorships within the Taikang group. Prior to this, Chen Dongsheng served as the chairman and the general manager of China Guardian Auctions Co., Ltd (中國嘉德國際拍賣有限公司) from May 1993. Prior to this, Chen Dongsheng worked as the deputy editor of the Management World (monthly), published by the Development Research Center of the State Council of China.

Chen Dongsheng has accumulated extensive corporate governance experience during his leadership in the Taikang group, as he oversaw the reform and optimization of the group's corporate governance structure. Key corporate governance initiatives implemented during Chen Dongsheng's tenure include (i) formalizing the structure, functions and accountability of the corporate governance bodies within the Taikang group, (ii) introducing board executive, audit, nomination and remuneration committees, the members of which are selected by election, and (iii) appointing independent directors.

Chen Dongsheng received a Bachelor's degree in Political Economics on July 30, 1983, and a PhD in Political Economics on June 30, 1996, both from Wuhan University (武漢大學).

**Wong Shun Tak** (王舜德), aged 59, currently serves as an independent non-executive Director, the chairman of the Audit Committee, and a member of the Remuneration Committee, Corporate Governance Committee and Nomination Committee. Wong Shun Tak is a co-founder and had been the CFO of Rokid Corporation Ltd, an artificial intelligence devices design and development company. Wong Shun Tak served as an executive director and CFO of Kingsoft from October 2011 to July 2012, and also acted as an independent non-executive director, the chairman of the audit committee and a member of the remuneration committee of Kingsoft from April 2007 to September 2011. Wong Shun Tak has served as an independent non-executive Director and the chairman of the Audit Committee of the Company since June 2018.

Wong Shun Tak was vice president of finance and financial controller of Alibaba Group Holding Ltd (NYSE ticker: BABA; SEHK Stock Code: 9988) from August 2007 to September 2011. During his service with Alibaba Group, he also acted as the chairman of Group Financial Control Committee of Alibaba Group.

Wong Shun Tak served as the CFO of Goodbaby Children Products Group ("**Goodbaby**") from August 2003 to August 2007, a leading juvenile product manufacturer in China. Before joining Goodbaby, Wong Shun Tak worked as the vice president of finance in IDT International Limited (SEHK Stock Code: 167) from September 2001 to July 2003.

In the past, Wong Shun Tak held key financial management positions in various multi-national companies, including as the financial controller of AMF Bowling, Inc. from November 1996 to March 1998 and International Distillers China Ltd. from December 1993 to October 1996. Wong Shun Tak has extensive experience in financial control, operations, strategic planning and implementation, private fund investments and exit strategies.

Wong Shun Tak received a Master's degree in Finance from the University of Lancaster in the United Kingdom and a Master's degree in Accounting from Charles Stuart University in Australia. He is also a fellow CPA member of the Hong Kong Institute of Certified Public Accountants and a fellow CPA member of Australian Society of CPAs.

**Professor Tong Wai Cheung Timothy** (唐偉章) ("Prof. Tong"), aged 67, is an independent non-executive Director, the chairman of the Nomination Committee and a member of the Corporate Governance Committee. He joined the Group in August 2019.

Prof. Tong received a Bachelor's degree in Mechanical Engineering from Oregon State University, and a Master of Science and PhD degree in the same discipline from the University of California at Berkeley. Prof. Tong serves as the chairman of the Council, Hong Kong Laureate Forum, and the chairman of the Citizens Advisory Committee on Community Relations of the Independent Commission Against Corruption (ICAC). He also serves as a member of the Advisory Committee on Corruption of the ICAC and the InnoHK Steering Committee. Additionally, he has been appointed a Non-official Justice of the Peace and a member of the Chinese People's Political Consultative Conference since 2010 and 2013 respectively. Prof. Tong has over 30 years of teaching, research and administrative experience in universities in the United States and Hong Kong. Prior to taking the office as president of The Hong Kong Polytechnic University from 2009 to 2018, he was a professor and dean of the School of Engineering and Applied Science at The George Washington University. Since July 2019, Prof. Tong has been serving as CEO of AMTD Foundation. He is a fellow of the American Society of Mechanical Engineers, the Hong Kong Academy of Engineering Sciences ("**HKAES**") and the International Thermal Conductivity Conference. He served as the president of HKAES in 2018.

Prof. Tong is currently an independent non-executive director of Airstar Bank Limited, a subsidiary of the Company. He is also an independent non-executive director of Gold Peak Industries (Holdings) Limited (SEHK Stock Code: 40), a non-executive director of Freetech Road Recycling Technology (Holdings) Limited (SEHK Stock Code: 6888) and an independent non-executive director of GP Industries Limited (SGX Stock Code: G20).

**Senior Management (Non-Directors)**

**Chang Cheng** (常程), aged 49, is a Vice President and is responsible for the Group's smartphone product planning. Prior to joining the Group in January 2020, Chang Cheng served as vice president of Lenovo Group Limited (SEHK Stock Code: 992) since July 2011.

Chang Cheng received a Bachelor's degree in Mathematics from Beijing Normal University (北京師範大學) in July 1993 and a PhD in Engineering from Beihang University (北京航空航天大學) in July 2000.

**Dr. Cui Baoqiu** (崔寶秋), aged 51, is a Vice President and the Chairman of the Technical Committee. He has over 20 years of experience in software and Internet development. Dr. Cui oversees decision-making related to the Group's technology development, as well as the recruitment, training, appointment and retention of technical talents. Prior to his current roles, Dr. Cui was Chief Architect and Vice President of the AI and Cloud Platform, a team which he founded and led for over six years.

Prior to joining Xiaomi, Dr. Cui was Principal Engineer of LinkedIn from 2010 to 2012. From 2006 to 2010, Dr. Cui worked as Principal Engineer on the Yahoo Search Technology team. From 2000 to 2006, Dr. Cui was Senior Engineer and Senior R&D Manager at IBM.

Dr. Cui obtained a PhD degree in Computer Science from the State University of New York at Stony Brook in 2000. He received Master's and Bachelor's degrees in Computer Science from Wuhan University in 1994 and 1991 respectively.

**Gao Zi Guang** (高自光), aged 38, is a Vice President and is responsible for new retail business in the China Department. Prior to joining the Group in February 2014, Gao Zi Guang worked at Tencent Holdings Ltd. (SEHK Stock Code: 700) for 10 years, rising from basic engineer to T4 technical expert. He has rich experience in internet business, and has participated in and been in charge of QQ, SOSO, Tencent Microblog, Micro-Video and other products.

Gao Zi Guang received a Bachelor's degree in Computer Science and Technology from Xi'An Jiaotong University (西安交通大學) and a Master of Business Administration from Tsinghua University (清華大學).

**He Yong** (何勇), aged 47, is a Vice President and is responsible for the Group's public affairs, regional headquarters management, regional expansion and administrative management. Prior to joining the Group in 2018, He Yong served as deputy director of the Hubei Provincial Government Office in Beijing in February 2017, and has a wealth of management experience in governmental communication, public affairs, regional economy, project management and other related areas.

He Yong received a PhD in Economics from Wuhan University (武漢大學) in December 2018.

**Hong Feng** (洪鋒), aged 43, is a Co-founder and a Senior Vice President. He is currently the Chairman and Chief Executive Officer of Airstar Digital Technology, responsible for the development of finance businesses of the Group. Prior to joining the Group in December 2010, Hong Feng worked at Google Inc. from May 2005 to December 2010, where his responsibilities included product and engineering management. From May 2001 to May 2005, Hong Feng worked at Siebel Systems (which was subsequently acquired by Oracle America, Inc.) as chief software engineer.

Hong Feng received a Bachelor's degree in Computer and Applications from Shanghai Jiao Tong University (上海交通大學) in July 1999, and a Master of Science from Purdue University in May 2001.

**Jain Manu Kumar**, aged 39, is a Vice President and the Managing Director of Xiaomi India, responsible for the Group's business in India. Jain Manu Kumar joined the Group in May 2014 and led Xiaomi's business in India. Prior to January 2014, he had co-founded Jabong.com. Between June 2007 and December 2011, Jain Manu Kumar held the position of Engagement Manager in McKinsey & Company.

Jain Manu Kumar received a Bachelor's degree in Mechanical Engineering from Indian Institute of Technology (IIT), Delhi, in 2003 and a Post Graduate Diploma in Management and Master of Business Administration from Indian Institute of Management (IIM), Calcutta in 2007.

**Lam Sai Wai Alain** (林世偉), aged 47, is a Vice President and the CFO of the Group, and the Deputy Chairman of Airstar Digital Technology. Prior to joining the Group in October 2020, Lam Sai Wai Alain worked at Credit Suisse and served as a managing director and the head of technology, media and telecom in the investment banking and capital markets department in Asia Pacific. Prior to that, he worked at Morgan Stanley between 1997 and 2016, and served multiple roles in their London, New York, and Menlo Park offices during that period.

Lam Sai Wai Alain received a Master's degree in Engineering from the University of Oxford.

**Liu De** (劉德), aged 47, is a Co-founder, Senior Vice President and Head of the Organization Department. He is currently responsible for the recruitment, promotion, training and evaluation of the middle and senior management of the Group, as well as the organizational structure design and approval procedures of each department. In October 2002, Liu De co-founded Beijing Xinfengrui Industrial Design Co., Ltd. (北京新鋒銳工業設計公司) and served as its executive director.

Liu De received a Bachelor's degree in Industrial Design on July 1, 1996 and a Master's degree in Mechanical Design and Theory on March 27, 2001, both from the Beijing Institute of Technology (北京理工大學). Liu De received a Master's degree in Industrial Design from Art Center College of Design, Pasadena, California, US, on April 24, 2010.

**Lu Weibing** (盧偉冰), aged 45, is a Partner, a Vice President, the President of China Department and the General Manager of Redmi, responsible for sales management of the China Department, and the brand strategy, product planning, production and marketing of Redmi. Before joining the Group in January 2019, Lu Weibing served as the chairman and president of Shenzhen Chenyee Technology Co., Ltd. (深圳市誠壹科技有限公司) from June 2017 to December 2018. From April 2010 to June 2017, Lu Weibing served as president at Shenzhen Gionee Communication Equipment Co., Ltd. (深圳市金立通信設備有限公司). Before this, Lu Weibing worked as general manager of the overseas department at Tianyu Communication Equipment Co., Ltd. (北京天宇朗通通信設備有限公司) from January 2008 to March 2010. Lu Weibing worked as general sales manager at KONKA Communication Co., Ltd. (康佳通信科技有限公司) from July 1998 to December 2007.

Lu Weibing received a Bachelor of Science in Chemistry from Tsinghua University (清華大學) in 1998 and an Executive Master of Business Administration from Cheung Kong Graduate School of Business (長江商學院) in 2009.

**Peng Zhibin** (彭志斌), aged 47, is a Vice President and Chief Human Resource Officer of the Group. He has 17 years of experience in human resource management. Prior to joining the Group in September 2020, he served as vice president of Country Garden Group (碧桂園集團) (SEHK Stock Code: 2007), general manager of human resource center and president of Lanzhou Region, and was fully responsible for the human resource department of Country Garden Group for nearly 10 years. Prior to joining Country Garden Group, Peng Zhibin served in large corporations such as COFCO Real Estate (Group) (中糧地產 (集團)) (SZSE Stock Code: 000031), Watson Wyatt Worldwide (華信惠悅諮詢公司), ZTE Corporation (中興通訊) (SEHK Stock Code: 765; SZSE Stock Code: 000063) and China Railway Fourth Academy (中鐵四院).

Peng Zhibin received a Bachelor's degree in Engineering from Hefei University of Technology (合肥工業大學) and a Master of Business Administration and Executive Master of Business Administration from Wuhan University (武漢大學) and China Europe International Business School (中歐國際工商學院) respectively. He also received a PhD degree in Management from Hong Kong Polytechnic University (香港理工大學).

**Shang Jin** (尚進), aged 44, is a Vice President, deputy head of the Organization Department and commissar of China Department, currently responsible for the organizational development, executive development and performance appraisal. Before joining the Group in September 2014, Shang Jin co-founded and served as the chief executive officer of Beijing Kylin Culture Co., Ltd. (北京麒麟網文化股份有限公司) (formerly known as Beijing Kylin Information Technology Co, Ltd. (北京麒麟網信息科技有限公司)) between July 2007 and February 2014. Before this, Shang Jin served as vice general manager of Beijing AmazGame Age Internet Technology Co., Ltd. (北京暢遊天下網絡技術有限公司) (subsequently listed as part of the group of Changyou.com Limited, NASDAQ ticker: CYOU) since February 2005. From November 1999 to February 2005, Shang Jin worked at Kingsoft, including as project manager, technology officer and division deputy manager.

Shang Jin has served as a director of Ourpalm Co., Ltd (北京掌趣科技股份有限公司) (Shenzhen Stock Exchange Stock Code: 300315) since February 2018.

In 2010, Shang Jin was awarded Zhongguancun's leading talent and was named one of the top 10 most influential leaders in the gaming industry of the year in 2011. Shang Jin received a Bachelor's degree in Physics from Dalian University of Technology (大連理工) in July 1998.

**Wang Chuan** (王川), aged 51, is a Co-founder, a Senior Vice President and Chief Strategy Officer of the Company. He is responsible for assisting the CEO of the Company in the management and overall planning of the Quality Committee, Technical Committee and Procurement Committee of the Group. Wang Chuan co-founded Beijing Duokan in February 2010, where he currently serves as the chief executive officer. Wang Chuan also founded Beijing Leishitiandi Electron Technology Co., Ltd. (北京雷石天地電子技術有限公司) in June 2006 and served as the chairman. He has served as a director of iQIYI, Inc. (NASDAQ ticker: IQ) since November 2014.

Wang Chuan received a Bachelor's degree in Computer Science and Engineering from Beijing University of Technology (北京工業大學) in July 1993.

**Wang Xiang** (王翔), aged 59, as a Partner and the President of the Group, assists the CEO with Group operations. Wang Xiang joined the Group in July 2015 served as Senior Vice President of the Group, President for International Business, responsible for global expansion, IP strategy, and strategic partnership management. He became the President in November 2019.

Wang Xiang has more than 30 years of experience in the semiconductor and communications fields. previously served as Senior Vice President of Qualcomm and President of Qualcomm Greater China, leading Qualcomm's business and operations in Greater China. Prior to that role, Xiang was Vice President of Qualcomm CDMA Technology, responsible for Qualcomm chipset business and customer services in China. Before joining Qualcomm, he held key positions in sales and marketing of world leading companies, including Motorola Inc., Lucent Technologies, Inc. and Agere Systems Inc.

Wang Xiang received a Bachelor's degree in Electronic Engineering from Beijing University of Technology (北京工業大學) in July 1984.

**Yan Kesheng** (顏克勝), aged 50, is a Vice President, the Chairman of the Quality Committee, the deputy head of the Organization Department, deputy dean of Qinghe University, and General Manager of the Smart Manufacturing Division within the Smartphone Department. He is responsible for quality control of all products and services, the improvement of corporate organization and talent development of the Group. Before joining the Group in October 2010, Yan Kesheng was a senior mechanical design manager at Star Shine Tech Co., Ltd. (星耀無線科技有限公司) from October 2008 to October 2010. From October 2002 to October 2008, Yan Kesheng worked as the chief structural design engineer and project leader at Motorola Technology Co., Ltd. (摩托羅拉科技有限公司). Before this, Yan Kesheng worked as a senior mechanical engineer and design team leader at Vtech Telecommunications Limited (偉易達通訊設備有限公司) from December 1998 to October 2002 and as the chief engineer at Hubei Yichang Nanyuan Vehicle Manufacturing Co., Ltd. (湖北宜昌南苑車輛製造有限公司) from July 1992 to November 1998.

Yan Kesheng received a Bachelor's degree in Agricultural Machinery Manufacturing and Repair from Hefei University of Technology (合肥工業大學) (formerly known as Anhui Institute of Technology (安徽工學院)) in July 1992.

**Zeng Xuezhong** (曾學忠), aged 45, is a Vice President and President of Smartphone Department, responsible for the research and development and manufacturing of smartphones. He joined the Group in July 2020. Zeng Xuezhong served as senior vice president and president of ZTE Corporation (中興通訊) (SEHK Stock Code: 765; SZSE Stock Code: 000063) in mainland China, executive vice president of ZTE Corporation and chief executive officer of ZTE Terminal. He also held senior management positions such as global executive vice president of Tsinghua Unigroup (紫光集團有限公司), and chairman and general manager of Hatchip Communications (匯芯通信技術有限公司). As an excellent manager and expert in communication industry, he has rich practical experience in corporate strategy, innovation and transformation.

Zeng Xuezhong received a Bachelor's degree in Physics and an Executive Master of Business Administration from Tsinghua University (清華大學).

**Zhang Feng** (張峰), aged 51, is a Partner, a Vice President and the Chairman of the Procurement Committee. He is responsible for assisting the CEO of the Company in formulating the strategic planning of the Group, overseeing the execution of strategies in various business departments, integrating the procurement needs of the various departments, improving procurement capabilities, optimizing procurement processes and efficiency. Zhang Feng has more than 20 years of experience in the smartphone and telecommunications industry. Prior to joining the Group in September 2016, Zhang Feng founded Jiangsu Zimi Electronic Technology Co., Ltd. (江蘇紫米電子技術有限公司), which became one of the Company's ecosystem partners. He held various positions in the Inventec group between September 1993 and February 2012, including as the director of research and development and the general manager of the Inventec group's Nanjing branch.

Zhang Feng received a Bachelor's degree in Radio Electronics from Shanghai University of Science and Technology (上海科學技術大學) (now known as Shanghai University (上海大學)) in July 1991.

**Share Option Schemes**

The Company has adopted two share options schemes, namely the Pre-IPO ESOP and the Post-IPO Share Option Scheme. Each of two subsidiaries of the Company, Xiaomi Finance and Pinecone International Limited, has adopted two share options schemes, respectively, which are XMF Share Option Scheme I, XMF Share Option Scheme II, Pinecone Share Option Scheme I and Pinecone Share Option Scheme II.

***Pre-IPO ESOP***

The Pre-IPO ESOP was adopted by the Company on May 5, 2011, superseded on August 24, 2012. The eligible participants include employees, consultants, all members of the Board, and other individuals, as determined, authorized and approved by the Board or a committee authorized by the Board. The term of the Pre-IPO ESOP commenced on August 24, 2012 and will expire on the tenth anniversary of the above starting date. No further option could be granted under the Pre-IPO ESOP after the Listing.

***Post-IPO Share Option Scheme***

The Post-IPO Share Option Scheme was adopted by the Company on June 17, 2018. The eligible participants include any employee, director, officer, consultant, advisor, distributor, contractor, customer, supplier, agent, business partner, joint venture business partner or service provider of any member of the Group or any affiliate as the Board determines. The Post-IPO Share Option Scheme shall be valid and effective for the period of ten years commencing on the listing date of our initial public offering. The total number of Class B Shares which may be issued upon exercise of all share options to be granted under the Post-IPO Share Option Scheme is 2,237,613,083 Class B Shares.

***XMF Share Option Scheme I***

The XMF Share Option Scheme I was adopted by the shareholders of Xiaomi Finance on June 17, 2018. It will remain in force from June 17, 2018 until July 9, 2018. The eligible participants include any directors and employees of any member of Xiaomi Finance Group (including nominees and/or trustees of any employee benefit trusts established for them) or any associates as the board of directors of Xiaomi Finance, or XMF board, determines. The overall limit on the number of ordinary share(s) in the share capital of Xiaomi Finance, or XMF Shares, that may be issued upon exercise of all outstanding options granted and yet to be exercised under the XMF Share Option Scheme I at any time shall not exceed 42,070,000 XMF Shares.

***XMF Share Option Scheme II***

The XMF Share Option Scheme II was approved by the shareholders of Xiaomi Finance on June 17, 2018. It will remain valid and effective for the period of 10 years starting from the listing date of our initial public offering. The eligible participants include any individual, being an employee, director, officer, consultant, advisor, distributor, contractor, customer, supplier, agent, business partner, joint venture business partner or service provider of any member of the Xiaomi Finance Group or any of the Xiaomi Finance Group's affiliates as the XMF Board or its delegates determines. The maximum number of XMF Shares represented by the options to be issued under the XMF Share Option Scheme II shall be 150,000,000 XMF Shares.

***The Pinecone Share Option Scheme I***

The Pinecone Share Option Scheme I was adopted pursuant to the written resolutions of the shareholders of Pinecone International passed on July 30, 2015. The scheme will expire on the tenth anniversary of the date above. The eligible participants include any officer (whether or not a director) or employee, any director of Pinecone Group, or any individual consultant or advisor who renders or has rendered bona fide services (with certain exceptions) to Pinecone International and its subsidiaries as one or more committees appointed by the board of directors of Pinecone International, or Pinecone Board, determine.

***The Pinecone Share Option Scheme II***

The Pinecone Share Option Scheme II was adopted pursuant to the written resolutions of the shareholders of Pinecone International on June 17, 2018. The scheme shall be valid and effective for the period of 10 years commencing July 9, 2018. The eligible participants include any individual, being an employee, director, officer, consultant, advisor, distributor, contractor, customer, supplier, agent, business partner, joint venture business partner or service provider of any member of the Pinecone Group or any affiliate as the Pinecone Board or its delegates determines. The overall limit on the number of Pinecone Ordinary Shares that may be issued upon exercise of all outstanding options granted and yet to be exercised under the Pinecone Share Option Scheme II and any other schemes at any time must not exceed 48% of the Pinecone Ordinary Shares in issue from time to time.

**Share Award Scheme**

The Company adopted the Share Award Scheme on June 17, 2018. The eligible participants include any individual, being an employee, director (including executive directors, nonexecutive directors and independent non-executive directors), officer, consultant, advisor, distributor, contractor, customer, supplier, agent, business partner, joint venture business partner or service provider of any member of the Group or any affiliate as the Board determines. The aggregate number of Class B Shares underlying all grants made pursuant to the Share Award Scheme will not exceed 1,118,806,541 Shares without Shareholders' approval subject to an annual limit of 3% of the total number of issued Shares at the relevant time.

## SUBSTANTIAL SHAREHOLDERS AND DIRECTORS' INTERESTS

### Substantial Shareholders' Interests

As of November 30, 2020, the following persons, other than the directors or chief executive of the Company, had interests or short positions in the shares or underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO as recorded in the register required to be kept by the Company under section 336 of the SFO, or who was, directly or indirectly, interested in 5% or more of the shares of the Company:

### Long/short position in the shares of the Company

| Name of Substantial Shareholder | Nature of interest | Number of Shares | Approximate percentage of shareholding in the relevant class of Shares[1] |
|---|---|---|---|
| **Class A Shares** | | | |
| Smart Mobile Holdings Limited[2] | Beneficial owner | 4,226,640,526 | 90.06% |
| Sunrise Vision Holdings Limited[2] | Interest in controlled corporations | 4,226,640,526 | 90.06% |
| Parkway Global Holdings Limited[2] | Interest in controlled corporations | 4,226,640,526 | 90.06% |
| ARK Trust (Hong Kong) Limited[2] | Trustee | 4,226,640,526 | 90.06% |
| Apex Star LLC[3] | Beneficial owner | 466,447,815 | 9.94% |
| **Class B Shares** | | | |
| Smart Mobile Holdings Limited[2] | Beneficial owner | 2,292,431,944 | 11.79% |
| Sunrise Vision Holdings Limited[2] | Interest in controlled corporations | 2,351,653,574 | 12.09% |
| Parkway Global Holdings Limited[2] | Interest in controlled corporations | 2,351,653,574 | 12.09% |
| ARK Trust (Hong Kong) Limited[2] | Trustee | 4,835,967,052 | 24.86% |
| Apex Star LLC[3] | Beneficial owner | 1,802,000,000 | 9.27% |

Notes:

(1) The calculation is based on the total number of relevant class of Shares in issue as of November 30, 2020.

(2) Smart Mobile Holdings Limited and Smart Player Limited are both wholly-owned by Sunrise Vision Holdings Limited which is in turn wholly-owned by Parkway Global Holdings Limited. Team Guide Limited is wholly-owned by Techno Frontier Investments Limited. The entire interests in Parkway Global Holdings Limited and Techno Frontier Investments Limited are held by ARK Trust (Hong Kong) Limited as trustee for the trusts established by Lei Jun (as settlor) for the benefit of Lei Jun and his family. Accordingly, Lei Jun is deemed to be interested in 1) the 4,226,640,526 Class A Shares and the 2,292,431,944 Class B Shares held by Smart Mobile Holdings Limited; 2) the 59,221,630 Class B Shares held by Smart Player Limited and 3) the 92,245,042 Class B Shares held by Team Guide Limited under the SFO. ARK Trust (Hong Kong) Limited is also a trustee for a number of trusts and therefore is deemed to be interested in the 2,392,068,436 Class B shares held by the trusts.

(3) Apex Star LLC is wholly-owned by Lin Bin. Lin Bin therefore is deemed to be interested in 466,447,815 Class A Shares and 1,802,000,000 Class B Shares held by Apex Star LLC under the SFO.

**Directors' Interests**

As of November 30, 2020, the interests and short positions of the directors and the chief executive of the Company in the shares, underlying shares and debentures of the Company or its associated corporations (within the meaning of Part XV of the SFO) which (a) were required to be notified to the Company and SEHK pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they have taken, or are deemed to have taken, under such provisions of the SFO); or (b) were required, pursuant to section 352 of the SFO, to be recorded in the register required to be kept by the Company; or (c) were required, pursuant to the Model Code for Securities Transactions by directors of Listed Issuers set out in Appendix 10 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, to be notified to the Company and SEHK were as follows:

(A) *Interest in the shares and underlying shares of the Company*

| Name of Director or chief executive | Nature of interest[6] | Relevant company | Number and class of securities | Approximate percentage of shareholding in the relevant class of Shares [1] |
|---|---|---|---|---|
| Lei Jun[2]................ | Beneficiary, founder and settlor of a Trust(L) | ARK Trust (Hong Kong) Limited | 4,226,640,526 Class A Shares | 90.06% |
| | | | 2,443,898,616 Class B Shares | 12.57% |
| | Interest in controlled corporations(L) | Smart Mobile Holdings Limited | 4,226,640,526 Class A Shares | 90.06% |
| | | | 2,292,431,944 Class B Shares | 11.79% |
| | Interest in controlled corporations(L) | Smart Player Limited | 59,221,630 Class B Shares | 0.30% |
| | Interest in controlled corporations(L) | Team Guide Limited | 92,245,042 Class B Shares | 0.47% |
| Lin Bin[3] .............. | Trustee, beneficiary and settlor of a trust(L) | Bin Lin Trust | 93,438,272 Class B Shares | 0.48% |
| | Beneficial owner(L) | | 30,347,523 Class B Shares | 0.17% |
| | Interest in controlled corporations(L) | Apex Star LLC | 466,447,815 Class A Shares | 9.94% |
| | | | 1,802,000,000 Class B Shares | 9.27% |
| | Interest in controlled corporations(L) | Bin Lin and Daisy Liu Family Foundation | 7,686,600 Class B Shares | 0.04% |
| Chew Shou Zi[4]..... | Beneficial owner(L) | | 143,641,464 Class B Shares | 0.74% |
| | Trustee (L) | Shou Zi Chew 2019 Trust | 25,344,772 Class B Shares | 0.13% |
| Liu Qin[5] .............. | Interest in controlled corporations(L) | Morningside China TMT Fund I, L.P. | 196,903,974 Class B Shares | 1.01% |
| | Interest in controlled corporations(L) | Morningside China TMT Fund II, L.P. | 20,527,199 Class B Shares | 0.11% |

Notes:

(1) The calculation is based on the total number of relevant class of Shares in issue as of November 30, 2020.

(2) Smart Mobile Holdings Limited and Smart Player Limited are both wholly-owned by Sunrise Vision Holdings Limited which is in turn wholly-owned by Parkway Global Holdings Limited. Team Guide Limited is wholly-owned by Techno Frontier Investments Limited. The entire interests in Parkway Global Holdings Limited and Techno Frontier Investments Limited are held by ARK Trust (Hong Kong) Limited as trustee for the trusts established by Lei Jun (as settlor) for the benefit of Lei Jun and his family. Accordingly, Lei Jun is deemed to be interested in 1) the 4,226,640,526 Class A Shares and the 2,292,431,944 Class B Shares held by Smart Mobile Holdings Limited; and 2) the 59,221,630 Class B Shares held by Smart Player Limited and 3) the 92,245,042 Class B Shares held by Team Guide Limited under the SFO.

(3) Lin Bin as trustee of Bin Lin Trust is deemed to be interested in 93,438,272 Class B Shares held by Apex Star FT LLC which is controlled by Bin Lin Trust under the SFO. Apex Star LLC and BIN LIN AND DAISY LIU FAMILY FOUNDATION are wholly-owned by Lin Bin. Lin Bin therefore is deemed to be interested in 466,447,815 Class A Shares and 1,802,000,000 Class B Shares held by Apex Star LLC and 7,686,600 Class B Shares held by BIN LIN AND DAISY LIU FAMILY FOUNDATION, in addition to the 30,347,523 Class B Shares held by himself directly, under the SFO.

(4) Chew Shou Zi as trustee of Shou Zi Chew 2019 Trust is deemed to be interested in 25,344,772 Class B Shares held by Tamarind Limited which is controlled by Shou Zi Chew 2019 Trust under the SFO. Chew Shou Zi directly holds 18,986,236 Class B Shares and has interests in share options granted under the Pre-IPO ESOP to subscribe for 24,655,228 Class B Shares and share options granted under the Post-IPO Share Option Scheme to subscribe for 100,000,000 Class B Shares.

(5) Liu Qin is entitled to exercise or control the exercise of one-third of the voting power at general meetings of TMT General Partner Ltd. and is therefore deemed to be interested in the Shares in which TMT General Partner Ltd. is interested. TMT General Partner Ltd. controls Morningside China TMT GP, L.P. and Morningside China TMT GP II, L.P., which respectively controls Morningside China TMT Fund I, L.P. and Morningside China TMT Fund II, L.P. (the “Morningside Funds”). Consequently, TMT General Partner Ltd. is deemed to be interested in the Shares in which the Morningside Funds have an interest.

(6) The letter “L” denotes the person’s long position in the shares.

## (B) *Interest in the shares of associated corporations of the Company*

| **Name of director or chief executive** | **Nature of interest** | **Associated corporations** | **Approximate percentage of shareholding**[(1)] |
|---|---|---|---|
| Lei Jun .............................. | Beneficial owner | Xiaomi Finance[(2)] | 42.07% |
| | Interest in controlled corporations(L) | Parkway Global Holdings Limited[(3)] | 100% |
| | Interest in controlled corporations(L) | Sunrise Vision Holdings Limited[(3)] | 100% |
| | Interest in controlled corporations(L) | Smart Mobile Holdings Limited[(3)] | 100% |
| | Interest in controlled corporation(L) | Shenzhen Pineapple Games Co., Ltd. | 0% |
| | Interest in controlled corporation(L) | Zimi International Incorporation[(4)] | 9.97% |

Notes:

(1) The calculation is based on the total number of shares of the associated corporations in issue as of November 30, 2020.

(2) Xiaomi Finance is a subsidiary of the Company and therefore Xiaomi Finance is an associated corporation of the Company. Lei Jun is entitled to receive up to 42,070,000 shares in Xiaomi Finance pursuant to options granted to him under the XMF Share Option Scheme I (subject to the relevant vesting conditions).

(3) Smart Mobile Holdings Limited, the holding company of the Company, is wholly-owned by Sunrise Vision Holdings Limited which is in turn wholly-owned by Parkway Global Holdings Limited. Lei Jun is the beneficial owner of the entire interest in Smart Mobile Holdings Limited, and is deemed to be interested in the 4,226,640,526 Class A Shares and 2,292,431,944 Class B Shares held by Smart Mobile Holdings Limited under the SFO. Therefore, Smart Mobile Holdings Limited, Sunrise Vision Holdings Limited and Parkway Global Holdings Limited are associated corporations of the Company.

(4) As of November 30, 2020, the Company held 49.91% of the equity interest of Zimi International Incorporation, and Zimi International Incorporation is therefore an associated corporation of the Company. Lei Jun is ultimately interested in Zimi International Incorporation as to 9.97% (being 9,803,900 ordinary shares).

Save as disclosed above, none of the directors or chief executive of the Company and their associates, had interests or short positions in any shares, underlying shares or debentures of the Company and its associated corporations as of November 30, 2020.

## CONTINUING CONNECTED TRANSACTIONS

The following discussion describes certain continuing connected transactions between the Group and its subsidiaries, VIEs, associated companies, key management and other related parties. The continuing connected transactions were carried out in the normal course of business and at terms negotiated.

### Contractual Arrangements

Mainland China's laws and regulations currently prohibit or restrict foreign ownership and investment in a variety of businesses in mainland China in which we operate, including but not limited to online culture business, Internet audio-visual program service business, cloud storage service and other value-added telecommunication service business and resales of mobile communication products. As a result, we operate the relevant businesses through a number of VIEs and their subsidiaries based on a series of contractual arrangements that we, through our WFOEs, entered into with the VIEs and their subsidiaries and the VIEs' shareholders. Pursuant to these contractual arrangements, we obtained effective control over and had the right to receive all economic benefits from the business and operations of the VIEs and their subsidiaries. For information on the risks relating to the contractual arrangements, see "*Risk Factors – Risks Relating to Our Corporate Structure.*"

The contractual arrangements primarily include the following:

***Exclusive Business Cooperation Agreements***, pursuant to which the VIEs agreed to engage our WFOEs as its exclusive provider of technical support, consultation and various other services and to provide service fee consisting their total consolidated profits to the WFOEs in return subject to certain customary adjustments;

***Exclusive Option Agreements***, pursuant to which the WFOEs have the rights to require the VIEs' shareholders to transfer their equity interests in the VIEs to the WFOEs and/or designated third party in whole or in part at any time and from time to time, for considerations equivalent to the respectively outstanding loans owed to the VIEs' shareholders (or part of the loan amounts in proportion to the equity interests being transferred) or for a nominal price, unless otherwise required by relevant authorities;

***Equity Pledge Agreements***, pursuant to which the VIEs' shareholders agreed to pledge all their respective equity interests in the VIEs to the WFOEs as a security interest to guarantee the performance of contractual obligations and the payment of outstanding debts. The pledge in respect of the VIEs takes effect upon the completion of registration with the relevant administration for industry and commerce and shall remain valid until after all the contractual obligations of the VIEs' shareholders and the VIEs under the relevant contractual arrangements have been fully performed and all the outstanding debts of them under the relevant contractual arrangements have been fully paid

***Powers of Attorney***, pursuant to which the VIEs' shareholders irrevocably appointed the WFOEs and their designated persons as their attorneys-in-fact to exercise on their behalf, and agreed and undertook not to exercise without such attorneys-in-fact's prior written consent, any and all right that they have in respect of their equity interests in the VIEs; and

***Loan Agreements***, pursuant to which the relevant WFOEs agreed to provide loans to certain VIEs' shareholders to be exclusively used as investment in the relevant VIEs.

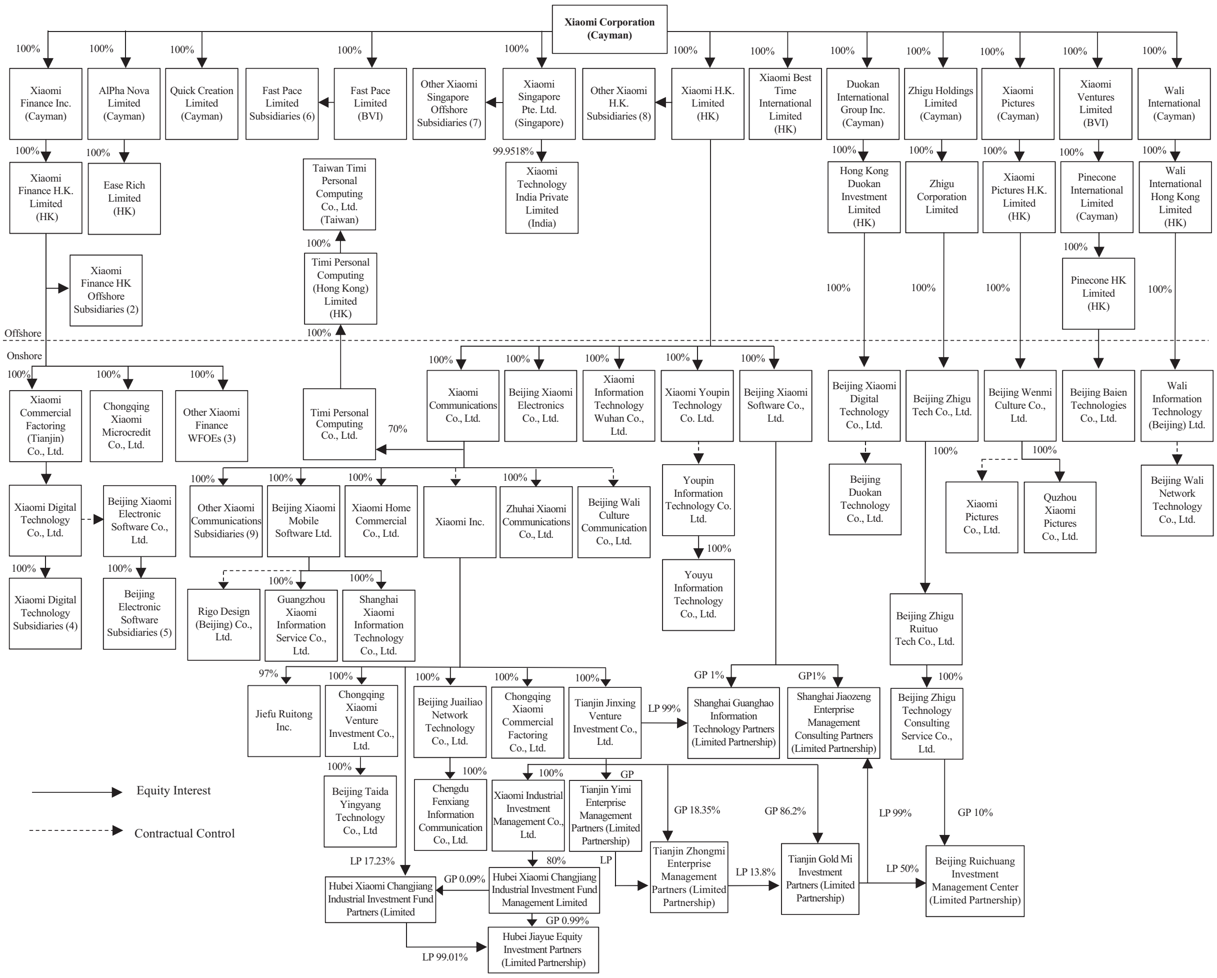
### The XMF Framework Agreement

On June 18, 2018, we and our wholly owned subsidiary Xiaomi Finance, entered into a framework agreement, or the XMF Framework Agreement, pursuant to which our Group (other than the Xiaomi Finance and its subsidiaries) and Xiaomi Finance and its subsidiaries shall provide to each other or by one to the other, (i) supply of products; (ii) data sharing and collaboration; (iii) intellectual property licensing; (iv) payment and settlement services; (v) marketing services; (vi) comprehensive support services; and (vii) financial services. Such arrangements have significant strategic advantages to our Group as a whole, particularly in terms of resources optimization and allocation, and the efficiency of intra-group coordination may also achieve considerable cost-savings to our Group as a whole.

The XMF Framework Agreement is for a term of three years from January 1, 2018 to December 31, 2020.

# CORPORATE STRUCTURE

The following chart illustrates the structure of the Group as of September 30, 2020.

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Notes:

(1) In the above corporate chart, references to:

i. "Xiaomi Finance HK" are to Xiaomi Finance H.K. Limited, a limited liability company incorporated under the laws of Hong Kong and our indirect wholly-owned subsidiary;

ii. "Tianjin Commercial Factoring" are to Xiaomi Commercial Factoring (Tianjin) Co., Ltd., a limited liability company established under the laws of mainland China and our indirect wholly-owned subsidiary;

iii. "Chongqing Microcredit" are to Chongqing Xiaomi Microcredit Co., Ltd., a limited liability company established under the laws of mainland China and our indirect wholly-owned subsidiary;

iv. "Beijing Electronic Software" are to Beijing Xiaomi Electronic Software Co., Ltd., a limited liability company established under the laws of mainland China and our VIE;

v. "Xiaomi Communications" are to Xiaomi Communications Co., Ltd., a limited liability company established under the laws of mainland China and our indirect wholly-owned subsidiary;

vi. "Xiaomi Youpin Technology" are to Xiaomi Youpin Technology Co. Ltd., a limited liability company established under the laws of mainland China and our indirect wholly-owned subsidiary;

vii. "Youpin Information Technology" are to Youpin Information Technology Co., Ltd., a limited liability company established under the laws of mainland China and our VIE;

viii. "Beijing Wali Culture" are to Beijing Wali Culture Communication Co., Ltd., a limited liability company established under the laws of mainland China and our VIE;

ix. "Xiaomi Mobile Software" are to Beijing Xiaomi Mobile Software Co., Ltd., a limited liability company established under the laws of mainland China and our indirect wholly-owned subsidiary;

x. "Beijing Digital Technology" are to Beijing Xiaomi Digital Technology Co., Ltd., a limited liability company established under the laws of mainland China and our indirect wholly-owned subsidiary;

xi. "Beijing Duokan" are to Beijing Duokan Technology Co., Ltd., a limited liability company established under the laws of mainland China and our VIE;

xii. "Beijing Wenmi" are to Beijing Wenmi Culture Co., Ltd., a limited liability company established under the laws of mainland China and our indirect wholly-owned subsidiary;

xiii. "Beijing Wali" are to Wali Information Technologies (Beijing) Ltd., a limited liability company established under the laws of mainland China and our indirect wholly-owned subsidiary;

xiv. "Beijing Wali Internet" are to Beijing Wali Internet Technologies Co., Ltd., a limited liability company established under the laws of mainland China and our VIE.

(2) Xiaomi Finance HK Offshore Subsidiaries include:

i. Gravitation Fintech HK Limited, which is owned by Xiaomi Finance HK as to 90%;

ii. Airstar Bank Limited, which is wholly-owned by Gravitation Fintech HK Limited;

iii. Xiaomi Singapore Fintech Private Limited, which is wholly-owned by Xiaomi Finance HK;

iv. Xiaomi Financial Services India Private Limited, which is owned by Xiaomi Finance HK as to 99.99% and Xiaomi Singapore Fintech Private Limited as to 0.01%.

(3) Other Xiaomi Finance WFOEs include the following direct wholly-owned subsidiaries of Xiaomi Finance HK:

i. Alpha Tianjin Financing Guarantee Co., Ltd.;

ii. Shanghai Hongmi Information Technology Co., Ltd.;

iii. Shanghai Xiaomi Financial Leasing Co., Ltd.;

iv. Tianjin Rongmi Financial Leasing Co., Ltd.

(4) Xiaomi Digital Technology Subsidiaries include the following direct wholly-owned subsidiaries of Xiaomi Digital Technology Co., Ltd.:

i. Chengdu Beida Asset Management Co., Ltd.;

ii. Beijing Shouwangxiangzhu Technology Co., Ltd;

iii. Shanghai Xiaomi Financial Information Service Co., Ltd.

(5) Beijing Electronic Software Subsidiaries include the following direct wholly-owned subsidiaries of Beijing Xiaomi Electronic Software Co., Ltd.:

i. Xiaomi Credit Management Co. Ltd.;

ii. Shanghai Xiaomi Huike Information Service Co., Ltd.;

iii. Sichuan Silver Mi Technology Co., Ltd.

(6) Fast Pace Limited Subsidiaries include:

i. the following direct wholly-owned subsidiaries of Fast Pace Limited, all incorporated in the BVI:

(a) Blue Better Limited;

(b) People Better Limited;

(c) Red Better Limited;

(d) Green Better Limited;

ii. Xiaomi USA LLC, which is wholly-owned by Blue Better Limited;

iii. Xiaomi USA Technology LLC, which is wholly-owned by Xiaomi USA LLC.

(7) Other Xiaomi Singapore Offshore Subsidiaries include:

i. Xiaomi Malaysia SDN. BHD., which is wholly-owned by Xiaomi Singapore Pte. Ltd.;

ii. Xiaomi Philippines Corporation, which is owned by Xiaomi Singapore Pte. Ltd. as to 99.9944%;

iii. Xiaomi Communications and Logistics India Private Limited, which is owned by Xiaomi Singapore Pte. Ltd. as to 99.9967%.

(8) Other Xiaomi H.K. Subsidiaries include:

i. the following direct wholly-owned subsidiaries of Xiaomi H.K. Limited:

(a) Xiaomi Vietnam Company Limited;

(b) Xiaomi Technology Netherlands B.V.;

(c) Xiaomi Technology Spain, S.L.;

(d) Xiaomi Technology Italy S.R.L.;

(e) Xiaomi LLC;

(f) Xiaomi. Japan, LLC;

(g) XIAOMI TECHNOLOGY UK LIMITED;

(h) Xiaomi Technology France S.A.S.;

(i) Taiwan Xiaomi Communications Co., Ltd.;

(j) MI Space Limited;

ii. Xiaomi Technology Germany GmbH, which is wholly-owned by Xiaomi Technology Netherlands B.V.;

iii. Xiaomi Finland Oy, which is wholly-owned by Xiaomi Technology Netherlands B.V.;

iv. Xiaomi Turkey Teknoloji Limited Sirketi, which is wholly-owned by Xiaomi Technology Netherlands B.V.;

v. MI Space NJ Limited, which is wholly-owned by MI Space Limited;

vi. MI Space BJ Limited, which is wholly-owned by MI Space Limited

vii. MI Space Nanjing Information Technology Co., Ltd., which is wholly-owned by MI Space NJ Limited;

viii. MI Space (Beijing) Information Technology Co., Ltd, which is wholly-owned by MI Space BJ Limited;

ix. Xiaomi Technologies Bangladesh Private Limited, which is owned by Xiaomi H.K. Limited as to 0.0976% and Xiaomi Singapore Pte. Ltd. as to 99.9024%;

x. XIAOMI DE MEXICO, S de R.L. de C.V., which is owned by Xiaomi H.K. Limited as to 99.9993% and Xiaomi Singapore Pte. Ltd. as to 0.0007%;

xi. PT. Xiaomi Technology Indonesia, which is owned by Xiaomi H.K. Limited as to 99.92% and Xiaomi Singapore Pte. Ltd. as to 0.08%;

xii. Xiaomi Technology (Polska) sp. z o.o., which is owned by Xiaomi H.K. Limited as to 99.9996% and Xiaomi Singapore Pte. Ltd. as to 0.0004%;

xiii. PT. Xiaomi Communications Indonesia, which is owned by Xiaomi H.K. Limited as to 80.37% and Xiaomi Singapore Pte. Ltd. as to 19.63%;

xiv. Xiaomi Technology (Thailand) Limited, which is owned by Xiaomi H.K. Limited as to 99.9999% and Xiaomi Singapore Pte. Ltd. as to 0.0001%.

(9) Other Xiaomi Communications Subsidiaries include:

i. the following direct wholly-owned subsidiaries of Xiaomi Communications Co., Ltd.:

(a) Beijing Pinecone Electronics Co., Ltd.;

(b) Shenzhen Xiaomi Information Technology Co., Ltd.;

(c) Beijing Shile Technology Co., Ltd.;

(d) Guangzhou Xiaomi Communications Co., Ltd.;

(e) Tibet Zimi Communications Co., Ltd.;

(f) Xiaomi Technology (Wuhan) Co., Ltd.;

(g) Beijing Xiaomi Intelligence Technology Co., Ltd.

(h) Xiaomi Home Technology Co., Ltd.;

(i) Guangdong Xiaomi Inc.;

ii. Beijing Zilin Real Estate Co., Ltd., which is owned by Guangzhou Xiaomi Communications Co., Ltd as to 95%;

iii. Shenzhen Xiaomi Communication Technology Co., Ltd, which is wholly-owned by Shenzhen Xiaomi Information Technology Co., Ltd.

## DESCRIPTION OF OTHER MATERIAL INDEBTEDNESS

The following summary of the general information regarding our material indebtedness does not purport to be a complete description of and may not contain all of the information that may be important to prospective investors. Investors should read the consolidated financial statements (including but not limited to note 33 attached thereto) contained elsewhere in this Offering Circular for additional information about our indebtedness. As of June 30, 2020 and September 30, 2020, we had total borrowings of RMB23.4 billion and RMB18.6 billion respectively. For the period ended September 30, 2020, the interest rate of the interest-bearing liabilities ranges from 2.05% to 10.0% per annum.

| | As of September 30, 2020 |
|---|---|
| | RMB |
| | (in thousands) |
| **Included in non-current liabilities** | |
| Asset-backed securities[1] | 930,000 |
| Fund raised through trusts[2] | 262,500 |
| Secured borrowings[3] | 1,772,757 |
| Unsecured borrowings[4] | 4,218,391 |
| | 7,183,648 |
| **Included in current liabilities** | |
| Asset-backed securities[1] | 4,338,851 |
| Fund raised through trusts[2] | 338,070 |
| Secured borrowings[3] | 1,607,280 |
| Unsecured borrowings[4] | 5,101,009 |
| | 11,385,210 |
| **Total** | **18,568,858** |

Notes:

(1) We have securitized certain loan receivables and completed several rounds of issuance of its asset-backed securities ("ABS"). As of September 30, 2020, the total ABS amounting to RMB5,268.9 million bore interest at 2.59%-7.50% per annum.

(2) We have securitized certain loan receivables and raised several rounds of funds through third party trusts. As of September 30, 2020, the fund raised through trust amounting to RMB600.6 million bore interest at 6.30%-10.00% per annum. We are committed to unconditionally repurchase the aforementioned securitized loan receivables. The balance will mature in 2020 and 2021.

(3) As of September 30, 2020, RMB2,232.8 million of borrowings were secured by construction in progress and land use rights amounting to approximately RMB7,063.9 million. The interest rate of these borrowings was 4.05%-4.90% per annum. RMB200.0 million should be repaid by the end of November 10, 2020, RMB30.0 million should be repaid by the end of March 8, 2021, RMB200.0 million should be repaid by the end of May 10, 2021, RMB30.0 million should be repaid by the end of September 7, 2021, RMB883.6 million should be repaid by the end of March 23, 2027, RMB450.7 million should be repaid by the end of December 12, 2027 and RMB438.5 million should be repaid by the end of September 27, 2032.

As of September 30, 2020, RMB1,147.3 million of short-term borrowings were secured by restricted deposits.

(4) As of September 30, 2020, we had RMB190.0 million unsecured borrowings with interest rate 6.43% per annum, RMB1,500.0 million unsecured borrowings with interest rate 2.92% per annum, RMB343.6 million unsecured borrowings with interest rate 1 to 3 months London Inter Bank Offered Rate ("LIBOR") + 1% or 0.7% per annum, RMB151.3 million unsecured borrowings with interest rate 3.50% per annum , RMB20.0 million unsecured borrowings with interest rate 4.57% per annum, all of these borrowings should be repaid by the Group in 2020. The Group had RMB1,087.3 million unsecured borrowings with interest rate 3.85% per annum which should be repaid by the end of September of 2021. The Group had RMB210.0 million unsecured borrowings with interest rate 3.59% per annum and RMB21.1 million unsecured borrowings with interest rate 2.05% per annum, which should be repaid by the Group in April and March of 2021, respectively.

We had RMB400.0 million and RMB200.0 million of borrowings with interest rate 6.00% per annum secured by intra-group companies, which should be repaid by the Group in April and June of 2021, respectively.

We had RMB206.0 million unsecured borrowings with interest rate 4.66% per annum which should be repaid by the end of November 26, 2029.

## TERMS AND CONDITIONS OF THE BONDS

*The following, subject to completion and amendment, and save for the paragraphs in italics, is the text of the Terms and Conditions of the Bonds which will be endorsed on the Certificate issued in respect of the Bonds and be referred to in the Global Certificate relating to the Bonds.*

The issue of the U.S.$855,000,000 in aggregate principal amount of zero coupon guaranteed convertible bonds due 2027 (the "**Bonds**", which term shall include, unless the context requires otherwise, any further bonds issued in accordance with Condition 17 and consolidated and forming a single series therewith) of Xiaomi Best Time International Limited (the "**Issuer**") and the right of conversion into Class B Shares (as defined in Condition 6(A)(iv)) was authorized by the board of directors of the Issuer on December 1, 2020 and the guarantee of the Bonds and the right of conversion into Class B Shares was authorized by the board of directors of Xiaomi Corporation (the "**Guarantor**") on December 1, 2020. The Bonds are constituted by the trust deed (as amended and/or supplemented from time to time, the "**Trust Deed**") dated December 17, 2020 (the "**Issue Date**") between the Issuer, the Guarantor and Citicorp International Limited (the "**Trustee**", which expression shall, whenever the context so permits, include all persons for the time being the trustee or trustees under the Trust Deed) as trustee for itself and the holders (as defined below) of the Bonds. These terms and conditions (the "**Conditions**") include summaries of, and are subject to, the detailed provisions of the Trust Deed, which includes the form of the Bonds. The Bondholders (as defined below) are entitled to the benefit of, and are bound by, and are deemed to have notice of, all of the provisions of the Trust Deed, and are deemed to have notice of those provisions applicable to them of the paying, conversion and transfer agency agreement dated December 17, 2020 (the "**Agency Agreement**") relating to the Bonds between the Issuer, the Guarantor, the Trustee, Citibank, N.A., London Branch as principal paying agent, principal conversion agent and principal transfer agent (collectively in such capacities, the "**Principal Agent**"), Citigroup Global Markets Europe AG as registrar (the "**Registrar**") and the other paying agents, conversion agents and transfer agents appointed under it (each a "**Paying Agent**", a "**Conversion Agent**" or, as applicable, a "**Transfer Agent**" and together with the Registrar and the Principal Agent, the "**Agents**") relating to the Bonds. References to the "**Paying Agents**" and the "**Conversion Agents**" each include the Principal Agent. References to the "**Principal Agent**", the "**Registrar**", the "**Transfer Agent**" and the "**Agents**" below are references to the principal agent, the registrar, the transfer agent and the agents for the time being for the Bonds.

Copies of the Trust Deed and of the Agency Agreement are available for inspection by the Bondholders at all reasonable times during usual business hours (being between 9:00 a.m. and 4:00 p.m. from Monday to Friday other than a public holiday) at the principal office for the time being of the Trustee (being at the Issue Date at 20/F, Citi Tower, One Bay East, 83 Hoi Bun Road, Kwun Tong, Kowloon, Hong Kong) following prior written request and proof of holding and identity satisfactory to the Trustee.

Unless otherwise defined, terms used in these Conditions have the meanings specified in the Trust Deed. In these Conditions, "**Bondholder**" and (in relation to a Bond) "**holder**" mean the person in whose name a Bond is registered.

### 1 Form, Denomination and Title

#### (A) Form and Denomination

The Bonds are issued in registered form in the denomination of U.S.$200,000 and integral multiples of U.S.$100,000 in excess thereof (each, an "**Authorized Denomination**"). A bond certificate (each a "**Certificate**") will be issued to each Bondholder in respect of its registered holding of Bonds. Each Certificate will be numbered serially with an identifying number which will be recorded on the relevant Certificate and in the register of Bondholders (the "**Register**") which the Issuer will procure to be kept by the Registrar.

*Upon issue, the Bonds will be represented by a global certificate (the "**Global Certificate**") registered in the name of a nominee of, and deposited with, a common depositary for Euroclear*

*Bank SA/NV ("**Euroclear**") and Clearstream Banking S.A. ("**Clearstream**"). The Conditions are modified by certain provisions contained in the Global Certificate. See "Description of the Global Certificate".*

*Except in the limited circumstances described in the Global Certificate, owners of interests in the Bonds represented by the Global Certificate will not be entitled to receive definitive Certificates in respect of their individual holdings of Bonds. The Bonds are not issuable in bearer form.*

**(B) Title**

Title to the Bonds will pass only by transfer and registration in the Register as described in Condition 3. The holder of any Bond will (except as otherwise required by law or as ordered by a court of competent jurisdiction) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any interest in it or any writing on, or the theft or loss of, the Certificate issued in respect of it) and no person will be liable for so treating the holder.

**2 Status and Guarantee**

**(A) Status**

The Bonds constitute direct, unconditional, unsubordinated and (subject to Condition 4(a)) unsecured obligations of the Issuer and shall at all times rank *pari passu* and without any preference or priority among themselves. The payment obligations of the Issuer under the Bonds and the obligations of the Guarantor under the Guarantee (as defined below) shall, save for such exceptions as may be provided by mandatory provisions of applicable legislation and subject to Condition 4(a), at all times rank at least equally with all of their respective other present and future unsecured and unsubordinated obligations.

**(B) Guarantee**

The due payment of all sums expressed to be payable by the Issuer under the Trust Deed and the Bonds have been unconditionally and irrevocably guaranteed by the Guarantor. The obligations of the Guarantor in that respect (the "**Guarantee**") are contained in the Trust Deed.

**3 Transfers of Bonds; Issue of Certificates**

**(A) Register**

The Issuer will cause the Register to be kept at the specified office of the Registrar outside the United Kingdom and in accordance with the terms of the Agency Agreement on which shall be entered the names and addresses of the holders of the Bonds and the particulars of the Bonds held by them and of all transfers, redemptions and conversions of the Bonds. Each Bondholder shall be entitled to receive only one Certificate in respect of its entire holding of Bonds.

**(B) Transfer**

Subject to Condition 3(E) and the terms of the Agency Agreement, a Bond may be transferred by delivery of the Certificate issued in respect of that Bond, with the form of transfer on the back duly completed and signed by the holder or his attorney duly authorized in writing, to the specified office of the Registrar or any of the Transfer Agents. No transfer of a Bond will be valid or effective unless and until entered on the Register.

*Transfers of interests in the Bonds evidenced by the Global Certificate will be effected in accordance with the rules of the relevant clearing systems.*

### (C) Delivery of New Certificates

Each new Certificate to be issued upon a transfer of Bonds will, within seven business days of receipt by the Registrar or, as the case may be, any Transfer Agent of the original Certificate and the form of transfer duly completed and signed, be made available for collection at the specified office of the Registrar or such Transfer Agent or, if so requested in the form of transfer, be mailed by uninsured mail at the risk of the holder entitled to the Bonds (but free of charge to the holder and at the Issuer's or the Guarantor's expense) to the address specified in the form of transfer.

Where only some of the Bonds (being that of one or more Bonds) in respect of which a Certificate is issued is to be transferred, converted, redeemed or repurchased, a new Certificate in respect of the Bonds not so transferred, converted, redeemed or repurchased will, within seven business days of delivery of the original Certificate to the Registrar or, as the case may be, any Transfer Agent, be made available for collection at the specified office of the Registrar or such Transfer Agent or, if so requested in the form of transfer, be mailed by uninsured mail at the risk of the holder of the Bonds not so transferred, converted, redeemed or repurchased (but free of charge to the holder and at the Issuer's or the Guarantor's expense) to the address of such holder appearing on the Register.

For the purposes of this Condition 3, "**business day**" means a day (other than a Saturday, Sunday or public holiday) on which commercial banks are generally open for business in the city in which the specified office of the Registrar or the Transfer Agent, as the case may be, with whom a Certificate is deposited in connection with a transfer or conversion is located.

### (D) Formalities Free of Charge

Registration of a transfer of Bonds and issuance of new Certificates will be effected without charge subject to (i) the person making such application for transfer paying or procuring the payment of any taxes, duties and/or other governmental charges in connection therewith, (ii) the Registrar or the Transfer Agent being satisfied with the documents of title and/or identity of the person making the application and (iii) the detailed regulations concerning transfer and registration of the Bonds set out in the Agency Agreement (as such regulations may be changed (a) by the Registrar, with the prior written approval of the Trustee and/or (b) by the Issuer, with the prior written consent of the Trustee and the Registrar).

### (E) Restricted Transfer Periods

No Bondholder may require the transfer of a Bond to be registered (i) during the period of seven days ending on (and including) the dates for payment of any principal pursuant to these Conditions (including any date of redemption pursuant to Conditions 8(B) or Condition 8(C)); (ii) after a Conversion Notice (as defined in Condition 6(B)(i)) has been delivered with respect to a Bond; or (iii) after a Relevant Event Put Exercise Notice (as defined in Condition 8(D)) or a Put Option Notice (as defined in Condition 8(E)) has been deposited in respect of such Bond pursuant to Condition 8(D) or Condition 8(E). Each such period is a "**Restricted Transfer Period**".

## 4 Covenants

### (A) Negative Pledge

So long as any Bond remains outstanding (as defined in the Trust Deed), the Guarantor will not create or have outstanding, and the Guarantor will ensure that none of its Principal Controlled Entities and the Issuer will create or have outstanding, any Lien upon the whole or any part of their respective present or future undertaking, assets or revenues (including any uncalled capital) securing any Relevant Indebtedness, or any guarantee or indemnity in respect of any Relevant

Indebtedness either of the Issuer, the Guarantor, or of any of the Guarantor's Principal Controlled Entities, without (i) at the same time or prior thereto securing or guaranteeing the Bonds, as applicable, equally and rateably therewith (or in priority thereto) or (ii) providing such other security or guarantee for the Bonds as shall be approved by an Extraordinary Resolution (as defined in the Trust Deed) of the Bondholders.

The foregoing restriction will not apply to:

(a) any Lien arising or already arisen automatically by operation of law which is timely discharged or disputed in good faith by appropriate proceedings;

(b) any Lien in respect of the obligations of any Person which becomes a Principal Controlled Entity or which merges with or into the Guarantor or a Principal Controlled Entity after the Issue Date which is in existence at the date on which it becomes a Principal Controlled Entity of the Guarantor or merges with or into the Guarantor or a Principal Controlled Entity; *provided that* any such Lien was not incurred in anticipation of such acquisition or of such Person becoming a Principal Controlled Entity or being merged with or into the Guarantor or a Principal Controlled Entity;

(c) any Lien created or outstanding in favor of the Issuer or the Guarantor;

(d) any Lien in respect of Relevant Indebtedness of the Issuer, the Guarantor or any Principal Controlled Entity with respect to which the Issuer, the Guarantor or such Principal Controlled Entity has paid money or deposited money or securities with a fiscal agent, trustee or depository to pay or discharge in full the obligations of the Issuer, the Guarantor or such Principal Controlled Entity in respect thereof (other than the obligation that such money or securities so paid or deposited, and the proceeds therefrom, be sufficient to pay or discharge such obligations in full);

(e) any Lien created in connection with Relevant Indebtedness of the Issuer, the Guarantor or any Principal Controlled Entity denominated in Renminbi and initially offered, marketed or issued primarily to Persons resident in the PRC;

(f) any Lien created in connection with a project financed with, or created to secure, Non-recourse Obligations; or

(g) any Lien arising out of the refinancing, extension, renewal or refunding of any Relevant Indebtedness secured by any Lien permitted by Conditions 4(A)(b) or 4(A)(f); *provided that* such Relevant Indebtedness is not increased beyond the principal amount thereof (together with the costs of such refinancing, extension, renewal or refunding) and is not secured by any additional property or assets.

**(B) NDRC Post-Issuance Filing**

The Guarantor undertakes that it will, within 10 PRC Business Days after the Issue Date, file or cause to be filed with the National Development and Reform Commission of the PRC or its local counterparts (the "**NDRC**") the requisite information and documents in accordance with the Circular on Promoting the Reform of the Administrative System on the Issuance by Enterprises of Foreign Debt Filings and Registrations (國家發展改革委關於推進企業發行外債備案登記制管理改革的通知 (發改外資[2015] 2044號) ) (the "**NDRC Circular**") issued by the NDRC and effective as of September 14, 2015, the Approval of Foreign Debt Quota Administration Reform Trial Enterprise (Second Batch) for 2017 issued by the NDRC on March 22, 2017 and any implementing rules and/or regulations as issued by the NDRC from time to time (the "**NDRC Post-Issuance Filing**").

The Trustee shall have no obligation or duty to monitor or ensure that the NDRC Post-Issuance Filing is filed with the NDRC or completed within the prescribed timeframe in accordance with these Conditions, the NDRC Circular and/or any other applicable PRC laws and regulations or to assist with the NDRC Post-Issuance Filing or to verify the accuracy, validity and/or genuineness of any documents in relation to or in connection with the NDRC Post-Issuance Filing or to give notice to the Bondholders confirming the submission of the NDRC Post-Issuance Filing, and shall not be liable to the Issuer, the Guarantor, the Bondholders or any other person for not doing so.

**(C) Definitions**

In these Conditions:

"**Capital Stock**" of any Person means any and all shares, interests, rights to purchase, warrants, options, participations or other equivalents of or interests in (however designated) equity of such Person, including any Preferred Shares and limited liability or partnership interests (whether general or limited), but excluding any notes convertible or exchangeable into such equity;

"**Consolidated Affiliated Entity**" of any Person means any corporation, association or other entity which is or is required to be consolidated with such Person under International Accounting Standards 27, Consolidated and Separate Financials Statements (including any changes, amendments or supplements thereto) or, if such person prepares its financial statements in accordance with accounting principles other than IFRS, the equivalent of International Accounting Standards 27, Consolidated and Separate Financial Statements under such accounting principles. Unless otherwise specified herein, each reference to a Consolidated Affiliated Entity will refer to a Consolidated Affiliated Entity of the Guarantor;

"**Controlled Entity**" of any Person means a Subsidiary or a Consolidated Affiliated Entity of such Person;

"**IFRS**" refers to International Financial Reporting Standards;

"**Lien**" means any mortgage, charge, pledge, lien or other form of encumbrance or security interest;

"**Non-Listed Controlled Entities**" means the Controlled Entities other than (i) any Controlled Entities with shares of common stock or other common equity interests listed on a nationally recognized stock exchange, including but not limited to the Shanghai Stock Exchange; and (ii) any Subsidiaries or Consolidated Affiliated Entities of any Controlled Entity referred to in clause (i) of this definition;

"**Non-recourse Obligations**" means indebtedness or other obligations substantially related to (i) the acquisition of assets (including any person that becomes a Controlled Entity) not previously owned by the Issuer, the Guarantor or any of the Guarantor's Controlled Entities or (ii) the financing of a project involving the purchase, development, improvement or expansion of properties of the Issuer, the Guarantor or any of the Guarantor's Controlled Entities, as to which the obligee with respect to such indebtedness or obligation has no recourse to the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities or to the Issuer, the Guarantor or any such Principal Controlled Entity's assets other than the assets which were acquired with the proceeds of such transaction or the project financed with the proceeds of such transaction (and the proceeds thereof);

a "**Person**" means any individual, corporation, firm, limited liability company, partnership, joint venture, undertaking, association, joint stock company, trust, unincorporated organization, trust, state, government or any agency or political subdivision thereof or any other entity (in each case whether or not being a separate legal entity);

"**PRC**" means the People's Republic of China, excluding, for purposes of this definition, the Hong Kong Special Administrative Region, the Macau Special Administrative Region and Taiwan;

"**PRC Business Day**" means a day other than a Saturday, Sunday or a day on which banking institutions in the PRC are authorized or obligated by law, regulation or executive order to remain closed;

"**Preferred Shares**" as applied to the Capital Stock of any corporation, means Capital Stock of any class or classes (however designated) that is preferred as to the payment of dividends upon liquidation, dissolution or winding up;

"**Principal Controlled Entities**" means at any time shall mean one of the Guarantor's Non-Listed Controlled Entities

(i) as to which one or more of the following conditions is/are satisfied:

(a) its total revenue or (in the case of one of the Non-Listed Controlled Entities which has one or more Non-Listed Controlled Entities) consolidated total revenue attributable to the Guarantor is at least 10 per cent. of the Guarantor's consolidated total revenue;

(b) its net profit or (in the case of one of the Non-Listed Controlled Entities which has one or more Non-Listed Controlled Entities) consolidated net profit attributable to the Guarantor (in each case before taxation and exceptional items) is at least 10 per cent. of the Guarantor's consolidated net profit (before taxation and exceptional items); or

(c) its net assets or (in the case of one of the Non-Listed Controlled Entities which has one or more Non-Listed Controlled Entities) consolidated net assets attributable to the Guarantor (in each case after deducting minority interests in Subsidiaries) are at least 10 per cent. of the Guarantor's consolidated net assets (after deducting minority interests in Subsidiaries);

all as calculated by reference to the then latest audited financial statements (consolidated or, as the case may be, unconsolidated) of such Non-Listed Controlled Entity and the Guarantor's then latest audited consolidated financial statements; *provided that*, in relation to paragraphs (a), (b) and (c) above of this definition:

(1) in the case of a corporation or other business entity becoming a Non-Listed Controlled Entity after the end of the financial period to which the Guarantor's latest consolidated audited accounts relate, the reference to the Guarantor's then latest consolidated audited accounts and the Guarantor's Non-Listed Controlled Entities for the purposes of the calculation above shall, until the Guarantor's consolidated audited accounts for the financial period in which the relevant corporation or other business entity becomes a Non-Listed Controlled Entity are issued, be deemed to be a reference to the then latest consolidated audited accounts of the Guarantor and its Controlled Entities adjusted to consolidate the latest audited accounts (consolidated in the case of a Non-Listed Controlled Entity which itself has Non-Listed Controlled Entities) of such Controlled Entity in such accounts;

(2) if at any relevant time in relation to the Guarantor or any Non-Listed Controlled Entity which itself has Non-Listed Controlled Entities, no consolidated accounts are prepared and audited, total revenue, net profit or net assets of the Guarantor and/or any such Non-Listed Controlled Entity shall be determined on the basis of pro forma consolidated accounts prepared for this purpose by or on behalf of the Guarantor;

(3) if at any relevant time in relation to any Non-Listed Controlled Entity, no accounts are audited, its net assets (consolidated, if appropriate) shall be determined on the basis of pro forma accounts (consolidated, if appropriate) of the relevant Non-Listed Controlled Entity prepared for this purpose by or on behalf of the Guarantor; and

(4) if the accounts of any Non-Listed Controlled Entity (not being a Non-Listed Controlled Entity referred to in proviso (1) above) are not consolidated with the Guarantor's accounts, then the determination of whether or not such Non-Listed Controlled Entity is a Principal Controlled Entity shall be based on a pro forma consolidation of its accounts (consolidated, if appropriate) with the Guarantor's consolidated accounts (determined on the basis of the foregoing); or

(ii) to which is transferred all or substantially all of the assets of a Non-Listed Controlled Entity which immediately prior to the transfer was a Principal Controlled Entity; *provided that*, with effect from such transfer, the Non-Listed Controlled Entity which so transfers its assets and undertakings shall cease to be a Principal Controlled Entity (but without prejudice to paragraph (i) above of this definition) and the Non-Listed Controlled Entity to which the assets are so transferred shall become a Principal Controlled Entity.

An officers' certificate in English of the Guarantor signed by an Authorized Signatory of the Guarantor delivered to the Trustee certifying in good faith as to whether or not a Non-Listed Controlled Entity is a Principal Controlled Entity shall be conclusive in the absence of manifest error and the Trustee shall be entitled to rely conclusively upon such officers' certificate (without further investigation or enquiry) and shall not be liable to any person for so accepting and relying on such officers' certificate;

"**Relevant Indebtedness**" means any indebtedness which is in the form of, or represented or evidenced by, bonds, notes, debentures, loan stock or other securities which for the time being are, or are intended to be or are commonly, quoted, listed or dealt in or traded on any stock exchange or over-the-counter or other securities market; and

a "**Subsidiary**" of any Person means (i) any corporation, association or other business entity (other than a partnership, joint venture, limited liability company or similar entity) of which more than 50 per cent. of the total ordinary voting power of shares of Capital Stock entitled (without regard to the occurrence of any contingency) to vote in the election of directors, managers or trustees thereof (or Persons performing similar functions) or (ii) any partnership, joint venture limited liability company or similar entity of which more than 50 per cent. of the capital accounts, distribution rights, total equity and voting interests or general or limited partnership interests, as applicable, is, in the case of clauses (i) and (ii), voting at the time owned or controlled, directly or indirectly, by (A) such Person, (B) such Person and one or more Subsidiaries of such Person or (C) one or more Subsidiaries of such Person. Unless otherwise specified herein, each reference to a Subsidiary will refer to a Subsidiary of the Guarantor.

## 5 Default Interest

The Bonds are zero coupon and do not bear interest unless, upon due presentation thereof, payment of principal is improperly withheld or refused. If the Issuer or the Guarantor (as the case may be) fails to pay any sum in respect of the Bonds when the same becomes due and payable under these Conditions, interest shall accrue on the overdue sum at the rate of one per cent. per annum from the due date up to whichever is the earlier of (A) the day on which all sums due in respect of such Bond up to that day are received by or on behalf of the relevant holder and (B) the day falling seven days after the Trustee or the Principal Agent has notified the Bondholders of receipt of all sums due in respect of all the Bonds up to that seventh day (except to the extent that there is failure in the subsequent payment to the relevant holders under these Conditions). If interest is required to be calculated for a period of less than one year, it will be calculated on the basis of a 360-day year consisting of twelve months of 30 days each and, in the case of an incomplete month, the number of days elapsed.

## 6 Conversion

### (A) Conversion Right

(i) *Conversion Period*: Subject as provided in these Conditions, each Bond shall entitle the holder to convert such Bond into Class B Shares credited as fully paid (as defined in

Condition 6(A)(iv)) at any time during the Conversion Period referred to below (the "**Conversion Right**").

Subject to and upon compliance with these Conditions, the Conversion Right in respect of a Bond may be exercised, at the option of the holder thereof, at any time (subject to any applicable fiscal or other laws or regulations and as hereinafter provided) on or after January 27, 2021 up to (a) the close of business (at the place where the Certificate evidencing such Bond is deposited for conversion) on the date falling 10 days prior to the Maturity Date (as defined in Condition 8) (both days inclusive) (but, except as provided in Condition 6(A)(iii), in no event thereafter), (b) if such Bond shall have been called for redemption by the Issuer before the Maturity Date, then up to and including the close of business (at the place aforesaid) on a date no later than 10 days (in the place aforesaid) prior to the date fixed for redemption thereof or (c) if notice requiring redemption has been given by the holder of such Bond pursuant to Condition 8(D) or Condition 8(E), up to the close of business (at the place aforesaid) on the business day (in the place aforesaid) prior to the giving of such notice (the "**Conversion Period**").

A Conversion Right may not be exercised (x) in respect of a Bond where the holder shall have exercised its right, by delivering or depositing the relevant notice, to require the Issuer to redeem or repurchase such Bond pursuant to Condition 8(D) or Condition 8(E) or (y) except as provided in Condition 6(A)(iii) following the giving of notice by the Trustee pursuant to Condition 10.

The price at which Class B Shares will be issued upon exercise of a Conversion Right (the "**Conversion Price**") will initially be HK$36.74 per Class B Share, but will be subject to adjustment in the circumstances described in Conditions 6(C) and 6(D).

The number of Class B Shares to be issued on exercise of a Conversion Right shall be determined by dividing the principal amount of the Bonds to be converted (translated into Hong Kong dollars at the fixed rate of HK$7.7529 = U.S.$1.00 (the "**Fixed Exchange Rate**")) by the Conversion Price in effect on the relevant Conversion Date (as defined in Condition 6(B)(i) below). A Conversion Right may only be exercised in respect of one or more Bonds. If more than one Bond held by the same holder is converted at any one time by the same holder, the number of Class B Shares to be issued upon such conversion will be calculated on the basis of the aggregate principal amount of the Bonds to be converted.

(ii) *Fractions of Class B Shares*: Fractions of Class B Shares will not be issued on exercise of Conversion Rights and no cash payment or other adjustment will be made in lieu thereof. However, if the Conversion Right in respect of more than one Bond is exercised at any one time such that Class B Shares to be issued on conversion are to be registered in the same name, the number of such Class B Shares to be issued in respect thereof shall be calculated on the basis of the aggregate principal amount of such Bonds being so converted and rounded down to the nearest whole number of Class B Shares. Notwithstanding the foregoing, in the event of a consolidation or re-classification of Class B Shares by operation of law or otherwise occurring after December 1, 2020 which reduces the number of Class B Shares outstanding, the Issuer (failing which, the Guarantor) will upon conversion of Bonds pay in cash in U.S. dollars a sum equal to such portion of the principal amount of the Bond or Bonds evidenced by the Certificate deposited in connection with the exercise of Conversion Rights, aggregated as provided in Condition 6(A)(i), as corresponds to any fraction of a Class B Share not issued as a result of such consolidation or re-classification aforesaid, provided that such sum exceeds U.S.$10. Any such sum shall be paid not later than five Class B Share Stock Exchange Business Days (as defined in Condition 6(B)(i)) after the relevant Conversion Date by a U.S. dollar-denominated check or by transfer to a U.S. dollar account maintained by the payee with, a bank in New York City in accordance with instructions given by the relevant Bondholder in the Conversion Notice.

(iii) *Revival and/or Survival after Default*: Notwithstanding the provisions of Condition 6(A)(i), if (a) the Issuer or the Guarantor shall default in making payment in full in respect of any Bond which shall have been called or put for redemption on the date fixed for redemption thereof; (b) any Bond has become due and payable prior to the Maturity Date by reason of the occurrence of any of the events under Condition 10; or (c) any Bond is not redeemed on the Maturity Date in accordance with Condition 8(A), the Conversion Right attaching to such Bond will revive and/or will continue to be exercisable up to, and including, the close of business (at the place where the Certificate evidencing such Bond is deposited for conversion) on the date upon which the full amount of the moneys payable in respect of such Bond has been duly received by the Principal Agent or the Trustee and notice of such receipt has been duly given to the Bondholders in accordance with Condition 11 and notwithstanding the provisions of Condition 6(A)(i), any Bond in respect of which the Certificate and the Conversion Notice (as defined below) are deposited for conversion prior to such date shall be converted on the relevant Conversion Date (as defined below) notwithstanding that the full amount of the moneys payable in respect of such Bond shall have been received by the Principal Agent or the Trustee before such Conversion Date or that the Conversion Period may have expired before such Conversion Date.

(iv) *Meaning of "Shares"*: As used in these Conditions, the expression (i) "**Class B Shares**" means class B ordinary shares in the share capital of the Guarantor with a par value of U.S.$0.0000025 each, conferring a holder of a Class B Share one vote per share on any resolution tabled at the Guarantor's general meetings, (ii) "**Class A Shares**" means class A ordinary shares in the share capital of the Guarantor with a par value of U.S.$0.0000025 each, conferring weighted voting rights in the Guarantor such that a holder of a Class A Share is entitled to 10 votes per share on any resolution tabled at the Guarantor's general meetings, save for resolutions with respect to any reserved matters as set out in amended and restated memorandum and articles of association of the Guarantor, in which case they shall be entitled to one vote per share, and (iii) "**Ordinary Shares**" means the Class B Shares, the Class A Shares and any fully-paid and non-assessable shares of any class or classes of the ordinary shares of the Guarantor authorized after the Issue Date which have no preference in respect of dividends or of amounts payable in the event of any voluntary or involuntary liquidation or dissolution of the Guarantor.

**(B) Conversion Procedure**

(i) *Conversion Notice*: Conversion Rights may be exercised by a Bondholder during the Conversion Period by delivering, at the Bondholder's own expense, the relevant Certificate to the specified office of any Conversion Agent during normal business hours (being between 9:00 a.m. and 4:00 p.m. on a business day) at the place where the Certificate evidencing such Bond is deposited for conversion accompanied by a duly completed and signed notice of conversion (a "**Conversion Notice**") in the form (for the time being current) obtainable from any Conversion Agent, together with (a) the relevant Certificate; and (b) confirmation that any amounts required to be paid by the Bondholder under Condition 6(B)(ii) have been so paid.

If such delivery is made after 4:00 p.m. on any business day or on a day which is not a business day in the place of the specified office of the relevant Conversion Agent, such delivery shall be deemed for all purposes of these Conditions to have been made on the next following such business day. For the purposes of this Condition 6, "**business day**" means a day (other than a Saturday, Sunday or public holiday) on which commercial banks are generally open for business in the city in which the specified office of the relevant Conversion Agent is located.

Any determination as to whether any Conversion Notice has been duly completed and properly delivered shall be made by the relevant Conversion Agent and shall, save in the case of manifest error, be conclusive and binding on the Issuer, the Trustee, the Conversion Agents and the relevant Bondholder.

Conversion Rights may only be exercised in respect of an Authorized Denomination. A Conversion Notice, once delivered, shall be irrevocable and may not be withdrawn unless the Issuer consents in writing to such withdrawal.

The conversion date in respect of a Bond (the "**Conversion Date**") must fall at a time when the Conversion Right attaching to that Bond is expressed in these Conditions to be exercisable (subject to the provisions of Condition 6(A)(iii)) and will be deemed to be the Class B Share Stock Exchange Business Day (as defined below) immediately following the later of the date of the surrender of the Certificate in respect of such Bond and delivery of such Conversion Notice (if they are not surrendered and delivered on the same day) and, if applicable, the date of making any payment or giving any indemnity under these Conditions in connection with the exercise of such Conversion Right. "**Class B Share Stock Exchange Business Day**" means any day (other than a Saturday or Sunday) on which the Relevant Stock Exchange (as defined in Condition 6(F) below) is open for trading of securities.

(ii) *Stamp Duty etc.*: A Bondholder exercising Conversion Rights must pay directly to the relevant authorities any taxes and/or capital, stamp, issue and registration and transfer taxes and duties (collectively, "**Duties**") arising on such exercise (other than any Duties payable in Hong Kong, the Cayman Islands and, if relevant, in the place of the Alternative Stock Exchange, by the Issuer and the Guarantor in respect of the allotment and issue of Class B Shares and listing of the Class B Shares on the Relevant Stock Exchange on conversion (such Duties payable by the Issuer being the "**Issuer Duties**") (the Duties payable by the Bondholder and the Issuer Duties being collectively "**Taxes**"). The Issuer (failing which, the Guarantor) will pay all other expenses arising on the issue of Class B Shares on conversion of Bonds and all charges of the Agents and the share transfer agent for the Class B Shares (the "**Share Transfer Agent**"). The Bondholder (and, if different, the person to whom the Class B Shares are to be issued) must declare in the relevant Conversion Notice that any and all amounts payable to the relevant tax authorities in settlement of Taxes payable by the Bondholders pursuant to this Condition 6(B)(ii) have been, or (where permitted by law) will be, paid.

If the Issuer shall fail to pay any Issuer Duties, the relevant holder shall be entitled to tender and pay the same and the Issuer, as a separate and independent stipulation, covenants to reimburse and indemnify each Bondholder on demand in respect of any payment thereof and any penalties payable in respect thereof.

Such Bondholder must also pay all, if any, taxes, duties, charges and assessments imposed on it and arising by reference to any disposal or deemed disposal of a Bond or interest therein in connection with the exercise of Conversion Rights by it.

Neither the Trustee nor any of the Agents shall be responsible or liable for paying any Taxes, expenses or other amounts referred to in this Condition 6(B)(ii) or for determining whether such Taxes, expenses or other amounts are payable or determining the amount thereof and none of them shall be responsible or liable for any failure by the Issuer, the Guarantor or any Bondholder to pay such Taxes, expenses or other amounts.

(iii) *Registration*: Upon exercise by a Bondholder of its Conversion Right and compliance with Conditions 6(B)(i) and 6(B)(ii) the Guarantor will, as soon as practicable, and in any event not later than seven Class B Share Stock Exchange Business Days after the Conversion Date, register the person or persons designated for the purpose in the Conversion Notice as holder(s) of the relevant number of Class B Shares in the Guarantor's Class B share register and will, if the Bondholder has also requested in the Conversion Notice and to the extent permitted under applicable law and the rules and procedures of the Central Clearing and Settlement System of Hong Kong ("**CCASS**") and the Guarantor's share registrar effective from time to time, take all necessary action to procure that Class B Shares are delivered through CCASS for so long as the Class B Shares are listed on the Hong Kong Stock Exchange; or will make such certificate or certificates available for collection at the office of the Guarantor's share registrar in Hong Kong (currently Computershare Hong Kong Investor Services Limited) notified to Bondholders in accordance with Condition 11 or, if so requested in the relevant Conversion Notice, will cause its share registrar to mail (at the risk, and, if sent at the request of such person otherwise than by ordinary mail, at the expense, of the person to whom such certificate or certificates are sent) such certificate or certificates to the person and at the place specified in the Conversion Notice, together (in either case) with any other securities, property or cash required to be delivered upon conversion of the Bonds and such assignments and other documents (if any) as may be required by law to effect the transfer thereof, in which case a single share certificate will be issued in respect of all Class B Shares issued on conversion of Bonds subject to the same Conversion Notice and which are to be registered in the same name.

The delivery of the Class B Shares to the converting Bondholder (or such person or persons designated in the relevant Conversion Notice) in the manner contemplated above in this Condition 6(B)(iii) will be deemed to satisfy the Issuer's obligation to pay the principal on such converted Bonds.

If the Conversion Date in relation to the conversion of any Bond shall be on or after the record date for any issue, distribution, grant, offer or other event as gives rise to the adjustment of the Conversion Price pursuant to Condition 6(C), but before the relevant adjustment becomes effective (the "**Relevant Effective Date**") under the relevant Condition (a "**Retroactive Adjustment**"), upon the relevant adjustment becoming effective the Guarantor shall procure the issue to the converting Bondholder (or in accordance with the instructions contained in the Conversion Notice (subject to applicable exchange control or other laws or other regulations)), such additional number of Class B Shares ("**Additional Class B Shares**") as is, together with Class B Shares to be issued on conversion of the Bond(s), equal to the number of Class B Shares which would have been required to be issued on conversion of such Bond if the relevant adjustment to the Conversion Price had been made and become effective on or immediately after the relevant record date and in such event and in respect of such Additional Class B Shares references in this Condition 6(B)(iii) to the Conversion Date shall be deemed to refer to the Relevant Effective Date (notwithstanding that the Relevant Effective Date falls after the end of the Conversion Period).

The person or persons specified for that purpose in the Conversion Notice will become the holder of record of the number of Class B Shares issuable upon conversion with effect from the date he is or they are registered as such in the Guarantor's register of members for Class B Shares (the "**Registration Date**").

The Class B Shares issued upon exercise of Conversion Rights will be fully paid and will in all respects rank *pari passu* with the fully paid Class B Shares in issue on the relevant Registration Date except for any right excluded by mandatory provisions of applicable law and except that such Class B Shares will not rank for (or, as the case may be, the relevant holder shall not be entitled to receive) any rights, distributions or payments the record or other due date for the establishment of entitlement for which falls prior to the relevant Registration Date.

If the record date for the payment of any dividend or other distribution in respect of the Class B Shares is on or after the Conversion Date in respect of any Bond, but before the Registration Date (disregarding any Retroactive Adjustment of the Conversion Price referred to in this Condition 6(B)(iii) prior to the time such Retroactive Adjustment shall have become effective), the Issuer will calculate and pay to the converting Bondholder or his designee an amount in U.S. dollars (the "**Equivalent Amount**") equal to the Fair Market Value (as defined in Condition 6(F) below) of such dividend or other distribution to which he would have been entitled had he on that record date been such a shareholder of record and will make the payment at the same time as it makes payment of the dividend or other distribution, or as soon as practicable thereafter, but, in any event, not later than seven days thereafter. The Equivalent Amount shall be paid by a U.S. dollar-denominated check or by transfer to a U.S. dollar account maintained by the payee with, a bank in New York City, in accordance with instructions given by the relevant Bondholder in the Conversion Notice.

**(C) Adjustments to Conversion Price**

The Conversion Price will be subject to adjustment as follows:

(1) **Consolidation, Subdivision or Reclassification**: If and whenever there shall be an alteration to the nominal value of Ordinary Shares of any class as a result of consolidation, subdivision or reclassification, the Conversion Price shall be adjusted by multiplying the Conversion Price in force immediately before such alteration by the following fraction:

$$\frac{A}{B}$$

Where:

A is the nominal amount of one Ordinary Share immediately after such alteration; and

B is the nominal amount of one Ordinary Share immediately before such alteration.

Such adjustment shall become effective on the date the alteration takes effect.

(2) **Capitalization of Profits or Reserves**:

(i) If and whenever the Guarantor shall issue Ordinary Shares of any class credited as fully paid to the holders of such Ordinary Shares ("**Ordinary Shareholders**") by way of capitalization of profits or reserves (including Ordinary Shares of such class paid up out of distributable profits or reserves and/or share premium account (except any Scrip Dividend)) and which would not have constituted a Capital Distribution, the Conversion Price shall be adjusted by multiplying the Conversion Price in force immediately before such issue by the following fraction:

$$\frac{A}{B}$$

Where:

A is the aggregate nominal amount of the issued Ordinary Shares immediately before such issue; and

B is the aggregate nominal amount of the issued Ordinary Shares immediately after such issue.

Such adjustment shall become effective on the date of issue of such Ordinary Shares or if a record date is fixed therefor, immediately after such record date; *provided that* if there are different effective dates for different classes of Ordinary Shares, the effective date of the Class B Shares will prevail.

(ii) In the case of an issue of Ordinary Shares of any class by way of a Scrip Dividend where the aggregate value of such Ordinary Shares issued by way of Scrip Dividend as determined by reference to the Current Market Price per Ordinary Share exceeds 105 per cent. of the amount of the Relevant Cash Dividend or the relevant part thereof and which would not have constituted a Capital Distribution, the Conversion Price shall be adjusted by multiplying the Conversion Price in force immediately before the issue of such Ordinary Shares by the following fraction:

$$\frac{A + B}{A + C}$$

Where:

A is the aggregate nominal amount of the issued Ordinary Shares of all classes immediately before such Scrip Dividend;

B is the aggregate nominal amount of Ordinary Shares issued by way of such Scrip Dividend multiplied by a fraction of which (i) the numerator is the amount of the whole, or the relevant part, of the Relevant Cash Dividend for which Ordinary Shareholders have elected to receive as Ordinary Shares issued by way of Scrip Dividend, and (ii) the denominator is the aggregate value of such Ordinary Shares issued by way of Scrip Dividend as determined by reference to the Current Market Price; and

C is the aggregate nominal amount of Ordinary Shares issued by way of such Scrip Dividend.

Such adjustment shall become effective on the date of issue of such Ordinary Shares or if a record date is fixed therefor, immediately after such record date; *provided that* if there are different effective dates for different classes of Ordinary Shares, the effective date of the Class B Shares will prevail.

(3) **Capital Distributions**: If and whenever the Guarantor shall pay or make any Capital Distribution to the Ordinary Shareholders (except to the extent that the Conversion Price falls to be adjusted under Condition 6(C)(2) above), the Conversion Price shall be adjusted by multiplying the Conversion Price in force immediately before such Capital Distribution by the following fraction:

$$\frac{A - B}{A}$$

Where:

A is the Current Market Price per Ordinary Share of such class on the date on which the Capital Distribution is first publicly announced; and

B is the Fair Market Value on the date of such announcement of the portion of the Capital Distribution attributable to one Ordinary Share.

Such adjustment shall become effective on the date that such Capital Distribution is actually made or if a record date is fixed therefor, immediately after such record date; *provided that* if there are different effective dates for different classes of Ordinary Shares, the effective date of the Class B Shares will prevail. For the purpose of the above, Fair Market Value shall (subject as provided in the definition of "Fair Market Value" in Condition 6(F) below) be determined as at the date on which the Capital Distribution is first publicly announced or, if later, the first date on which the Fair Market Value of the relevant Capital Distribution is capable of being determined as provided herein.

In making any calculation pursuant to this Condition 6(C)(3), such adjustments (if any) shall be made as an Independent Investment Bank may consider appropriate to reflect (a) any consolidation or subdivision of the Ordinary Shares, (b) issues of Ordinary Shares by way of capitalization of profits or reserves, or any like or similar event, (c) the modification of any rights to dividends of Ordinary Shares or (d) any change in the fiscal year of the Guarantor.

(4) **Rights Issues of Ordinary Shares or Options over Ordinary Shares**: If and whenever the Guarantor shall issue Ordinary Shares of one or more classes to all or substantially all holders of Ordinary Shares of such classes by way of rights, or issue or grant to all or substantially all Ordinary Shareholders of such classes by way of rights, options, warrants or other rights to subscribe for, purchase or otherwise acquire any Ordinary Shares of such classes, in each case at less than 95 per cent. of the Current Market Price per Ordinary Share on the date of the first public announcement of the terms of the issue or grant, the Conversion Price shall be adjusted by multiplying the Conversion Price in force immediately before such issue or grant by the following fraction:

$$\frac{A + B}{A + C}$$

Where:

A is the aggregate number of Ordinary Shares of all classes in issue immediately before such announcement;

B is the number of Ordinary Shares which the aggregate consideration receivable for the Ordinary Shares issued by way of rights or for the options or warrants or other rights issued or granted by way of rights and for the total number of Ordinary Shares comprised therein would subscribe for, purchase or otherwise acquire at such Current Market Price per Ordinary Share; and

C is the aggregate number of Ordinary Shares issued or, as the case may be, comprised in the issue or grant.

Such adjustment shall become effective on the date of issue of such Ordinary Shares or issue or grant of such options, warrants or other rights (as the case may be) or where a record date is set, the first date on which the Ordinary Shares are traded ex-rights, ex-options or ex-warrants, as the case may be.

(5) **Rights Issues of Other Securities**: In respect of each class of Ordinary Shares, if and whenever the Guarantor shall issue any securities (other than Ordinary Shares or options, warrants or other rights to subscribe for, purchase or otherwise acquire Ordinary Shares) to all or substantially all Ordinary Shareholders of such class by way of rights, or issue or grant to all or substantially all Ordinary Shareholders of such class by way of rights, options, warrants or other rights to subscribe for, purchase or otherwise acquire any securities (other than Ordinary Shares or options, warrants or other rights to subscribe for,

purchase or otherwise acquire Ordinary Shares), the Conversion Price shall be adjusted by multiplying the Conversion Price in force immediately before such issue or grant by the following fraction:

$$\frac{A - B}{A}$$

Where:

A is the Current Market Price per Ordinary Share on the date on which such issue or grant is publicly announced; and

B is the Fair Market Value per Ordinary Share on the date of such announcement of the portion of the rights attributable to one Ordinary Share.

Such adjustment shall become effective on the date of issue of the securities or the issue or grant of such rights, options or warrants (as the case may be) or where a record date is set, the first date on which the Ordinary Shares are traded ex-rights, ex-options or ex-warrants, as the case may be; *provided that* if there are different effective dates for different classes of Ordinary Shares, the effective date of the Class B Shares will prevail. For the purpose of the above, Fair Market Value shall (subject as provided in the definition of "Fair Market Value" in Condition 6(F) below) be determined as at the date on which the terms of such issue or grant are publicly announced, or if later, the first date on which the Fair Market Value of the aggregate rights attributable to the Ordinary Shares in relation to such issue or grant is capable of being determined as provided herein.

(6) **Issues at less than Current Market Price**: If and whenever the Guarantor shall issue (otherwise than as mentioned in Condition 6(C)(4) above) any Class B Shares (other than Class B Shares issued on the exercise of Conversion Rights or on the exercise of any other rights of conversion into, or exchange or subscription for, Class B Shares) or issue or grant (otherwise than as mentioned in Condition 6(C)(4) above) options, warrants or other rights (other than the Conversion Rights under the Bonds, which excludes any further bonds issued pursuant to Condition 17) to subscribe for, purchase or otherwise acquire Class B Shares, in each case at a price per Class B Share which is less than 95 per cent. of the Current Market Price per Class B Share on the date of the first public announcement of the terms of such grant or issue, the Conversion Price shall be adjusted by multiplying the Conversion Price in force immediately before such issue by the following fraction:

$$\frac{A + B}{C}$$

Where:

A is the aggregate number of Ordinary Shares of all classes in issue immediately before the issue of such additional Class B Shares or the grant of such options, warrants or other rights to subscribe for, purchase or otherwise acquire any Class B Shares;

B is the number of Class B Shares which the aggregate consideration receivable for the issue of the maximum number of Class B Shares to be issued or the exercise of such options, warrants or other rights would purchase at such Current Market Price per Class B Share; and

C is the aggregate number of Ordinary Shares in issue immediately after the issue of such additional Class B Shares.

References to additional Class B Shares in the above formula shall, in the case of an issue by the Guarantor of options, warrants or other rights to subscribe or purchase Class B Shares, mean such Class B Shares to be issued assuming that such options, warrants or other rights are exercised in full at the initial exercise price or rate on the date of issue or grant of such options, warrants or other rights.

Such adjustment shall become effective on the date of issue of such additional Class B Shares or, as the case may be, the issue or grant of such options, warrants or other rights.

(7) **Other Issues at less than Current Market Price**: Save in the case of an issue of securities arising from a conversion or exchange of other securities in accordance with the terms applicable to such securities themselves falling within this Condition 6(C)(7), if and whenever the Guarantor or any of its Subsidiaries (otherwise than as mentioned in Conditions 6(C)(4), 6(C)(5) or 6(C)(6)), or (at the direction or request of or pursuant to any arrangements with the Guarantor or any of its Subsidiaries) any other company, person or entity shall issue any securities (other than the Bonds) which by their terms of issue carry rights of conversion into, or exchange or subscription for, Class B Shares to be issued by the Guarantor upon conversion, exchange or subscription at a consideration per Class B Share which is less than 95 per cent. of the Current Market Price per Class B Share on the date of the first public announcement of the terms of issue of such securities, the Conversion Price shall be adjusted by multiplying the Conversion Price in force immediately before such issue by the following fraction:

$$\frac{A + B}{A + C}$$

Where:

A is the aggregate number of Ordinary Shares of all classes in issue immediately before such issue;

B is the number of Class B Shares which the aggregate consideration receivable by the Guarantor for the Class B Shares to be issued on conversion or exchange or on exercise of the right of subscription attached to such securities would purchase at such Current Market Price per Class B Share; and

C is the maximum number of Class B Shares to be issued on conversion or exchange of such securities or on the exercise of such rights of subscription attached thereto at the initial conversion, exchange or subscription price or rate on the issue date of such securities.

Such adjustment shall become effective on the date of issue of such securities.

(8) **Modification of Rights of Conversion etc.**: If and whenever there shall be any modification of the rights of conversion, exchange or subscription attaching to any such securities as are mentioned in Condition 6(C)(7) (other than in accordance with the terms of such securities) so that the consideration per Class B Share (for the number of Class B Shares available on conversion, exchange or subscription following the modification) is reduced and is less than 95 per cent. of the Current Market Price per Class B Share on the date of announcement of the proposals for such modification, the Conversion Price shall be adjusted by multiplying the Conversion Price in force immediately before such modification by the following fraction:

$$\frac{A + B}{A + C}$$

Where:

A is the aggregate number of Ordinary Shares of all classes in issue immediately before such modification;

B is the maximum number of Class B Shares which the aggregate consideration receivable by the Guarantor for the Class B Shares to be issued on conversion or exchange or on exercise of the right of subscription attached to the securities so modified would purchase at such Current Market Price per Class B Share or, if lower, the existing conversion, exchange or subscription price of such securities; and

C is the maximum number of Class B Shares to be issued on conversion or exchange of such securities or on the exercise of such rights of subscription, purchase or acquisition attached thereto at the modified conversion, exchange or subscription price or rate but giving credit in such manner as an Independent Investment Bank considers appropriate (if at all) for any previous adjustment under this Condition 6(C)(8) or under Condition 6(C)(7).

Such adjustment shall become effective on the date of modification of the rights of conversion, exchange or subscription attaching to such securities.

(9) **Other Offers to Ordinary Shareholders**: In respect of each class of Ordinary Shares, if and whenever the Guarantor or any of its Subsidiaries or (at the direction or request of or pursuant to any arrangements with the Guarantor or any of its Subsidiaries) any other company, person or entity issues, sells or distributes any securities in connection with an offer pursuant to which the Ordinary Shareholders of such class generally are entitled to participate in arrangements whereby such securities may be acquired by them (except where the Conversion Price falls to be adjusted under Conditions 6(C)(4), 6(C)(5), 6(C)(6) or 6(C)(7)), the Conversion Price shall be adjusted by multiplying the Conversion Price in force immediately before such issue, sale or distribution by the following fraction:

$$\frac{A - B}{A}$$

Where:

A is the Current Market Price per Ordinary Share on the date on which such issue, sale or distribution is publicly announced; and

B is the Fair Market Value of the portion of the rights attributable to one Ordinary Share.

Such adjustment shall become effective on the date of issue, sale or distribution of the securities or, if a record date is fixed therefor, immediately after such record date or if later, the first date upon which the Fair Market Value of the relevant securities is capable of being determined as provided herein; *provided that* if there are different effective dates for different classes of Ordinary Shares, the effective date of the Class B Shares will prevail. For the purpose of the above, Fair Market Value shall (subject as provided in the definition of "Fair Market Value" in Condition 6(F) below) be determined as at the date on which the terms of such issue, sale or distribution of securities are first publicly announced or, if later, the first date on which the Fair Market Value of the portion of the aggregate rights attributable to the Ordinary Shares is capable of being determined as provided herein.

(10) **Other Events**: If the Guarantor determines that an adjustment should be made to the Conversion Price as a result of one or more events or circumstances not referred to in this Condition 6, the Issuer or the Guarantor shall, at its own expense, consult an Independent Investment Bank to determine as soon as practicable what adjustment (if any) to the Conversion Price is fair and reasonable to take account thereof, if the adjustment would result in a reduction in the Conversion Price, and the date on which such adjustment should take effect and upon such determination by the Independent Investment Bank such adjustment (if any) shall be made and shall take effect in accordance with such determination, *provided that* where the events or circumstances giving rise to any adjustment pursuant to this Condition 6 have already resulted or will result in an adjustment to the Conversion Price or where the events or circumstances giving rise to any adjustment arise by virtue of events or circumstances which have already given rise or will give rise to an adjustment to the Conversion Price, such modification (if any) shall be made to the operation of the provisions of this Condition 6 as may be advised by the Independent Investment Bank to be in its opinion appropriate to give the intended result. Notwithstanding the foregoing, the per Class B Share value of any such adjustment shall not exceed the per Class B Share value of the dilution in the interest of holders of Class B Shares (**"Class B Shareholders"**) in the Guarantor's equity caused by such events or circumstances.

(11) **Adjustment upon Change of Control**: If a Change of Control shall occur, the Issuer shall give to Bondholders notice of that fact (a "**Change of Control Notice**") in accordance with Condition 11 within 14 days after it becomes aware of such Change of Control. Following the giving of a Change of Control Notice, upon any exercise of Conversion Rights such that the relevant Conversion Date falls within 30 days following a Change of Control, or, if later, 30 days following the date on which the Change of Control Notice is given to Bondholders (such period, the "**Change of Control Conversion Period**"), the Conversion Price shall be adjusted in accordance with the following formula:

$$NCP = \frac{OCP}{1+(CP x \frac{c}{t})}$$

Where:

NCP is the Conversion Price after such adjustment;

OCP is the Conversion Price in effect on the relevant Conversion Date before such adjustment;

CP is the conversion premium of 55.0 per cent. expressed as a fraction;

c is the number of days from and including the date the Change of Control occurs to but excluding the Maturity Date; and t is the number of days from and including the Issue Date to but excluding the Maturity Date,

provided that the Conversion Price shall not be reduced pursuant to this Condition 6(C)(12) below the level permitted by applicable laws and regulations from time to time (if any).

If the last day of a Change of Control Conversion Period shall fall during a Restricted Transfer Period, the Change of Control Conversion Period shall be extended such that its last day will be the fifteenth day following the last day of the Restricted Transfer Period.

On the Class B Share Stock Exchange Business Day immediately following the last day of the Change of Control Conversion Period, the Conversion Price shall be re-adjusted to the Conversion Price in force immediately before the adjustment to the Conversion Price during the Change of Control Conversion Period.

**(D) Undertakings**

The Guarantor has undertaken in the Trust Deed, *inter alia*, that so long as any Bond remains outstanding, save with the approval of an Extraordinary Resolution of the Bondholders:

(i) it will use all reasonable endeavors (a) to maintain a listing for all the issued Class B Shares on the Hong Kong Stock Exchange, and (b) to obtain and maintain a listing for all the Class B Shares issued on the exercise of the Conversion Rights on the Hong Kong Stock Exchange, and if the Guarantor is unable to obtain or maintain such listing, or the maintenance of such listing is unduly onerous, to use all reasonable endeavors to obtain and maintain a listing for all the issued Class B Shares on an Alternative Stock Exchange as the Guarantor may from time to time determine and will forthwith give notice to the Bondholders in accordance with Condition 11 of the listing or delisting of the Class B Shares (as a class) by any such stock exchange;

(ii) it will use all reasonable endeavors to maintain or procure that the Issuer maintains the listing of the Bonds on the Hong Kong Stock Exchange and if the Guarantor is unable to maintain or procure the maintenance of such listing, or the maintenance of such listing is unduly onerous, it will use all reasonable endeavors to obtain and maintain or procure that the Issuer obtains and maintains a listing on another internationally recognized stock exchange as the Issuer may from time to time determine and it will forthwith give or procure that the Issuer gives notice to the Bondholders in accordance with Condition 11 of the listing or delisting of the Bonds by any such stock exchange;

(iii) it will pay the expenses of the issue of, and all expenses of obtaining a listing for, Class B Shares arising on conversion of the Bonds (save for the Duties payable by the relevant Bondholder specified in Condition 6(B)(ii)); and

(iv) it will not make any reduction of its ordinary share capital or any uncalled liability in respect thereof or of any share premium account or capital redemption reserve fund except, in each case, where the reduction is permitted by applicable law and results in (or would, but for the provision of these Conditions relating to rounding or the carry forward of adjustments, result in) an adjustment to the Conversion Price or is otherwise taken into account for the purposes of determining whether such an adjustment should be made, *provided always that* the Guarantor shall not be prohibited from purchasing its Class B Shares to the extent permitted by law.

In the Trust Deed, the Guarantor has also undertaken to the Trustee that so long as any Bond remains outstanding:

(I) it will reserve, free from any other pre-emptive or other similar rights, out of its authorized but unissued ordinary share capital the full number of Class B Shares liable to be issued on conversion of the Bonds from time to time remaining outstanding and shall ensure that all Class B Shares delivered on conversion of the Bonds will be duly and validly issued as fully-paid; and

(II) it will not make any offer, issue, grant or distribute or take any action the effect of which would be to reduce the Conversion Price below the par value of the Class B Shares of the Guarantor, *provided always that* the Guarantor shall not be prohibited from purchasing its Class B Shares to the extent permitted by law.

The Guarantor has also given certain other undertakings in the Trust Deed for the protection of the Conversion Rights.

**(E) Provisions Relating to Changes in Conversion Price**

(i) *Minor adjustments*: On any adjustment, the resultant Conversion Price, if not an integral multiple of one Hong Kong cent, shall be rounded down to the nearest Hong Kong cent. No adjustment shall be made to the Conversion Price if such adjustment (rounded down if applicable) would be less than one per cent. of the Conversion Price then in effect. Any adjustment not required to be made, and/or any amount by which the Conversion Price has been rounded down, shall be carried forward and taken into account in any subsequent adjustment, and such subsequent adjustment shall be made on the basis that the adjustment not required to be made had been made at the relevant time and/or, as the case may be, that the relevant rounding down had not been made. Notice of any adjustment shall be given by the Issuer to Bondholders in accordance with Condition 11 and to the Trustee as soon as reasonably practicable after the determination thereof.

(ii) *Decision of an Independent Investment Bank*: If any doubt shall arise as to whether an adjustment falls to be made to the Conversion Price or as to how an adjustment to the Conversion Price under Condition 6(C) should be made, and following consultation between the Issuer, the Guarantor and an Independent Investment Bank, a written opinion of such Independent Investment Bank in respect thereof shall be conclusive and binding on the Issuer, the Guarantor, the Bondholders and the Trustee, save in the case of manifest error. Notwithstanding the foregoing, the per Class B Share value of any such adjustment shall not exceed the per Class B Share value of the dilution in the shareholders' interest in the Guarantor's equity caused by such events or circumstances.

(iii) *Minimum Conversion Price*: Notwithstanding the provisions of this Condition 6, the Issuer undertakes that: (a) the Conversion Price shall not in any event be reduced to below the nominal or par value of the Class B Shares as a result of any adjustment hereunder unless under applicable law then in effect the Bonds may be converted at such reduced Conversion Price into legally issued, fully paid and non-assessable Class B Shares; and (b) it shall not take any action, and shall procure that no action is taken, that would otherwise result in an adjustment to the Conversion Price to below such nominal or par value or any minimum level permitted by applicable laws or regulations.

(iv) *Reference to "fixed"*: Any references herein to the date on which a consideration is "fixed" shall, where the consideration is originally expressed by reference to a formula which cannot be expressed as an actual cash amount until a later date, be construed as a reference to the first day on which such actual cash amount can be ascertained.

(v) *Multiple events*: Where more than one event which gives or may give rise to an adjustment to the Conversion Price occurs within such a short period of time that in the opinion of an Independent Investment Bank, the foregoing provisions would need to be operated subject to some modification in order to give the intended result, such modification shall be made to the operation of the foregoing provisions as may be advised by such Independent Investment Bank to be in its opinion appropriate in order to give such intended result.

(vi) *Upward/downward adjustment*: No adjustment involving an increase in the Conversion Price will be made, except in the case of a consolidation or re-classification of the Class B Shares as referred to in Condition 6(C)(1) above. The Issuer may at any time and for a specified period of time only, following notice being given to the Trustee and the Principal Agent in writing and to the Bondholders in accordance with Condition 11, reduce the Conversion Price, subject to Condition 6(E)(iii).

(vii) *Not obliged to Monitor*: Neither the Trustee nor any Agent shall be under any duty to monitor whether any event or circumstance has happened or exists which may require or may lead to an adjustment to be made to the Conversion Price or to make any determination or calculation (or any verification thereof) in connection with the Conversion Price and none of them will be responsible or liable to Bondholders or any other person for any loss arising from any failure by the Trustee or any Agent to do so or for any delay by the Issuer, the Guarantor or any Independent Investment Bank in making a determination or calculation or any erroneous determination or calculation in connection with the Conversion Price. All adjustments to the Conversion Price under Condition 6(C) shall be determined by the Issuer, the Guarantor and, if applicable, the Independent Investment Bank (as specified in this Condition 6) and neither the Trustee nor the Agents shall be responsible for verifying, or otherwise liable for, such determinations or for verifying any calculation, certification, advice or opinion in connection with such determinations.

(viii) *Notice of Change in Conversion Price*: The Issuer (failing which, the Guarantor) shall give notice to the Trustee and the Principal Agent in writing and to the Bondholders in accordance with Condition 11 and, for so long as the Bonds are listed on the Hong Kong Stock Exchange, to the Hong Kong Stock Exchange of any change in the Conversion Price. Any such notice relating to a change in the Conversion Price shall set forth the event giving rise to the adjustment, the Conversion Price prior to such adjustment, the adjusted Conversion Price and the effective date of such adjustment.

(ix) *No adjustment*: Notwithstanding any provision in this Condition 6, no adjustment will be made to the Conversion Price when (i) Class B Shares or other securities (including rights or options) are issued, offered, exercised, allotted or granted to, or for the benefit of employees (including directors) of the Guarantor or any of its Subsidiaries pursuant to any share option, share award, restricted share or employee share incentive scheme or plan (and which share scheme or plan is in compliance with the listing rules of the Relevant Stock Exchange) ("**Share Scheme Shares/Options**") unless any grant or issue of Share Scheme Shares/Options (which, but for this Condition 6(E)(ix), would have required adjustment pursuant to Condition 6) would result in the total number of Class B Shares which may be issued upon exercise of such Share Scheme Shares/Options granted during any 12-month period up to and including the date of such grant representing, in aggregate, over 3.0 per cent. of the average number of issued and outstanding Class B Shares during such 12-month period, in which case only such portion of the grant or issue of Share Scheme Shares/Options that exceeds 3.0 per cent. of the average number of issued and outstanding Class B Shares during the relevant 12-month period shall be taken into account in determining adjustment of the Conversion Price pursuant to Condition 6, or (ii) Class B Shares are issued upon conversion of Class A Shares into Class B Shares on a one to one basis.

**(F) Definitions**

For the purposes of these Conditions:

"**Alternative Stock Exchange**" means at any time, in the case of the Class B Shares, if they are not at that time listed and traded on the Hong Kong Stock Exchange, the principal stock exchange or securities market on which the Class B Shares are then listed or quoted or dealt in;

"**Capital Distribution**" means, on a per Class B Share basis, (i) the aggregate distribution of assets *in specie* by the Guarantor for any financial period whenever paid or made and however (and for these purposes a distribution of assets *in specie* includes, without limitation, an issue of Class B Shares or other securities credited as fully or partly paid by way of capitalization of reserves, but excludes any Class B Shares credited as fully paid to the extent an adjustment to the Conversion Price is made in respect hereof under Condition 6(C)(2)(i) and a Scrip Dividend adjusted for under Condition 6(C)(2)(ii)); and (ii) the aggregate cash dividend or distribution on a gross basis (including, without limitation, the relevant cash amount of a Scrip Dividend) of any kind by the Guarantor for any financial period (whenever paid and however described) unless it comprises a purchase or redemption of Class B Shares by or on behalf of the Guarantor (or a purchase of Class B Shares by or on behalf of a Subsidiary of the Guarantor), where the weighted average price or consideration per Class B Share (before expenses) on any one day in respect of such purchases does not exceed the Current Market Price of the Class B Shares by more than five per cent. either (a) on that date, or (b) where an announcement has been made of the intention to purchase Class B Shares at some future date at a specified price, on the Trading Day immediately preceding the date of such announcement and, if in the case of either (a) or (b), the relevant day is not a Trading Day, the immediately preceding Trading Day. In the event the weighted average price or consideration per Class B Share of such purchase or redemption of Class B Shares does exceed the Current Market Price of the Class B Shares by the amount referred to in this definition, for the purposes of the adjustment in Condition 6(C)(3), "**Capital Distribution**" shall mean the portion of such weighted average price or consideration per Class B Share which exceeds such amount;

a "**Change of Control**" occurs when:

(i) any Person or Persons acting together, except where such Person(s) is Controlled by the Permitted Holders, acquires Control of the Guarantor;

(ii) the Guarantor consolidates with or merges into or sells or transfers all or substantially all of the assets of the Guarantor to any other Person or Persons acting together, except where such Person(s) is Controlled by the Permitted Holders;

(iii) the Permitted Holders together cease to hold (directly or indirectly) at least 50.0 per cent. of the voting rights of the issued share capital of the Guarantor; or

(iv) the Guarantor ceases to hold (directly or indirectly) 100 per cent. of the issued shares of the Issuer;

"**Closing Price**" means, in respect of a Class B Share for any Trading Day, the price published in the Daily Quotation Sheet published by the Hong Kong Stock Exchange or, as the case may be, the equivalent quotation sheet of an Alternative Stock Exchange for such Trading Day;

"**Control**" means the acquisition or control of more than 50 per cent. of the Voting Rights of the issued share capital of the Guarantor or the right to appoint and/or remove all or the majority of the members of the Guarantor's board of directors or other governing body, whether obtained directly or indirectly, and whether obtained by ownership of share capital, the possession of Voting Rights, contract or otherwise;

"**Current Market Price**" means, in respect of an Ordinary Share on a particular date, the average of the Closing Prices for one Ordinary Share (being an Ordinary Share carrying full entitlement to dividend) on each of the 20 consecutive Trading Days ending on including (i) the Trading Day immediately preceding such date or (ii) if the relevant announcement was made after the close of trading on such day (being a Trading Day), such date of announcement, provided that if at any time during such 20 Trading Day-period the Ordinary Shares of such class shall have been quoted ex-dividend (or ex-any other entitlement) and during some other part of that period the Ordinary Shares of such class shall have been quoted cum-dividend (or cum-any other entitlement) then:

(a) if the Ordinary Shares of such class to be issued in such circumstances do not rank for the dividend (or other entitlement) in question, the Closing Price on the dates on which the Ordinary Shares of such class shall have been quoted cum-dividend (or cum-any other entitlement) shall for the purpose of this definition be deemed to be the amount thereof reduced by an amount equal to the Fair Market Value of any such dividend or other entitlement per Ordinary Share of such class; or

(b) if the Ordinary Shares of such class to be issued in such circumstances rank for the dividend (or other entitlement) in question, the Closing Price on the dates on which the Ordinary Shares of such class shall have been quoted ex-dividend (or ex-any other entitlement) shall for the purpose of this definition be deemed to be the amount thereof increased by the Fair Market Value of any such dividend or other entitlement per Ordinary Share of such class,

*provided further that* if the Ordinary Shares of such class on each of the said 20 Trading Days have been quoted cum-dividend (or cum-any other entitlement) in respect of a dividend (or other entitlement) which has been declared or announced but the Ordinary Shares to be issued do not rank for that dividend, the Closing Price on each of such dates shall for the purpose of this definition be deemed to be the amount thereof reduced by an amount equal to the Fair Market Value of any such dividend or other entitlement per Ordinary Share of such class, and *provided further that* in respect of a Class A Share on a particular date, the "Current Market Price" of such Class A Share shall mean the Current Market Price of a Class B Share on such date as determined in accordance with the foregoing definition;

"**Dollar Equivalent**" means, with respect to any monetary amount in a currency other than U.S. dollars, at any time for the determination thereof, the amount of U.S. dollars obtained by converting such foreign currency involved in such computation into U.S. dollars at the base rate for the purchase of U.S. dollars with the applicable foreign currency as quoted by the Federal Reserve Bank of New York on the date of determination;

"**Fair Market Value**" means, with respect to any asset, security, option, warrant or other right on any date, the fair market value of that asset, security, option, warrant or other right as determined by an Independent Investment Bank on the basis of commonly accepted market valuation method and taking into account such factors as it considers appropriate, provided that an Independent Investment Bank will not be required to determine the fair market value where (i) the Capital Distribution is paid in cash, in which case the fair market value of such cash Capital Distribution per Class B Share shall be the amount of such cash Capital Distribution per Class B Share, (ii) any other amounts are paid in cash, in which case the fair market value of such cash amount shall be the amount of cash, and (iii) options, warrants or other rights or securities are or will upon issuance be publicly traded in a market of adequate liquidity (as determined by such Independent Investment Bank), the fair market value of such options, warrants or other rights or securities shall equal the arithmetic mean of the daily closing price of such options, warrants or other rights or securities during the period of 10 Trading Days on the relevant market commencing on the first such Trading Day such options, warrants or other rights or securities are publicly traded. Such amounts, if expressed in a currency other than HK dollars shall be translated into HK dollars at the Prevailing Rate on such date. In addition, in the case of proviso (i) and (ii) above in this definition, the Fair Market Value shall be determined on a gross basis and disregarding any withholding or deduction required to be made for or on account of tax and disregarding any associated tax credit;

"**Hong Kong Stock Exchange**" means The Stock Exchange of Hong Kong Limited or its successor thereto;

"**Independent Investment Bank**" means an independent investment bank of international repute (acting as an expert) selected and appointed by the Issuer and notified in writing by the Trustee. If the Issuer fails to select and appoint an Independent Investment Bank when required by these Conditions, the Trustee shall not be responsible for or under any obligation to select or appoint an Independent Investment Bank;

"**Permitted Holders**" means the aggregate shareholding of Mr. Lei Jun and Mr. Lin Bin, and:

(i) any heir, estate, lineal descendent (or spouse thereof), spouse or parent of any of Mr. Lei Jun or Mr. Lin Bin; or

(ii) any trust, corporation, partnership or other entity, of which the direct or indirect beneficiaries, equity holders, partners or owners are any of Mr. Lei Jun or Mr. Lin Bin and/or such other Persons referred to in paragraph (i) above;

"**Prevailing Rate**" means, in respect of any currency on any day, the bid exchange rate between the relevant currencies prevailing as at or about 12:00 noon (Hong Kong time) on that date as appearing on or derived from the Relevant Page or, if such a rate cannot be determined at such time, the rate prevailing as at or about 12:00 noon (Hong Kong time) on the immediately preceding day on which such rate can be so determined;

"**Relevant Cash Dividend**" means the aggregate cash dividend or distribution declared by the Guarantor, including any cash dividend in respect of which there is any Scrip Dividend;

a "**Relevant Event**" occurs:

(i) when the Class B Shares cease to be listed or admitted to trading or are suspended from trading for a period equal to or exceeding 30 consecutive Trading Days on the Relevant Stock Exchange; or

(ii) when there is a Change of Control; or

(iii) when (a) there is any change in or amendment to the laws, regulations and rules of the PRC or the official interpretation or official application thereof (a "**Change in Law**") that results in (x) the Guarantor and its Controlled Entities (collectively, the "**Group**") (as in existence immediately subsequent to such Change in Law), as a whole, being legally prohibited from operating substantially all of the business operations conducted by the Group (as in existence immediately prior to such Change in Law) as of the last date of the period described in the Guarantor's consolidated financial statements for the most recent fiscal quarter and (y) the Guarantor being unable to continue to derive substantially all of the economic benefits from the business operations conducted by the Group (as in existence immediately prior to such Change in Law) in the same manner as reflected in the Guarantor's consolidated financial statements for the most recent fiscal quarter and (b) the Guarantor has not furnished to the Trustee, prior to the date that is 12 months after the date of the Change in Law, an opinion from an independent financial adviser or external legal counsel stating either (x) that the Guarantor is able to continue to derive substantially all of the economic benefits from the business operations conducted by the Group (as in existence immediately prior to such Change in Law), taken as a whole, as reflected in the Guarantor's consolidated financial statements for the most recent fiscal quarter (including after giving effect to any corporate restructuring or reorganization plan of the Guarantor) or (y) that such Change in Law would not materially adversely affect the Issuer's and the Guarantor's ability to make principal and premium (if any) payments on the Bonds when due or to convert the Bonds in accordance with these Conditions;

"**Relevant Page**" means the relevant Bloomberg BFIX page (or its successor page) or, if there is no such page, on the relevant Reuters HKDFIX page (or its successor page) or such other information service provider that displays the relevant information;

"**Relevant Stock Exchange**" means at any time, in respect of the Class B Shares, the Hong Kong Stock Exchange or the Alternative Stock Exchange;

"**Scrip Dividend**" means any Class B Shares issued in lieu of the whole or any part of any Relevant Cash Dividend, being a dividend which the Class B Shareholders concerned would or could otherwise have received (and for the avoidance of doubt, to the extent that an adjustment is made under Condition 6(C)(3) in respect of the Relevant Cash Dividend, no adjustment is to be made for the amount by which the Current Market Price of the Class B Shares exceeds the Relevant Cash Dividend or part thereof for which an adjustment is already made under Condition 6(C)(2)(ii));

"**Stated Maturity**" means, when used with respect to any Bond, the date specified in such Bond as the fixed date on which the principal (or any portion thereof) of or premium, if any, on such Bond is due and payable;

"**Trading Day**" means a day when the Hong Kong Stock Exchange or, as the case may be, an Alternative Stock Exchange is open for dealing business, provided that if no closing price is reported for one or more consecutive dealing days such day or days will be disregarded in any relevant calculation and shall be deemed not to have been dealing days when ascertaining any period of dealing days;

"**Total Equity**" means of any date, means the total equity attributable to shareholders of the Guarantor on a consolidated basis determined in accordance with IFRS, as shown on the Guarantor's consolidated balance sheet for the most recent fiscal quarter; and

"**Voting Rights**" means the right generally to vote at a general meeting of shareholders of the Guarantor.

References to any issue or offer or grant to Class B Shareholders "**as a class**" or "**by way of rights**" shall be taken to be references to an issue or offer or grant to all or substantially all Class B Shareholders, other than Class B Shareholders by reason of the laws of any territory or requirements of any recognized regulatory body or any other stock exchange or securities market in any territory or in connection with fractional entitlements, it is determined not to make such issue or offer or grant.

## 7 Payments

### (A) Method of Payment

Payment of principal and default interest (if any) and any other amount due will be made by transfer to the registered account of the Bondholder. Such payment will only be made after surrender of the relevant Certificate at the specified office of the Principal Agent or any of the other Paying Agents.

If an amount which is due on the Bonds is not paid in full, the Registrar will annotate the Register with a record of the amount (if any) in fact paid.

*So long as the Bonds are represented by the Global Certificate and the Global Certificate is held on behalf of Euroclear or Clearstream (each, a "**relevant clearing system**"), each payment* *of principal of, and any other amounts due under, the Bonds evidenced by the Global Certificate will be made to the person shown as the holder thereof in the Register at the close of business (in the relevant clearing system) on the Clearing System Business Day before the due date for such payment, where "**Clearing System Business Day**" means Monday to Friday inclusive except December 25 and January 1.*

**(B) Registered Accounts**

For the purposes of this Condition 7, a Bondholder's registered account means the U.S. dollar account maintained by or on behalf of it with a bank in New York City, details of which appear on the Register at the close of business on the fifteenth Payment Business Day (as defined in Condition 7(F) below) before the due date for payment, and a Bondholder's registered address means its address appearing on the Register at that time.

**(C) Payments Subject to Fiscal Laws**

All payments are subject in all cases to (i) any applicable fiscal or other laws, regulations and directives in the place of payment but without prejudice to the provisions of Condition 9 and (ii) any withholding or deduction required pursuant to an agreement described in Section 1471(b) of the U.S. Internal Revenue Code of 1986, as amended (the "**Code**") or otherwise imposed pursuant to Sections 1471 through 1474 of the Code, any regulations or agreements thereunder, any official interpretations thereof, or (without prejudice to the provisions of Condition 9 any law implementing an intergovernmental approach thereto). No commission or expenses shall be charged to the Bondholders in respect of such payments.

**(D) Payment Initiation**

Payment instructions (for value on the due date or, if that is not a Payment Business Day (as defined in Condition 7(F) below), for value on the first following day which is a Payment Business Day) will be initiated on the due date for payment (or, if it is not a Payment Business Day, the immediately following Payment Business Day) or, in the case of a payment of principal, if later, on the Payment Business Day on which the relevant Certificate is surrendered at the specified office of a Paying Agent.

**(E) Delay in Payment**

Bondholders will not be entitled to any interest or other payment for any delay after the due date in receiving the amount due if the due date is not a Payment Business Day, if the Bondholder is late in surrendering its Certificate (if required to do so).

**(F) Payment Business Day**

In this Condition 7, "**Payment Business Day**" means a day other than a Saturday, Sunday or public holiday on which commercial banks are open for business in Hong Kong and the city in which the specified office of the Principal Agent is located and, in the case of the surrender of a Certificate, in the place where the Certificate is surrendered.

**(G) Agents**

The initial Agents and their initial specified offices are listed below. The Issuer and the Guarantor reserve the right at any time, with the prior written approval of the Trustee, to vary or terminate the appointment of any Agent and appoint additional or replacement Agents, provided that they will maintain (i) a Principal Agent, (ii) a Registrar with a specified office outside Hong Kong and the United Kingdom, and (iii) such other agents as may be required by the Hong Kong Stock Exchange. Notice of any changes in any Agent or their specified offices will promptly be given by the Issuer to the Bondholders in accordance with Condition 11.

## 8 Redemption, Purchase and Cancelation

### (A) Maturity

Unless previously redeemed, converted or purchased and canceled as provided herein, the Issuer will redeem each Bond at its principal amount on December 17, 2027 (the "**Maturity Date**"). The Issuer may not redeem the Bonds at its option prior to that date except as provided in Conditions 8(B) or 8(C) (but without prejudice to Conditions 8(D), 8(E) and 10).

### (B) Redemption for Taxation Reasons

The Bonds may be redeemed, at the option of the Issuer in whole, but not in part, at any time, on giving not less than 30 nor more than 60 days' notice (a "**Tax Redemption Notice**") to the Bondholders in accordance with Condition 11 and in writing to the Trustee and the Principal Agent (which notice shall be irrevocable), on the date specified in the Tax Redemption Notice for redemption (the "**Tax Redemption Date**") at their principal amount, if the Issuer satisfies the Trustee immediately prior to the giving of such notice that (i) the Issuer (or if the Guarantee was called, the Guarantor) has or will become obliged to pay Additional Tax Amounts as provided or referred to in Condition 9 as a result of any change in, or amendment to, the laws or regulations of Hong Kong, the Cayman Islands or the PRC or, in any such case, any political subdivision or any authority thereof or therein having power to tax, or any change in the general application or official interpretation of such laws or regulations, which change or amendment becomes effective on or after December 1, 2020, and (ii) such obligation cannot be avoided by the Issuer (or, as the case may be, the Guarantor) taking reasonable measures available to it, provided that no Tax Redemption Notice shall be given earlier than 90 days prior to the earliest date on which the Issuer (or, as the case may be, the Guarantor) would be obliged to pay such Additional Tax Amounts were a payment in respect of the Bonds then due. Prior to the publication of any Tax Redemption Notice pursuant to this Condition 8(B), the Issuer (or, as the case may be, the Guarantor) shall deliver to the Trustee (a) a certificate in English signed by an Authorized Signatory (as defined in the Trust Deed) of the Issuer (or, as the case may be, the Guarantor) stating that the obligation referred to in (i) above of this Condition 8(B) cannot be avoided by the Issuer taking reasonable measures available to it and (b) an opinion of independent legal or tax advisors of recognized standing addressed to the Trustee to the effect that such change or amendment referred to in (i) above of this Condition 8(B) has occurred (irrespective of whether such amendment or change is then effective), and the Trustee shall be entitled (but not obliged) to accept such certificate and opinion (without further investigation or query and without liability to the Bondholders or any other person) as sufficient evidence thereof, in which event the same shall be conclusive and binding on the Bondholders.

On the Tax Redemption Date, the Issuer (subject to the following paragraph of this Condition 8(B)) shall redeem the Bonds at their principal amount.

If the Issuer issues a Tax Redemption Notice, each Bondholder will have the right to elect that his Bond(s) shall not be redeemed and that the provisions of Condition 9 shall not apply in respect of any payment to be made in respect of such Bond(s) which falls due after the relevant Tax Redemption Date, whereupon no Additional Tax Amounts shall be payable in respect thereof pursuant to Condition 9 and payment of all amounts shall be made subject to the deduction or withholding of any taxation required to be withheld or deducted. To exercise such a right, the relevant Bondholder must complete, sign and deposit during normal business hours (being between 9:00 a.m. and 4:00 p.m.) at the specified office of any Paying Agent a duly completed and signed notice of election, substantially in the form as scheduled to the Agency Agreement, obtainable during normal business hours (being between 9:00 a.m. and 4:00 p.m.) from the specified office of any Paying Agent (the "**Tax Option Exercise Notice**") together with the Certificate evidencing the Bonds to be redeemed, on or before the day falling 10 days prior to the Tax Redemption Date. A Tax Option Exercise Notice, once delivered, shall be irrevocable and may not be withdrawn without the Issuer's consent.

**(C) Redemption at the Option of the Issuer**

On giving not less than 30 nor more than 60 days' notice (an "**Optional Redemption Notice**") to the Bondholders in accordance with Condition 11 and to the Trustee and the Principal Agent in writing, the Bonds may be redeemed by the Issuer in whole, but not in part, on the date (the "**Optional Redemption Date**") specified in the Optional Redemption Notice at their principal amount:

(i) at any time after December 17, 2025, provided that the Closing Price of a Class B Share (translated into U.S. dollars at the Prevailing Rate), for 20 out of 30 consecutive Trading Days, the last of which occurs not more than five Trading Days prior to the date of the Optional Redemption Notice, was at least 130 per cent. of the Conversion Price (translated into U.S. dollars at the Fixed Exchange Rate) then in effect immediately prior to the date upon which notice of such redemption is given; or

(ii) at any time if, immediately prior to the date the relevant Optional Redemption Notice is given, Conversion Rights shall have been exercised and/or purchases (and corresponding cancelations) and/or redemptions effected in respect of 90 per cent. or more in principal amount of the Bonds originally issued (which shall for this purpose include any further bonds issued in accordance with Condition 17 and consolidated and forming a single series therewith).

If there shall occur an event giving rise to a change in the Conversion Price during any such 30 consecutive Trading Day period as mentioned in Condition 8(C)(i) above, appropriate adjustments for the relevant days shall be made, as determined by an Independent Investment Bank, for the purpose of calculating the Closing Price for such days.

**(D) Redemption for Relevant Event**

Following the occurrence of a Relevant Event, the holder of each Bond will have the right at such holder's option to require the Issuer to redeem all or some only of such holder's Bonds on the Relevant Event Put Date at their principal amount. To exercise such right, the holder of the relevant Bond must deposit during normal business hours (being between 9:00 a.m. and 4:00 p.m.) at the specified office of any Paying Agent a duly completed and signed notice of redemption, substantially in the form as scheduled to the Agency Agreement, obtainable during normal business hours (being between 9:00 a.m. and 4:00 p.m.) from the specified office of any Paying Agent (a "**Relevant Event Put Exercise Notice**"), together with the Certificate evidencing the Bonds to be redeemed by not later than 60 days following a Relevant Event, or, if later, 60 days following the date upon which notice thereof is given to Bondholders by the Issuer in accordance with Condition 11. The "**Relevant Event Put Date**" shall be the fourteenth day after the expiry of such period of 60 days as referred to above.

A Relevant Event Put Exercise Notice, once delivered, shall be irrevocable and may not be withdrawn without the Issuer's consent. The Issuer shall redeem the Bonds the subject of the Relevant Event Put Exercise Notice (subject to delivery of the relevant Certificate as aforesaid) on the Relevant Event Put Date.

Neither the Trustee nor any of the Agents shall be required to monitor or to take any steps to ascertain whether a Relevant Event or any event which could lead to a Relevant Event has occurred or may occur and none of them will be responsible or liable to Bondholders or any other person for any loss arising from any failure by it to do so, and each of them shall be entitled to assume that no such event has occurred until it has received written notice to the contrary from the Issuer.

The Issuer shall give notice to Bondholders in accordance with Condition 11 by not later than 14 days following the first day on which it becomes aware of the occurrence of a Relevant Event, which notice shall specify the procedure for exercise by holders of their rights to require redemption of the Bonds pursuant to this Condition 8(D) and shall give brief details of the Relevant Event.

**(E) Redemption at the Option of the Bondholders**

The Issuer will, at the option of the holder of any Bond, redeem all or some of that holder's Bonds on December 17, 2025 (the "**Put Option Date**") at the principal amount of the Bonds. To exercise such right, the holder of the relevant Bond must complete, sign and deposit at the specified office of any Paying Agent a duly completed and signed notice (the "**Put Option Notice**") together with the Certificate evidencing the Bonds to be redeemed not earlier than 60 days and not later than 30 days prior to the Put Option Date.

A Put Option Notice, once delivered, shall be irrevocable (and may not be withdrawn unless the Issuer consents to such withdrawal) and the Issuer shall redeem the Bonds the subject of a Put Option Notice delivered as aforesaid on the Put Option Date.

**(F) Purchase**

The Issuer, the Guarantor or any of its Controlled Entities may, in accordance with all applicable laws and regulations, at any time purchase the Bonds in the open market or otherwise at any price, so long as such purchase does not otherwise violate the terms of the Trust Deed or the Bonds. The Bonds so purchased, while held by or on behalf of the Issuer, the Guarantor or any of its Controlled Entities, shall not be deemed to be outstanding for certain purposes, including without limitation for the purpose of calculating quorums at meetings of the Bondholders or for the purposes of Condition 10, Condition 14(a) and Condition 15.

**(G) Cancelation**

All Bonds which are redeemed, converted or purchased by the Issuer, the Guarantor or any of the Guarantor's Subsidiaries, will forthwith be canceled. Certificates in respect of all Bonds canceled will be forwarded to or to the order of the Registrar and such Bonds may not be reissued or resold.

**(H) Redemption Notices**

All notices to Bondholders given by or on behalf of the Issuer pursuant to this Condition 8 will be irrevocable and will be given in accordance with Condition 11 specifying: (i) the Conversion Price as at the date of the relevant notice; (ii) the last day on which Conversion Rights may be exercised; (iii) the Closing Price of the Class B Shares on the latest practicable date prior to the publication of the notice; (iv) the applicable redemption amount; (v) the date for redemption; (vi) the manner in which redemption will be effected; and (vii) the aggregate principal amount of the Bonds outstanding as at the latest practicable date prior to the publication of the notice.

If more than one notice of redemption is given (being a notice given by either the Issuer or a Bondholder pursuant to this Condition 8), the first in time shall prevail. Neither the Trustee nor the Agents shall be responsible for calculating or verifying any calculations of any amounts payable under these Conditions.

**9 Taxation**

All payments made by the Issuer (or, as the case may be, the Guarantor) under or in respect of the Bonds (or, in the case of the Guarantor, the Guarantee), the Trust Deed or the Agency Agreement will be made free from any restriction or condition and be made without deduction or withholding for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature imposed, levied collected, withheld or assessed by Hong Kong, the Cayman Islands or the PRC or, in any such case, any authority thereof or therein having power to tax, unless such deduction or withholding is required by law.

Where such withholding or deduction is made by the Issuer (or, as the case may be, the Guarantor) by or within the PRC up to and including the aggregate rate applicable on December 1, 2020 (the

"**Applicable Rate**"), the Issuer (or, as the case may be, the Guarantor) will increase the amounts paid by it to the extent required, so that the net amount received by Bondholders equals the amounts which would otherwise have been receivable by them had no such withholding or deduction been required.

If the Issuer (or, as the case may be, the Guarantor) is required to make a deduction or withholding (i) by or within the PRC in excess of the Applicable Rate or (ii) by or within Hong Kong or the Cayman Islands, the Issuer (or, as the case may be, the Guarantor) shall pay such additional amounts ("**Additional Tax Amounts**") as will result in the receipt by the Bondholders of such amounts as would have been received by them had no such deduction or withholding been required, except that no Additional Tax Amounts shall be payable in respect of any Bond:

(a) *Other connection*: to a holder (or to a third party on behalf of a holder) who is subject to such taxes, duties, assessments or governmental charges in respect of such Bond by reason of his having some connection with Hong Kong, the Cayman Islands or the PRC otherwise than by the mere holding of the Bond or by the receipt of amounts in respect of the Bond; or

(b) *Presentation more than 30 days after the relevant date*: (in the case of a payment of principal) if the Certificate in respect of such Bond is surrendered more than 30 days after the Relevant Date except to the extent that the holder of it would have been entitled to such additional amounts on surrendering the relevant Certificate for payment on the last day of such period of 30 days.

For the purposes hereof, "**Relevant Date**" means whichever is the later of (x) the date on which such payment first becomes due and (y) if the full amount payable has not been received by the Trustee or the Principal Agent on or prior to such due date, the date on which, the full amount having been so received, notice to that effect shall have been given to the Bondholders and payment made.

References in these Conditions to principal and default interest (if any) shall be deemed also to refer to any additional amounts which may be payable under this Condition 9 or any undertaking or covenant given in addition thereto or in substitution therefor pursuant to the Trust Deed.

Neither the Trustee nor any Agent shall be responsible for paying any tax, duty, assessments or governmental charges, withholding or other payment referred to in this Condition 9 or for determining whether such amounts are payable or the amount thereof, and none of them shall be responsible or liable for any failure by the Issuer, the Guarantor, any Bondholder or any third party to pay such tax, duty, assessments or governmental charges, withholding or other payment in any jurisdiction or to provide any notice or information to the Trustee or any Agent that would permit, enable or facilitate the payment of any principal or other amount under or in respect of the Bonds without deduction or withholding for or on account of any tax, duty, assessments or governmental charge imposed by or in any jurisdiction.

The provisions of this Condition 9 shall not apply in respect of any payments which fall due after the relevant Tax Redemption Date in respect of any Bonds which are the subject of a Bondholder election pursuant to Condition 8(B).

## 10 Events of Default

If any of the following events (each an "**Event of Default**") occurs, the Trustee at its discretion may, and if so requested in writing by the holders of not less than 25 per cent. in aggregate principal amount of the Bonds then outstanding, or if so directed by an Extraordinary Resolution, shall (subject to being indemnified and/or secured and/or pre-funded by the holders to its satisfaction), give notice to the Issuer and the Guarantor that the Bonds are, and they shall immediately become due and repayable at their principal amount (subject as provided below and without prejudice to the right of Bondholders to exercise the Conversion Right in respect of their Bonds in accordance with Condition 6):

(i) there is a failure to pay principal or premium in respect of any Bonds by the due date for such payment (whether at Stated Maturity or upon acceleration, repurchase, redemption or otherwise);

(ii) there is a failure by the Guarantor to deliver any Class B Shares as and when the Class B Shares are required to be delivered following Conversion of Bonds and such failure continues for a period of three days; or

(iii) the Issuer or the Guarantor does not perform or comply with any one or more of its other obligations in the Bonds or the Trust Deed, which default is in the opinion of the Trustee incapable of remedy or, if in the opinion of the Trustee capable of remedy, is not remedied within 30 days after written notice of such default shall have been given to the Issuer or the Guarantor by the Trustee; or

(iv) (1) there occurs with respect to any indebtedness of the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities, whether such indebtedness now exists or shall hereafter be created, (A) an event of default that has resulted in the holder thereof declaring the principal of such indebtedness to be due and payable prior to its stated maturity or (B) a failure to make a payment of principal or premium when due (after giving effect to the expiration of any applicable grace period therefor, a "**Payment Default**") and (2) the outstanding principal amount of such indebtedness, together with the outstanding principal amount of any other indebtedness of such Persons under which there has been a Payment Default or the maturity of which has been so accelerated, is equal to or exceeds the greater of (x) U.S.$100,000,000 (or the Dollar Equivalent thereof) and (y) 2.5 per cent. of the Guarantor's Total Equity; or

(v) one or more final judgments or orders for the payment of money are rendered against the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities and are not paid or discharged, and there is a period of 90 consecutive days following entry of the final judgment or order that causes the aggregate amount for all such final judgments or orders outstanding and not paid or discharged against all such Persons (net of any amounts that the Guarantor's insurance carriers have paid or agreed to pay with respect thereto under applicable policies) to exceed the greater of (x) U.S.$100,000,000 (or the Dollar Equivalent thereof) and (y) 2.5 per cent. of the Guarantor's Total Equity, during which a stay of enforcement, by reason of a pending appeal or otherwise, is not in effect;

(vi) the entry by a court having jurisdiction in the premises of (i) a decree or order for relief in respect of the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities in an involuntary case or proceeding under any applicable bankruptcy, insolvency or other similar law or (ii) a decree or order adjudging the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities bankrupt or insolvent, or approving as final and non-appealable a petition seeking reorganization, arrangement, adjustment, or composition of or in respect of the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities under any applicable bankruptcy, insolvency or other similar law, or appointing a custodian, receiver, liquidator, assignee, trustee, sequestrator, or other similar official of the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities or of any substantial part of their respective property, or ordering the winding up or liquidation of their respective affairs (or any similar relief granted under any foreign laws), and in any such case the continuance of any such decree or order for relief or any such other decree or order unstayed and in effect for a period of 90 consecutive calendar days;

(vii) the commencement by the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities of a voluntary case or proceeding under any applicable federal, state or foreign bankruptcy, insolvency or other similar law or of any other case or proceeding to be adjudicated bankrupt or insolvent, or the consent by the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entity to the entry of a decree or order for relief in respect of the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities in an involuntary case or proceeding under any applicable bankruptcy, insolvency or other similar law or the commencement of any bankruptcy or insolvency case or proceeding against the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entity, or the filing by the Issuer, the

Guarantor or any of the Guarantor's Principal Controlled Entity of a petition or answer or consent seeking reorganization or relief with respect to the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities under any applicable bankruptcy, insolvency or other similar law, or the consent by the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entity to the filing of such petition or to the appointment of or taking possession by a custodian, receiver, liquidator, assignee, trustee, sequestrator, or other similar official of the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities or of any substantial part of their respective property pursuant to any such law, or the making by the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities of a general assignment for the benefit of creditors in respect of any indebtedness as a result of an inability to pay such indebtedness as it becomes due, or the admission by the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities in writing of their inability to pay the debts generally as they become due, or the taking of corporate action by the Issuer, the Guarantor or any of the Guarantor's Principal Controlled Entities that resolves to commence any such action; or

(viii) the Bonds, the Guarantee or the Trust Deed is or becomes or is claimed by the Issuer or the Guarantor to be unenforceable, invalid or ceases to be in full force and effect otherwise than is permitted by the Trust Deed.

## 11 Notices

Notices to the holders of Bonds shall be mailed to them at their respective addresses in the Register and deemed to have been given on the fourth weekday (being a day other than a Saturday, Sunday or public holiday) after the date of mailing. The Issuer shall also ensure that notices are duly published in a manner that complies with the rules and regulations of any stock exchange or other relevant authority on which the Bonds are for the time being listed. Any such notice shall be deemed to have been given on the date of such publication or, if published more than once, on the first date on which publication is made.

*So long as the Bonds are represented by the Global Certificate and the Global Certificate is held on behalf of Euroclear or Clearstream or the Alternative Clearing System (as defined in the form of the Global Certificate), notices to Bondholders shall be given by delivery of the relevant notice to Euroclear or Clearstream or the Alternative Clearing System, for communication by it to entitled accountholders in substitution for notification as required by the Conditions, and such notice shall be deemed to be received by the Bondholders on the date of delivery of such notice to Euroclear or Clearstream or the Alternative Clearing System.*

## 12 Prescription

Claims in respect of amounts due in respect of the Bonds will become prescribed and become void unless made within 10 years (in the case of principal) and five years (in the case of default interest) from the appropriate Relevant Date.

## 13 Replacement of Certificates

If any Certificate is lost, stolen, mutilated, defaced or destroyed, it may be replaced at the specified office of the Registrar or any Transfer Agent, subject to all applicable laws and stock exchange requirements, upon payment by the claimant of the expenses incurred in connection with such replacement and on such terms as to evidence and indemnity and/or security as the Issuer, the Registrar or such Transfer Agent may require. Mutilated or defaced Certificates must be surrendered before replacements will be issued.

## 14 Meetings of Bondholders, Modification and Waiver

### (A) Meetings of Bondholders

The Trust Deed contains provisions for convening meetings of Bondholders (and for passing resolutions by Electronic Consent (as defined in the Trust Deed) or by written resolution) to consider matters affecting their interests, including without limitation the sanctioning by Extraordinary Resolution of a modification of any of these Conditions or any provisions of the Trust Deed. Such a meeting may be convened by the Trustee, the Issuer or the Guarantor and shall be convened by the Trustee upon request in writing from Bondholders holding not less than 10 per cent. in aggregate principal amount of the Bonds for the time being outstanding and subject to the Trustee being indemnified and/or secured and/or pre-funded to its satisfaction against all costs and expenses. The quorum for any meeting convened to consider an Extraordinary Resolution will be two or more persons holding or representing more than 50 per cent. in aggregate principal amount of the Bonds for the time being outstanding or, at any adjourned such meeting, two or more persons being or representing Bondholders whatever the aggregate principal amount of the Bonds held or represented, unless the business of such meeting includes consideration of proposals, *inter alia*, (i) to modify the maturity of the Bonds or the Optional Redemption Date, (ii) to modify the circumstances in which the Issuer or Bondholders are entitled to redeem the Bonds pursuant to Conditions 8(B), 8(C), 8(D) or 8(E), (iii) to reduce or cancel the principal amount or Equivalent Amount payable in respect of the Bonds, (iv) to change the currency of denomination or payment of the Bonds, (v) to modify (except by a unilateral and unconditional reduction in the Conversion Price) or cancel the Conversion Rights, (vi) to modify or cancel the Guarantee (other than as provided in Condition 14(B)) or (vii) to modify the provisions concerning the quorum required at any meeting of the Bondholders or the majority required to pass an Extraordinary Resolution, in which case the necessary quorum will be two or more persons holding or representing not less than 66 per cent., or at any adjourned meeting not less than 33 per cent., in aggregate principal amount of the Bonds for the time being outstanding. Any Extraordinary Resolution duly passed shall be binding on all Bondholders (whether or not they were present at the meeting at which such resolution was passed).

The Trust Deed provides that (a) a written resolution signed by or on behalf of the holders of not less than 90 per cent. of the aggregate principal amount of Bonds for the time being outstanding and who are entitled to receive notice of a meeting of holders under the Trust Deed or (b) passed by Electronic Consent (as defined in the Trust Deed), shall for all purposes be as valid and effective as a duly passed Extraordinary Resolution of the Bondholders. Such a resolution in writing may be contained in one document or several documents in the same form, each signed by or on behalf of one or more Bondholders.

### (B) Modification and Waiver

The Trustee may (but shall not be obliged to) agree, without the consent of the Bondholders, to (i) any modification of any of the provisions of the Trust Deed, any trust deed supplemental to the Trust Deed, the Agency Agreement, any agency agreement supplemental to the Agency Agreement, the Bonds or these Conditions (together the "**Documentation**") which in the Trustee's opinion is of a formal, minor or technical nature, or is made to correct a manifest error, or is made to comply with mandatory provisions of law, and (ii) any other modification to the Documentation (except as mentioned in the Trust Deed), and any waiver or authorization of any breach or proposed breach, of any of the provisions of the Documentation which is, in the opinion of the Trustee, not materially prejudicial to the interests of the Bondholders. The Trustee may, without the consent of the Bondholders, determine any Event of Default or a Potential Event of Default (as defined in the Trust Deed) should not be treated as such, provided that in the opinion of the Trustee, the interests of Bondholders will not be materially prejudiced thereby. Any such modification, authorization or waiver shall be binding on the Bondholders and, unless the Trustee otherwise agrees, any such modification and any authorization or waiver (which shall be in writing) shall be notified by the Issuer to the Bondholders as soon as reasonably practicable in accordance with Condition 11.

**(C) Entitlement of the Trustee**

In connection with the exercise of its functions, rights, powers and/or discretions (including but not limited to those referred to in this Condition 14) the Trustee shall have regard to the interests of, or be responsible for, the interests of the Bondholders as a class and shall not have regard to the consequences of such exercise for individual Bondholders and the Trustee shall not be entitled to require on behalf of any Bondholder, nor shall any Bondholder be entitled to claim from the Issuer, any indemnification or payment in respect of any tax consequences of any such exercise upon individual Bondholders.

*In the event of the passing of an Extraordinary Resolution in accordance with Condition 14(A), a modification, waiver or authorization in accordance with Condition 14(B), the Issuer will procure that the Bondholders be notified in accordance with Condition 11.*

**15 Enforcement**

The Trustee may, at any time, at its discretion and without further notice, take such steps and/or actions and/or institute such proceedings against the Issuer and/or the Guarantor as it may think fit to enforce the terms of the Trust Deed and the Bonds, but it needs not take any such steps, actions and/or proceedings unless (A) it shall have been so directed by an Extraordinary Resolution or shall have been so requested in writing by the holders of not less than 25 per cent. in aggregate principal amount of the Bonds then outstanding and (B) it shall have been indemnified and/or secured and/or prefunded to its satisfaction. No Bondholder may proceed directly against the Issuer and/or the Guarantor unless the Trustee, having become bound so to proceed, fails to do so within a reasonable period and such failure is continuing.

**16 Indemnification of the Trustee**

The Trust Deed contains provisions for the indemnification of the Trustee and for its relief from responsibility, including without limitation provisions relieving it from taking any steps and/or actions and/or instituting proceedings to enforce its rights under the Trust Deed, the Agency Agreement and/or these Conditions and in respect of the Bonds and payment or taking other actions unless indemnified and/or secured and/or prefunded to its satisfaction and be paid or reimbursed for any fees, costs, expenses and indemnity payments and for liabilities incurred by it in priority to the claims of Bondholders. The Trustee is entitled to enter into business transactions with the Issuer, the Guarantor and any entity relating (directly or indirectly) to the Issuer and/or the Guarantor without accounting for any profit.

The Trustee may rely conclusively and without liability to Bondholders, the Issuer, the Guarantor or any other person on any report, confirmation or certificate from or any opinion or advice of any accountants, lawyers, financial advisers, financial institution or any other expert or professional adviser, whether or not addressed to it and whether their liability in relation thereto is limited (by its terms or by any engagement letter relating thereto entered into by the Trustee or any other person or in any other manner) by reference to a monetary cap, methodology or otherwise. The Trustee may accept and shall be entitled to rely conclusively on any such report, confirmation, certificate, opinion or advice, in which case such report, confirmation, certificate, opinion or advice shall be binding on the Issuer, the Guarantor and the Bondholders.

Whenever the Trustee is required or entitled by the terms of the Trust Deed, the Agency Agreement or these Conditions to exercise any discretion or power, take any action, make any decision or give any direction or certification, the Trustee is entitled, prior to exercising any such discretion or power, taking any such action, making any such decision or giving any such direction or certification, to seek directions from the Bondholders by way of Extraordinary Resolution or clarification of any directions, and the Trustee shall not be responsible or liable for any loss or liability incurred by the Issuer, the Guarantor, the Bondholders or any other person as a result of any delay in it exercising such discretion or power, taking such action, making such decision or giving such direction or certification as a result of seeking such direction or clarification of directions from the Bondholders or in the event that no direction or clarification is given to the Trustee by the Bondholders.

None of the Trustee or any of the Agents shall be responsible for the performance by the Issuer, the Guarantor and any other person appointed by the Issuer or the Guarantor, as the case may be, in relation to the Bonds of the duties and obligations on their part expressed in respect of the same and, unless it has written notice from the Issuer or the Guarantor, as the case may be, to the contrary, the Trustee and each Agent shall be entitled to assume that the same are being duly performed. None of the Trustee or any Agent shall be liable to any Bondholder, the Issuer, the Guarantor or any other person for any action taken by the Trustee or such Agent in accordance with the instructions of the Bondholders. The Trustee shall be entitled to rely conclusively on any direction, request or resolution of Bondholders given by Bondholders holding the requisite principal amount of Bonds outstanding or passed at a meeting of Bondholders convened and held in accordance with the Trust Deed (including without limitation passed by Written Resolution or by Electronic Consent).

Neither the Trustee nor any of the Agents shall have any obligation to monitor whether an Event of Default or a Potential Event of Default has occurred or monitor compliance by the Issuer or the Guarantor with the provisions of the Trust Deed, the Agency Agreement or these Conditions, and none of them shall be liable to the Bondholders or any other person for not doing so.

Each Bondholder shall be solely responsible for making and continuing to make its own independent appraisal and investigation into the financial condition, creditworthiness, condition, affairs, status and nature of the Issuer, the Guarantor, the Guarantor's Controlled Entities or the Group (as defined in Condition 6(F)) and neither the Trustee nor any Agent shall at any time have any responsibility for the same and each Bondholder shall not rely on the Trustee or any Agent in respect thereof.

## 17 Further Issues

The Issuer may from time to time without the consent of the Bondholders create and issue further bonds having the same terms and conditions as the Bonds in all respects (or in all respects except for the issue date and the timing for complying with the requirements set out in these Conditions in relation to NDRC Post-Issuance Filing) and so that such further issue shall be consolidated and form a single series with the outstanding Bonds. References in these Conditions to the Bonds include (unless the context requires otherwise) any other bonds issued pursuant to this Condition 17 and consolidated and forming a single series with the Bonds. Any further bonds consolidated and forming a single series with the outstanding Bonds constituted by the Trust Deed or any deed supplemental to it shall be constituted by a deed supplemental to the Trust Deed.

## 18 Contracts (Rights of Third Parties) Act 1999

No person shall have any right to enforce any term or condition of the Bonds under the Contracts (Rights of Third Parties) Act 1999 (the "**Act**"), but this shall not affect any right or remedy which exists or is available apart from the Act and is without prejudice to the rights of the Bondholders as contemplated in Condition 15.

## 19 Governing Law and Submission to Jurisdiction

### (A) Governing Law

The Bonds, the Trust Deed and the Agency Agreement and any non-contractual obligations arising out of or in connection with them are governed by, and shall be construed in accordance with, English law.

**(B) Jurisdiction**

The courts of Hong Kong are to have exclusive jurisdiction to settle any disputes which may arise out of or in connection with the Bonds, the Trust Deed and the Agency Agreement and any non-contractual obligations arising out of or in connection with them and accordingly any legal action or proceedings arising out of or in connection with the Bonds, the Trust Deed and the Agency Agreement ("**Proceedings**") may be brought in such courts. Pursuant to the Trust Deed, each of the Issuer and the Guarantor has irrevocably submitted to the jurisdiction of such courts.

**(C) Agent for Service of Process**

Pursuant to the Trust Deed, each of the Issuer and the Guarantor has irrevocably appointed an agent in Hong Kong to receive service of process in any Proceedings in Hong Kong based on any of the Bonds or the Trust Deed.

**(D) Waiver of Immunity**

Each of the Issuer and the Guarantor hereby waives any right to claim sovereign or other immunity from jurisdiction or execution and any similar defense, and irrevocably consents to the giving of any relief or the issue of any process, including, without limitation, the making, enforcement or execution against any property whatsoever (irrespective of its use or intended use) of any order or judgment made or given in connection with any Proceedings.

## MARKET PRICE INFORMATION

The Class B Shares have been listed on the Main Board of the Hong Kong Stock Exchange since July 9, 2018. The following table sets out the high, low and average closing prices and the average daily trading volume of the Class B Shares for the periods indicated.

| | Closing price | | | |
|---|---|---|---|---|
| | High | Low | End of Period Average | Daily average trading volume |
| | | (HK$) | | (000's) |
| **2019** | | | | |
| First Quarter | 12.50 | 9.70 | 11.10 | 107,415 |
| Second Quarter | 12.36 | 9.02 | 10.57 | 70,248 |
| Third Quarter | 9.99 | 8.35 | 9.09 | 84,630 |
| Fourth Quarter | 10.80 | 8.39 | 9.17 | 115,099 |
| **2020** | | | | |
| First Quarter | 13.90 | 9.50 | 11.94 | 220,100 |
| Second Quarter | 13.88 | 10.00 | 11.63 | 168,778 |
| Third Quarter | 25.70 | 13.60 | 18.35 | 240,715 |

*Source: Bloomberg*

## EXCHANGE RATES

### The PRC

Under current PRC regulations, the Renminbi is convertible for "current account transactions," which include among other things dividend payments and payments for the import of goods and services, subject to compliance with certain procedural requirements. Although the Renminbi has been fully convertible for current account transactions since 1996, we cannot assure you that the relevant PRC government authorities will not limit or eliminate our ability to purchase and retain foreign currencies for current account transactions in the future. Conversion of Renminbi into foreign currencies and of foreign currencies into Renminbi, for payments relating to "capital account transactions," which principally include investments and loans, generally requires the approval of the State Administration of Foreign Exchange, or SAFE, and other relevant PRC governmental authorities.

The value of the Renminbi against the U.S. dollar, HK dollar and other currencies is affected by, among other things, changes in the PRC's political and economic conditions and the PRC's foreign exchange policies. On July 21, 2005, the PRC Government changed its decade-old policy of pegging the value of the Renminbi to the U.S. dollar. However, PBOC regularly intervenes in the foreign exchange market to limit fluctuations in Renminbi exchange rates and achieve policy goals. Following the removal of the U.S. dollar peg, the RMB appreciated more than 20% against the U.S. dollar over the following three years. On June 21, 2010, PBOC further reformed the Renminbi exchange rate to increase its flexibility particularly with respect to the U.S. dollar. It is difficult to predict how long the current situation may last and when and how Renminbi exchange rates may change going forward.

The following table sets forth the exchange rate as set forth in the H.10 statistical release of the Federal Reserve Board for the periods indicated:

| | Exchange rate | | | |
|---|---|---|---|---|
| | Period end | Average(1) | High | Low |
| | (RMB per US$1.00) | | | |
| 2012 | 6.2301 | 6.3093 | 6.3879 | 6.2221 |
| 2013 | 6.0537 | 6.1412 | 6.2438 | 6.0537 |
| 2014 | 6.2046 | 6.1704 | 6.2591 | 6.0402 |
| 2015 | 6.4778 | 6.2869 | 6.4896 | 6.1870 |
| 2016 | 6.9430 | 6.6549 | 6.9580 | 6.4480 |
| 2017 | 6.5063 | 6.7360 | 6.9575 | 6.4773 |
| 2018 | 6.8755 | 6.6292 | 6.9737 | 6.2649 |
| 2019 | 6.9618 | 6.9014 | 7.1786 | 6.6822 |
| 2020 | | | | |
| January | 6.9161 | 6.9184 | 6.9749 | 6.8589 |
| February | 6.9906 | 6.9967 | 7.0286 | 6.9650 |
| March | 7.0808 | 7.0205 | 7.1099 | 6.9244 |
| April | 7.0622 | 7.0708 | 7.0989 | 7.0341 |
| May | 7.1348 | 7.1016 | 7.1681 | 7.0622 |
| June | 7.0651 | 7.0816 | 7.1263 | 7.0575 |
| July | 6.9744 | 7.0041 | 7.0703 | 6.9744 |
| August | 6.8474 | 6.9270 | 6.9799 | 6.8474 |
| September | 6.7896 | 6.8106 | 6.8474 | 6.7529 |
| October | 6.6919 | 6.7254 | 6.7898 | 6.6503 |
| November | 6.5600 | 6.6020 | 6.6899 | 6.5556 |

Note:

(1) Annual averages are calculated using the average of the rates on the last business day of each month during the relevant year. Monthly averages are calculated using the average of the daily rates during the relevant month.

## DESCRIPTION OF THE ORDINARY SHARES

*Set out below is certain selected information concerning the Company's share capital and certain provisions of its memorandum and articles. This summary does not purport to be complete and is qualified in its entirety by reference to the memorandum and the articles.*

The following is a description of the Ordinary Shares, including summaries of material relevant provisions of our Memorandum and the Articles of Association and the Companies Act (2020 Revision) (the "**Cayman Companies Act**"). These summaries do not purport to be complete and are qualified in their entirety by reference to the full Memorandum and the Articles of Association, which are uploaded to both the Company's and the Stock Exchange's website.

### AUTHORIZED AND ISSUED SHARE CAPITAL

The following is a description of the authorized and issued share capital of our Company.

(i) Authorized share capital

| Number | Description of Shares | Approximate aggregate nominal value of shares |
|---|---|---|
| 70,000,000,000 | Class A Share | US$175,000.00 |
| 200,000,000,000 | Class B Share | US$500,000.00 |
| **Total** | | **US$675,000.00** |

(ii) Issued and to be issued, fully paid or credited to be fully paid, as of November 30, 2020

| Number | Description of Shares | Approximate aggregate nominal value of shares |
|---|---|---|
| 4,693,088,341 | Class A Share | US$11,732.72 |
| 19,449,368,963 | Class B Share | US$48,623.42 |
| **Total** | | **US$60,356.14** |

The tables above do not take into account any Shares that may be issued or repurchased by the Company under the general mandates granted to our Directors referred to below.

### WEIGHTED VOTING RIGHTS STRUCTURE

The Company adopts a weighted voting rights structure. Under this structure, the Company's share capital will comprise Class A Shares and Class B Shares. Each Class A Share will entitle the holder to exercise 10 votes, and each Class B Share will entitle the holder to exercise one vote, respectively, on any resolution tabled at the Company's general meetings, except for resolutions with respect to a limited number of Reserved Matters, in relation to which each Share is entitled to one vote.

The Reserved Matters are:

(i) any amendment to the Memorandum or Articles, including the variation of the rights attached to any class of shares;

(ii) the appointment, election or removal of any independent non-executive Director;

(iii) the appointment of removal of the Company's auditors; and

(iv) the voluntary liquidation or winding-up of the Company.

In addition, Shareholders, including holders of Class B Shares, holding not less than one-tenth of the paid up capital of the Company that carries the right of voting at general meetings are entitled to convene an extraordinary general meeting of the Company and add resolutions to the meeting agenda.

1. Classes of Shares

(a) Restrictions on issue of Shares with weighted voting rights

No further Class A Shares shall be issued by the Company, except with the approval of the Hong Kong Stock Exchange and pursuant to (i) an offer to subscribe for shares in the Company made to all the members of the Company pro rata (apart from fractional entitlements) to their existing holdings; (ii) a pro rata issue of shares to all the members of the Company by way of scrip dividends; or (iii) pursuant to a share subdivision or other similar capital reorganization, provided that each member of the Company shall be entitled to subscribe for or be issued shares in the same class as the shares then held by him, and further provided that the proposed allotment or issuance will not result in an increase in the proportion of Class A Shares in issue, so that:

(i) if, under a pro rata offer, any holder of Class A Shares does not take up any part of the Class A Shares or the rights thereto offered to him, such untaken shares or rights shall only be transferred to another person on the basis that such transferred rights will only entitle the transferee to an equivalent number of Class B Shares; and

(ii) to the extent that that rights to Class B Shares in a pro rata offer are not taken up in their entirety, the number of Class A Shares that shall be allotted, issued or granted in such pro rata offer shall be reduced proportionately.

(b) Reduction of Shares with weighted voting rights on repurchase of Shares

In the event the Company reduces the number of Class B Shares in issue through a purchase of its own shares, the holders of Class A Shares shall reduce their voting rights in the Company proportionately, whether through a conversion of a portion of their Class A Shares or otherwise, if the reduction in the number of Class B Shares in issue would otherwise result in an increase in the proportion of Class A Shares to the total number of shares in issue.

(c) Prohibition on variation of terms of shares with weighted voting rights

The Company shall not vary the rights of the Class A Shares so as to increase the number of votes to which each Class A Share is entitled.

(d) Qualification of holders of shares with weighted voting rights

Class A Shares shall only be held by a Director or a vehicle wholly-owned or controlled by a Director. Subject to the Listing Rules or other applicable laws and regulations, each Class A Share shall be automatically converted into one Class B Share upon the occurrence of any of the following events:

(i) the death of the holder of such Class A Share (or where the holder is a vehicle owned or controlled by a Director, the death of that Director);

(ii) the holder of such Class A Share ceasing to be a Director or a vehicle owned or controlled by a Director for any reason;

(iii) the holder of such Class A Share (or, where the holder is a vehicle owned or controlled by a Director, the Director owning or controlling such vehicle) being deemed by the Stock Exchange to be incapacitated for the purpose of performing his duties as a Director;

(iv) the holder of such Class A Share (or, where the holder is a vehicle owned or controlled by a Director, the Director owning or controlling such vehicle) being deemed by the Stock Exchange to no longer meet the requirements of a director set out in the Listing Rules; or

(v) the transfer to another person of the beneficial ownership of, or economic interest in, those shares or the control over the voting rights attached to them (through voting proxies or otherwise), other than (A) the grant of any encumbrance, lien or mortgage over such share which does not result in the transfer of the legal title or beneficial ownership of, or the voting rights attached to, such share, until the same is transferred upon the enforcement of such encumbrance, lien or mortgage; (B) a transfer by a Director to a vehicle wholly owned or wholly controlled by him, or by a vehicle wholly owned or wholly controlled by a Director to such Director or another vehicle wholly owned or wholly controlled by him and (C) any transfer of legal title to such share by a holder of Class A Shares to a limited partnership, trust, private company or other vehicle which holds Class A Shares on behalf of such holder.

(e) Cessation of weighted voting rights

All of the Class A Shares in the authorized share capital shall be automatically re-designated into Class B Shares in the event all of the Class A Shares in issue are converted into Class B Shares, and no further Class A Shares shall be issued by the Company.

2. Variation of rights of existing shares or classes of shares

If at any time the share capital of the Company is divided into different classes of shares, all or any of the rights attached to any class of shares for the time being issued (unless otherwise provided for in the terms of issue of the shares of that class) may, subject to the provisions of the Cayman Companies Act, be varied or abrogated only with (in addition to a special resolution to amend the Memorandum or the Articles) the consent in writing of the holders of not less than three-fourths in nominal value of the issued shares of that class or with the sanction of a resolution passed at a separate meeting of the holders of the shares of that class by members holding shares representing three-fourths in nominal value of the shares present in person or by proxy and voting at such meeting. For so long as any Class A Share is in issue and unless such change is otherwise required by law or the Listing Rules, (a) any change to the composition of the board of Directors; (b) any change in the proportion of votes required to pass a resolution of the members, whether as an ordinary resolution or a special resolution or in respect of particular matters or generally; (c) any variation to the number of votes attached to a share of any class, except any such variation arising from an automatic conversion of a Class A Share into a Class B Share pursuant to the operation of the provisions detailed in paragraph 1(d) above ; and (d) any change to this provision or the matters in respect of which each Class A Ordinary Share and each Class B Ordinary Share shall entitle its holder to one vote on a poll at a general meeting and any change to the quorum requirements for meetings of Directors, shall require the consent in writing of the holders of not less than three-fourths in nominal or par value of the issued Class A Shares. To every such separate meeting all the provisions of the Articles of Association relating to general meetings shall *mutatis mutandis* apply, but so that the quorum for the purposes of any such separate meeting and of any adjournment thereof shall be a person or persons together holding (or representing by proxy or duly authorized representative) at the date of the relevant meeting not less than one-third in nominal value of the issued shares of that class.

The special rights conferred upon the holders of shares of any class shall not, unless otherwise expressly provided in the rights attaching to or the terms of issue of such shares, be deemed to be varied by the creation or issue of further shares ranking *pari passu* therewith.

3. Alteration of capital

The Company may, from time to time, whether or not all the shares for the time being authorized shall have been issued and whether or not all the shares for the time being issued shall have been fully paid up, by ordinary resolution, increase its share capital by the creation of new shares, such new capital to be of such amount and to be divided into shares of such respective amounts as the resolution shall prescribe.

The Company may from time to time by ordinary resolution:

(a) consolidate and divide all or any of its share capital into shares of a larger amount than its existing shares. On any consolidation of fully paid shares and division into shares of larger amount, the Directors may settle any difficulty which may arise as they think expedient and in particular (but without prejudice to the generality of the foregoing) may as between the holders of shares to be consolidated determine which particular shares are to be consolidated into each consolidated share, and if it shall happen that any person shall become entitled to fractions of a consolidated share or shares, such fractions may be sold by some person appointed by the Directors for that purpose and the person so appointed may transfer the shares so sold to the purchaser thereof and the validity of such transfer shall not be questioned, and so that the net proceeds of such sale (after deduction of the expenses of such sale) may either be distributed among the persons who would otherwise be entitled to a fraction or fractions of a consolidated share or shares rateably in accordance with their rights and interests or may be paid to the Company for the Company's benefit;

(b) cancel any shares which at the date of the passing of the resolution have not been taken or agreed to be taken by any person, and diminish the amount of its share capital by the amount of the shares so canceled subject to the provisions of the Cayman Companies Act; and

(c) sub-divide its shares or any of them into shares of smaller amount than is fixed by the Memorandum of Association, subject nevertheless to the provisions of the Cayman Companies Act, and so that the resolution whereby any share is sub-divided may determine that, as between the holders of the shares resulting from such sub-division, one or more of the shares may have any such preferred or other special rights, over, or may have such deferred rights or be subject to any such restrictions as compared with the others as the Company has power to attach to unissued or new shares.

The Company may by special resolution reduce its share capital or any capital redemption reserve in any manner authorized and subject to any conditions prescribed by the Cayman Companies Act.

4. Special resolution – majority required

A "special resolution" is defined in the Articles of Association to have the meaning ascribed thereto in the Cayman Companies Act, for which purpose, the requisite majority shall be not less than three-fourths of the votes of such members of the Company as, being entitled to do so, vote in person or, in the case of corporations, by their duly authorized representatives or, where proxies are allowed, by proxy at a general meeting of which notice specifying the intention to propose the resolution as a special resolution has been duly given and includes a special resolution approved in writing by all of the members of the Company entitled to vote at a general meeting of the Company in one or more instruments each signed by one or more of such members, and the effective date of the special resolution so adopted shall be the date on which the instrument or the last of such instruments (if more than one) is executed.

In contrast, an "ordinary resolution" is defined in the Articles of Association to mean a resolution passed by a simple majority of the votes of such members of the Company as, being entitled to do so, vote in person or, in the case of corporations, by their duly authorized representatives or, where proxies are allowed, by proxy at a general meeting held in accordance with the Articles of Association and includes an ordinary resolution approved in writing by all the members of the Company aforesaid.

5. Annual general meetings

The Company shall hold a general meeting as its annual general meeting each year, within a period of not more than 15 months after the holding of the last preceding annual general meeting (or such longer period as the Stock Exchange may authorize). The annual general meeting shall be specified as such in the notices calling it.

6. Convening of extraordinary general meeting

The Board may, whenever it thinks fit, convene an extraordinary general meeting.

General meetings shall also be convened on the written requisition of any one or more members, which shall include a recognized clearing house (or its nominee(s)), holding, as at the date of deposit of the requisition, in aggregate shares representing not less than one-tenth of the paid up capital of the Company which carry the right of voting at general meetings of the Company, provided that, in the case of a recognized clearing house (or its nominee(s)), it has received instructions to deposit such requisition from account holders holding in aggregate the beneficial interests in shares representing not less than one-tenth of the paid up capital of the Company which carry the right of voting at general meetings of the Company. A written requisition shall be deposited at the principal office of the Company in Hong Kong or, in the event the Company ceases to have such a principal office, the registered office specifying the objects of the meeting and signed by the requisitionist(s).

7. Transfer of shares

Transfers of shares may be effected by an instrument of transfer in the usual common form or in such other form as the Directors may approve which is consistent with the standard form of transfer as prescribed by the Stock Exchange.

The instrument of transfer shall be executed by or on behalf of the transferor and, unless the Directors otherwise determine, the transferee, and the transferor shall be deemed to remain the holder of the share until the name of the transferee is entered in the register of members of the Company in respect thereof. All instruments of transfer shall be retained by the Company.

The Directors may refuse to register any transfer of any share which is not fully paid up or on which the Company has a lien. The Directors may also decline to register any transfer of any shares unless:

(a) the instrument of transfer is lodged with the Company accompanied by the certificate for the shares to which it relates (which shall upon the registration of the transfer be canceled) and such other evidence as the Directors may reasonably require to show the right of the transferor to make the transfer;

(b) the instrument of transfer is in respect of only one class of shares;

(c) the instrument of transfer is properly stamped (in circumstances where stamping is required);

(d) in the case of a transfer to joint holders, the number of joint holders to whom the share is to be transferred does not exceed four;

(e) the shares concerned are free of any lien in favor of the Company; and

(f) a fee of such amount not exceeding the maximum amount as the Stock Exchange may from time to time determine to be payable (or such lesser sum as the Directors may from time to time require) is paid to the Company in respect thereof.

If the Directors refuse to register a transfer of any share they shall, within two months after the date on which the transfer was lodged with the Company, send to each of the transferor and the transferee notice of such refusal.

The registration of transfers may, on 10 business days' notice (or on 6 business days' notice in the case of a rights issue) being given by advertisement published on the Stock Exchange's website, or, subject to the Listing Rules, by electronic communication in the manner in which notices may be served by the Company by electronic means as provided in the Articles of Association or by advertisement published in the newspapers, be suspended and the register of members of the Company closed at such times for such periods as the Directors may from time to time determine, provided that the registration of transfers shall not be suspended or the register closed for more than 30 days in any year (or such longer period as the members of the Company may by ordinary resolution determine provided that such period shall not be extended beyond 60 days in any year).

8. Power of the Company to purchase its own shares

The Company is empowered by the Cayman Companies Act and the Articles of Association to purchase its own shares subject to certain restrictions and the Directors may only exercise this power on behalf of the Company subject to the authority of its members in general meeting as to the manner in which they do so and to any applicable requirements imposed from time to time by the Stock Exchange and the Securities and Futures Commission of Hong Kong. Shares which have been repurchased will be treated as canceled upon the repurchase.

9. Power of any subsidiary of the Company to own shares

There are no provisions in the Articles of Association relating to the ownership of shares by a subsidiary.

10. Dividends and other methods of distribution

Subject to the Cayman Companies Act and the Articles of Association, the Company in general meeting may declare dividends in any currency but no dividends shall exceed the amount recommended by the Directors. No dividend may be declared or paid other than out of profits and reserves of the Company lawfully available for distribution, including share premium.

Unless and to the extent that the rights attached to any shares or the terms of issue thereof otherwise provide, all dividends shall (as regards any shares not fully paid throughout the period in respect of which the dividend is paid) be apportioned and paid pro rata according to the amounts paid up on the shares during any portion or portions of the period in respect of which the dividend is paid. For these purposes no amount paid up on a share in advance of calls shall be treated as paid up on the share.

The Directors may from time to time pay to the members of the Company such interim dividends as appear to the Directors to be justified by the profits of the Company. The Directors may also pay half-yearly or at other intervals to be selected by them any dividend which may be at a fixed rate if they are of the opinion that the profits available for distribution justify the payment.

The Directors may retain any dividends or other monies payable on or in respect of a share upon which the Company has a lien, and may apply the same in or towards satisfaction of the debts, liabilities or engagements in respect of which the lien exists. The Directors may also deduct from any dividend or other monies payable to any member of the Company all sums of money (if any) presently payable by him to the Company on account of calls, installments or otherwise.

No dividend shall carry interest against the Company.

Whenever the Directors or the Company in general meeting have resolved that a dividend be paid or declared on the share capital of the Company, the Directors may further resolve: (a) that such dividend be satisfied wholly or in part in the form of an allotment of shares credited as fully paid up on the basis that the shares so allotted are to be of the same class as the class already held by the allottee, provided that the members of the Company entitled thereto will be entitled to elect to receive such dividend (or part thereof) in cash in lieu of such allotment; or (b) that the members of the Company entitled to such dividend will be entitled to elect to receive an allotment of shares credited as fully paid up in lieu of the whole or such part of the dividend as the Directors may think fit on the basis that the shares so allotted are to be of the same class as the class already held by the allottee. The Company may upon the recommendation of the Directors by ordinary resolution resolve in respect of any one particular dividend of the Company that notwithstanding the foregoing a dividend may be satisfied wholly in the form of an allotment of shares credited as fully paid without offering any right to members of the Company to elect to receive such dividend in cash in lieu of such allotment.

Any dividend, interest or other sum payable in cash to a holder of shares may be paid by check or warrant sent through the post addressed to the registered address of the member of the Company entitled, or in the case of joint holders, to the registered address of the person whose name stands first in the register of members of the Company in respect of the joint holding or to such person and to such address as the holder or joint holders may in writing direct. Every check or warrant so sent shall be made payable to the order of the holder or, in the case of joint holders, to the order of the holder whose name stands first on the register of members of the Company in respect of such shares, and shall be sent at his or their risk and the payment of any such check or warrant by the bank on which it is drawn shall operate as a good discharge to the Company in respect of the dividend and/or bonus represented thereby, notwithstanding that it may subsequently appear that the same has been stolen or that any endorsement thereon has been forged. The Company may cease sending such checks for dividend entitlements or dividend warrants by post if such checks or warrants have been left uncashed on two consecutive occasions. However, the Company may exercise its power to cease sending checks for dividend entitlements or dividend warrants after the first occasion on which such a check or warrant is returned undelivered. Any one of two or more joint holders may give effectual receipts for any dividends or other monies payable or property distributable in respect of the shares held by such joint holders.

Any dividend unclaimed for six years from the date of declaration of such dividend may be forfeited by the Directors and shall revert to the Company.

The Directors may, with the sanction of the members of the Company in general meeting, direct that any dividend be satisfied wholly or in part by the distribution of specific assets of any kind, and in particular of paid up shares, debentures or warrants to subscribe securities of any other company, and where any difficulty arises in regard to such distribution the Directors may settle it as they think expedient, and in particular may disregard fractional entitlements, round the same up or down or provide that the same shall accrue to the benefit of the Company, and may fix the value for distribution of such specific assets and may determine that cash payments shall be made to any members of the Company upon the footing of the value so fixed in order to adjust the rights of all parties, and may vest any such specific assets in trustees as may seem expedient to the Directors.

11. Calls on shares and forfeiture of shares

The Directors may from time to time make calls upon the members of the Company in respect of any monies unpaid on their shares (whether on account of the nominal amount of the shares or by way of premium or otherwise) and not by the conditions of allotment thereof made payable at fixed times and each member of the Company shall (subject to the Company serving upon him at least 14 days' notice specifying the time and place of payment and to whom such payment shall be made) pay to the person at the time and place so specified the amount called on his shares. A call may be revoked or postponed as the Directors may determine. A person upon whom a call is made shall remain liable on such call notwithstanding the subsequent transfer of the shares in respect of which the call was made.

A call may be made payable either in one sum or by installments and shall be deemed to have been made at the time when the resolution of the Directors authorizing the call was passed. The joint holders of a share shall be jointly and severally liable to pay all calls and installments due in respect of such share or other monies due in respect thereof.

If a sum called in respect of a share shall not be paid before or on the day appointed for payment thereof, the person from whom the sum is due shall pay interest on the sum from the day appointed for payment thereof to the time of actual payment at such rate, not exceeding 15% per annum, as the Directors may determine, but the Directors shall be at liberty to waive payment of such interest wholly or in part.

If any call or installment of a call remains unpaid on any share after the day appointed for payment thereof, the Directors may at any time during such time as any part thereof remains unpaid serve a notice on the holder of such shares requiring payment of so much of the call or installment as is unpaid together with any interest which may be accrued and which may still accrue up to the date of actual payment.

The notice shall name a further day (not being less than 14 days from the date of service of the notice) on or before which, and the place where, the payment required by the notice is to be made, and shall state that in the event of non-payment at or before the time and at the place appointed, the shares in respect of which such call was made or installment is unpaid will be liable to be forfeited.

If the requirements of such notice are not complied with, any share in respect of which such notice has been given may at any time thereafter, before payment of all calls or installments and interest due in respect thereof has been made, be forfeited by a resolution of the Directors to that effect. Such forfeiture shall include all dividends and bonuses declared in respect of the forfeited shares and not actually paid before the forfeiture. A forfeited share shall be deemed to be the property of the Company and may be re-allotted, sold or otherwise disposed of.

A person whose shares have been forfeited shall cease to be a member of the Company in respect of the forfeited shares but shall, notwithstanding the forfeiture, remain liable to pay to the Company all monies which at the date of forfeiture were payable by him to the Company in respect of the shares, together with (if the Directors shall in their discretion so require) interest thereon at such rate not exceeding 15% per annum as the Directors may prescribe from the date of forfeiture until payment, and the Directors may enforce payment thereof without being under any obligation to make any allowance for the value of the shares forfeited, at the date of forfeiture.

12. Rights of minorities in relation to fraud or oppression

There are no provisions in the Articles of Association concerning the rights of minority shareholders in relation to fraud or oppression.

13. Procedure on liquidation

If the Company shall be wound up, and the assets available for distribution amongst the members of the Company as such shall be insufficient to repay the whole of the paid-up capital, such assets shall be distributed so that, as nearly as may be, the losses shall be borne by the members of the Company in proportion to the capital paid up, or which ought to have been paid up, at the commencement of the winding up on the shares held by them respectively. If in a winding up the assets available for distribution amongst the members of the Company shall be more than sufficient to repay the whole of the capital paid up at the commencement of the winding up, the excess shall be distributed amongst the members of the Company in proportion to the capital paid up at the commencement of the winding up on the shares held by them respectively. The foregoing is without prejudice to the rights of the holders of shares issued upon special terms and conditions.

If the Company shall be wound up, the liquidator may with the sanction of a special resolution of the Company and any other sanction required by the Cayman Companies Act, divide amongst the members of the Company in specie or kind the whole or any part of the assets of the Company (whether they shall consist of property of the same kind or not) and may, for such purpose, set such value as he deems fair upon any property to be divided as aforesaid and may determine how such division shall be carried out as between the members or different classes of members of the Company. The liquidator may, with the like sanction, vest the whole or any part of such assets in trustees upon such trusts for the benefit of the members of the Company as the liquidator, with the like sanction and subject to the Cayman Companies Act, shall think fit, but so that no member of the Company shall be compelled to accept any assets, shares or other securities in respect of which there is a liability.

14. Untraceable members

The Company shall be entitled to sell any shares of a member of the Company or the shares to which a person is entitled by virtue of transmission on death or bankruptcy or operation of law if: (a) all checks or warrants, not being less than three in number, for any sums payable in cash to the holder of such shares have remained uncashed for a period of 12 years; (b) the Company has not during that time or before the expiry of the three month period referred to in (d) below received any indication of the whereabouts or existence of the member; (c) during the 12 year period, at least three dividends in respect of the shares in question have become payable and no dividend during that period has been claimed by the member; and (d) upon expiry of the 12 year period, the Company has caused an advertisement to be published in the newspapers or subject to the Listing Rules, by electronic communication in the manner in which notices may be served by the Company by electronic means as provided in the Articles of Association, giving notice of its intention to sell such shares and a period of three months has elapsed since such advertisement and the Stock Exchange has been notified of such intention. The net proceeds of any such sale shall belong to the Company and upon receipt by the Company of such net proceeds it shall become indebted to the former member for an amount equal to such net proceeds.

## PROVISIONS RELATING TO THE BONDS IN GLOBAL FORM

The Global Certificate contains provisions which apply to the Bonds in respect of which the Global Certificate is issued, some of which modify the effect of the Conditions set out in this Offering Circular. Terms defined in the Conditions have the same meaning in the paragraphs below. The following is a summary of those provisions:

### Meetings

The registered holder (as defined in the Conditions) (and any proxy or representative appointed by it) of the Global Certificate will be treated as being two persons for the purposes of any quorum requirements of a meeting of Bondholders and, at any such meeting, as having one vote in respect of each U.S.$100,000 in principal amount of Bonds for which the Global Certificate is issued. The Trustee may allow a person with an interest in Bonds in respect of which the Global Certificate has been issued to attend and speak (but not to vote) at a meeting of Bondholders on appropriate proof of his identity and interest.

### Cancelation

Cancelation of any Bond represented by the Global Certificate by the Issuer following redemption, conversion or purchase by the Issuer, the Guarantor or any of the Guarantor's Subsidiaries will be effected by a reduction in the principal amount of the Bonds in the register of Bondholders.

### Trustee's Powers

In considering the interests of Bondholders while the Global Certificate is registered in the name of a nominee for a clearing system, the Trustee may, to the extent it considers it appropriate to do so in the circumstances, but without being obliged to do so, (a) have regard to any information as may have been made available to it by or on behalf of the relevant clearing system or its operator as to the identity of its accountholders (either individually or by way of category) with entitlements in respect of the Bonds and (b) consider such interests on the basis that such accountholders were the holders of the Bonds in respect of which the Global Certificate is issued.

### Conversion

Subject to the requirements of Euroclear and Clearstream (or any Alternative Clearing System), the Conversion Right attaching to the Bonds in respect of which the Global Certificate is issued may be exercised by the presentation to or to the order of the Principal Agent of one or more Conversion Notices duly completed by or on behalf of a holder of a book-entry interest in such Bonds. Deposit of the Global Certificate with the Principal Agent together with the relevant conversion notice(s) shall not be required. The exercise of the Conversion Right shall be notified by the Principal Agent to the Registrar and the holder of the Global Certificate.

### Payment

The Issuer, for value received, will pay to the registered holder of the Bonds in respect of which the Global Certificate is issued such amount or amounts as shall become due in respect of such Bonds at the rates, on the dates for payment, and in accordance with the method of calculation provided for in the Conditions, save that the calculation is made in respect of the total aggregate amount of the Bonds represented by the Global Certificate, together with such other sums and additional amounts (if any) as may be payable under the Conditions, in accordance with the Conditions and otherwise will comply with the Trust Deed and the Conditions.

Payments of principal in respect of Bonds represented by the Global Certificate will be made without presentation or if no further payment falls to be made in respect of the Bonds, against presentation and surrender of the Global Certificate to or to the order of the Principal Agent or such other Paying Agent as shall have been notified to the Bondholders for such purpose.

Such payment will be made to, or to the order of, the person whose name is entered on the Register at the close of business on the Clearing System Business Day immediately prior to the date for payment, where "**Clearing System Business Day**" means Monday to Friday inclusive except December 25 and January 1.

**Notices**

So long as the Bonds are represented by the Global Certificate and the Global Certificate is held on behalf of Euroclear or Clearstream or the Alternative Clearing System (as defined below), notices to Bondholders may be given by delivery of the relevant notice to Euroclear or Clearstream or the Alternative Clearing System, for communication by it to entitled accountholders in substitution for notification as required by the Conditions.

**Bondholder's Redemption**

The Bondholder's redemption options in Condition 8(D) of the Conditions may be exercised by the holder of the Global Certificate giving notice to any Paying Agent of the principal amount of Bonds in respect of which the option is exercised and presenting the Global Certificate for endorsement or exercise (if required) within the time limits specified in the Conditions.

**Redemption at the Option of the Issuer**

The option of the Issuer provided for in Condition 8(B) and Condition 8(C) of the Conditions shall be exercised by the Issuer giving notice to the Bondholders within the time limits set out in and containing the information required by such Conditions and Condition 8(G).

**Bondholder's Tax Option**

The option of Bondholders not to have the Bonds redeemed as provided in Condition 8(B) shall be exercised by the presentation to any Paying Agent, or to the order of such Paying Agent, of a duly completed Tax Option Exercise Notice within the time limits set out in and containing the information required by Condition 8(B).

**Exchange of Bonds Represented by Global Certificates**

Owners of interests in the Bonds in respect of which the Global Certificate is issued will be entitled to have title to the Bonds registered in their names and to receive individual definitive Certificates if either Euroclear or Clearstream (or any other clearing system (an "**Alternative Clearing System**") as shall have been designated by the Issuer and approved in writing by the Trustee, the Principal Agent and the Registrar on behalf of which the Bonds evidenced by the Global Certificate may be held) is closed for business for a continuous period of 14 days (other than by reason of holidays, statutory or otherwise) or announces an intention permanently to cease business or does in fact do so. In such circumstances, the Issuer at its own expense will cause sufficient individual definitive Certificates to be executed and delivered to the Registrar for completion, authentication and dispatch to the relevant holders of the Bonds. A person with an interest in the Bonds in respect of which the Global Certificate is issued must provide the Registrar with a written order containing instructions and such other information as the Issuer and the Registrar may require to complete, execute and deliver such individual definitive Certificates.

**Transfers**

Transfers of interests in the Bonds will be effected through the records of Euroclear and Clearstream (or any Alternative Clearing System) and their respective participants in accordance with the rules and procedures of Euroclear and Clearstream (or any Alternative Clearing System) and their respective direct and indirect participants.

# TAXATION

*The following summary of certain Cayman Islands, Hong Kong and PRC tax consequences of the purchase, ownership and disposition of Bonds and Class B Shares is based upon applicable laws, regulations, rulings and decisions as of the date of this Offering Circular, all of which are subject to change (possibly with retroactive effect). This discussion does not purport to be a comprehensive description of all the tax considerations that may be relevant to a decision to purchase, own or dispose of the Bonds or the Class B Shares and does not purport to deal with consequences applicable to all categories of investors, some of which may be subject to special rules. Persons considering the purchase of Bonds should consult their own tax advisors concerning the tax consequences of the purchase, ownership and disposition of Bonds and Class B Shares, including such possible consequences under the laws of their country of citizenship, residence or domicile.*

## Cayman Islands

Under existing laws of the Cayman Islands, payments of interest and principal on the Bonds will not be subject to taxation in the Cayman Islands and no withholding will be required on the payment of interest and principal to any holder of the Bonds, as the case may be, nor will gains derived from the disposal of the Bonds be subject to Cayman Islands income or corporation tax. The Cayman Islands currently has no income, corporation or capital gains tax and no estate duty, inheritance tax or gift tax.

No stamp duty is payable in respect of the issue of the Bonds. The holder of any Bonds (or a legal personal representative of such holder) whose Bonds are brought into the Cayman Islands may in certain circumstances be liable to pay stamp duty imposed under the laws of the Cayman Islands in respect of such Bonds. An instrument transferring title to a registered Bond, if brought to or executed in the Cayman Islands, would be subject to nominal Cayman Islands stamp duty. Stamp duty may be payable if any original documents are brought to or executed in the Cayman Islands.

## Hong Kong

### Withholding tax

No withholding tax is payable in Hong Kong in respect of payments of principal or interest on the Bonds or in respect of any capital gains arising from the sale of the Bonds.

### Profits tax

Hong Kong profits tax is chargeable on every person carrying on a trade, profession or business in Hong Kong in respect of profits arising in or derived from Hong Kong from such trade, profession or business (excluding profits arising from the sale of capital assets).

Interest on the Bonds may be deemed to be profits arising in or derived from Hong Kong from a trade, profession or business carried on in Hong Kong in the following circumstances:

(i) interest on the Bonds is derived from Hong Kong and is received by or accrues to a corporation carrying on a trade, profession or business in Hong Kong;

(ii) interest on the Bonds is derived from Hong Kong and is received by or accrues to a person, other than a corporation, carrying on a trade, profession or business in Hong Kong and is in respect of the funds of that trade, profession or business;

(iii) interest on the Bonds is received by or accrues to a financial institution (as defined in the Inland Revenue Ordinance (Cap. 112) of Hong Kong (the "**IRO**")) and arises through or from the carrying on by the financial institution of its business in Hong Kong; or

(iv) interest on the Bonds is received by or accrues to a corporation, other than a financial institution, and arises through or from the carrying on in Hong Kong by the corporation of its intra-group financing business (within the meaning of section 16(3) of the IRO).

Sums received by or accrued to a financial institution by way of gains or profits arising through or from the carrying on by the financial institution of its business in Hong Kong from the sale, disposal and redemption of Bonds will be subject to Hong Kong profits tax. Sums received by or accrued to a corporation, other than a financial institution, by way of gains or profits arising through or from the carrying on in Hong Kong by the corporation of its intra-group financing business (within the meaning of section 16(3) of the IRO) from the sale, disposal or other redemption of Bonds will be subject to Hong Kong profits tax.

Sums derived from the sale, disposal or redemption of Bonds will be subject to Hong Kong profits tax where received by or accrued to a person, other than a financial institution, who carries on a trade, profession or business in Hong Kong and the sum has a Hong Kong source unless otherwise exempted. The source of such sums will generally be determined by having regard to the manner in which the Bonds are acquired and disposed of.

In certain circumstances, Hong Kong profits tax exemptions (such as concessionary tax rates) may be available. Investors are advised to consult their own tax advisors to ascertain the applicability of any exemptions to their individual position.

**Stamp Duty**

No Hong Kong stamp duty will be chargeable upon the issuance or transfer of a Bond.

**PRC Taxation**

The following summary of certain PRC tax consequences of the purchase, ownership and disposition of Bonds is based upon applicable laws, rules and regulations in effect as of the date of this Offering Circular, all of which are subject to change (possibly with retroactive effect). This discussion does not purport to be a comprehensive description of all the tax considerations that may be relevant to a decision to purchase, own or dispose of the Bonds and does not purport to deal with consequences applicable to all categories of investors, some of which may be subject to special rules. Persons considering the purchase of Bonds should consult their own tax advisors concerning the tax consequences of the purchase, ownership and disposition of Bonds, including such possible consequences under the laws of their country of citizenship, residence or domicile.

**Taxation on Interests**

The EIT Law imposes a tax at the rate of 10 per cent. on interests realized by an enterprise holder of the Bonds that is a "non-resident enterprise" which does not have an establishment or place of business in the PRC or, whose relevant income is not effectively connected with its establishment or place of business in the PRC despite the existence of such establishment or place of business in the PRC, to the extent such interests are sourced within the PRC. The Individual Income Tax Law imposes a tax at the rate of 20 per cent. on interest paid to a foreign individual who is neither domiciled nor resides in the PRC; to the extent such income is sourced within the PRC. Pursuant to these provisions of the EIT Law and the Individual Income Tax Law, it is unclear whether we are considered as a PRC resident enterprise. If we are considered as a PRC resident enterprise, interests paid to non-resident enterprise holders and non-resident individual holders of the Bonds may be treated as income derived from sources within the PRC and thus subject to PRC withholding tax. To the extent that China has entered into arrangements relating to the avoidance of double-taxation with any jurisdiction, such as Hong Kong, that allow a lower withholding tax rate, such lower rate may apply to qualified enterprise investors in the Bonds.

**Taxation on Capital Gains**

The EIT Law impose a tax at the rate of 10 per cent. on capital gains realized by an enterprise holder of Bonds that is a "non-resident enterprise" which does not have an establishment or place of business in the PRC or, where despite the existence of establishment or place of business in the PRC, the relevant gain is not effectively connected with such establishment or place of business in the PRC, to the extent such capital gains are sourced within the PRC. The Individual Income Tax Law imposes a tax at the rate of 20 per cent.

on capital gains realized by a foreign individual who is neither domiciled nor resident in the PRC; to the extent such capital gains are sourced within the PRC. Pursuant to these provisions of the EIT Law and the Individual Income Tax Law, although the matter is unclear, if we are considered a PRC resident enterprise, capital gains realized by non-resident enterprise holders and non-resident individual holders of the Bonds may be treated as income derived from sources within the PRC and be subject to PRC withholding tax. To the extent that China has entered into arrangements relating to the avoidance of double-taxation with any jurisdiction, such as Hong Kong, that allow a lower rate of withholding tax, such lower rate may apply to qualified enterprise investors in the Bonds.

**Stamp duty**

No PRC stamp tax will be chargeable upon the issue or transfer (for so long as the register of holders of the Bonds is maintained outside the PRC) of a Bond.

## SUBSCRIPTION AND SALE

The Issuer and the Guarantor have entered into a subscription agreement with the Managers dated December 1, 2020 (the "**Subscription Agreement**") pursuant to which, and subject to certain conditions contained therein, the Issuer agreed to sell to the Managers, and each of the Managers has agreed severally and not jointly to subscribe and pay for, or to procure subscribers to subscribe and pay for, the aggregate principal amount of the Bonds set forth opposite its name below.

| | **Principal amount of the Bonds to be subscribed** |
|---|---|
| | **(U.S.$)** |
| Credit Suisse (Hong Kong) Limited | 303,525,000 |
| Goldman Sachs (Asia) L.L.C. | 303,525,000 |
| J.P. Morgan Securities plc | 123,975,000 |
| Morgan Stanley & Co. International plc | 123,975,000 |
| **Total** | **855,000,000** |

The Subscription Agreement provides that the Issuer and the Guarantor will jointly and severally indemnify the Managers against certain liabilities in connection with the offer and sale of the Bonds. The Subscription Agreement provides that the obligations of the Managers are subject to certain conditions precedent, and entitles the Managers to terminate it in certain circumstances prior to payment being made to the Issuer.

The Managers or their respective affiliates may purchase the Bonds or Class B Shares for their own account and enter into transactions, including, without limitation, credit derivatives, including asset swaps, repackaging and credit default swap relating to the Bonds or Class B Shares at the same time as the offer and sale of the Bonds or in secondary market transactions. Such transactions would be carried out as bilateral trades with selected counterparties and separately from any existing sale or resale of the Bonds or Class B Shares to which this Offering Circular relates (notwithstanding that such selected counterparties may also be purchaser of the Bonds). The Managers and their respective affiliates have engaged in, and may in the future engage in, investment banking and other commercial dealings in the ordinary course of business with the Issuer, the Guarantor or their respective subsidiaries or affiliates from time to time. The Managers may receive customary fees and commissions for these transactions. The Managers or certain of their respective affiliates may purchase Bonds or Class B Shares and be allocated Bonds or Class B Shares for asset management and/or proprietary purposes but not with a view to distribution. In addition to the transactions noted above, the Managers and their respective affiliates may, from time to time, engage in other transactions with, and perform services for, the Issuer, the Guarantor or their respective subsidiaries or affiliates in the ordinary course of their business. In addition, the Managers and certain of their respective subsidiaries and affiliates may hold shares or other securities in the Issuer or the Guarantor as beneficial owners, on behalf of clients or in the capacity of investment advisers.

Each of the Issuer and the Guarantor has agreed in the Subscription Agreement that neither the Issuer, the Guarantor nor any person acting on its or their behalf will (a) issue, offer, sell, pledge, contract to sell or otherwise dispose of or grant options, issue warrants or offer rights entitling persons to subscribe or purchase any interest in any Ordinary Shares or securities of the same class as the Bonds or the Ordinary Shares or any securities convertible into, exchangeable for or which carry rights to subscribe or purchase the Bonds, the Ordinary Shares or securities of the same class as the Bonds, the Ordinary Shares or other instruments representing interests in the Bonds, the Ordinary Shares or other securities of the same class as them, (b) enter into any swap or other agreement that transfers, in whole or in part, any of the economic consequences of the ownership of the Ordinary Shares, (c) enter into any transaction with the same economic effect as, or which is designed to, or which may reasonably be expected to result in, or agree to do, any of the foregoing, whether any such transaction of the kind described in (a), (b) or (c) is to be settled by delivery of Ordinary Shares or other securities, in cash or otherwise or (d) announce or otherwise make public an intention to do any of the foregoing, in any such case without the prior written consent of the Managers between the date hereof and the date which is 90 days after the Issue Date (both dates inclusive) except for (i) the Bonds and the new Class B Shares issued on conversion of the Bonds, (ii) any Ordinary Shares or options granted pursuant to the Guarantor's publicly disclosed share option schemes and share award scheme, and (iii) the issue of any Ordinary Shares which are issued as consideration for any merger or acquisition.

In addition, Smart Mobile Holdings Limited has executed a lock-up undertaking in respect of the 4,226,640,526 Class A Shares and 2,443,898,616 Class B Shares held directly (or through nominees) or indirectly through companies controlled by it or their subsidiaries (or through their nominees) (collectively, the "**Lock-up Shares**"), representing 90.06 per cent. and 12.57 per cent. respectively of the relevant class of Ordinary Shares of the Guarantor, on the date of the Subscription Agreement, whereby it undertakes that for a period from the date of the Subscription Agreement up to 90 days after the Issue Date, it will not, without the prior written consent of the Managers, (a) issue, offer, sell, contract to sell, pledge or otherwise dispose of or grant options, issue warrants or offer rights entitling persons to subscribe or purchase any interest in any Ordinary Shares or securities of the same class as the Ordinary Shares or any securities convertible into, exchangeable for or which carry rights to subscribe or purchase the Ordinary Shares or securities of the same class as the Ordinary Shares or other instruments representing interests in the Ordinary Shares or other securities of the same class as them, (b) enter into any swap or other agreement that transfers, in whole or in part, any of the economic consequences of the ownership of the Ordinary Shares, (c) enter into any transaction with the same economic effect as, or which is designed to, or which may reasonably be expected to result in, or agree to do, any of the foregoing, whether any such transaction of the kind described in (a), (b) or (c) is to be settled by delivery of Ordinary Shares or other securities, in cash or otherwise or (d) announce or otherwise make public an intention to do any of the foregoing. The foregoing sentence shall not apply to transfers of any Ordinary Shares or any security convertible into the Ordinary Shares pursuant to any donation for genuine charitable purposes.

## Selling Restrictions

### General

The distribution of this Offering Circular or any offering material and the offering, sale or delivery of the Bonds is restricted by law in certain jurisdictions. Therefore, persons who may come into possession of this Offering Circular or any offering material are advised to consult their own legal advisers as to what restrictions may be applicable to them and to observe such restrictions. This Offering Circular may not be used for the purpose of an offer or invitation in any circumstances in which such offer or invitation is not authorized.

No action has been or will be taken in any jurisdiction by the Issuer, the Guarantor or the Managers that would permit a public offering, or any other offering under circumstances not permitted by applicable law, of the Bonds, or possession or distribution of this Offering Circular, any amendment or supplement thereto issued in connection with the proposed resale of the Bonds or any other offering or publicity material relating to the Bonds, in any country or jurisdiction where action for that purpose is required. Accordingly, the Bonds may not be offered or sold, directly or indirectly, and neither this Offering Circular nor any other offering material or advertisements in connection with the Bonds may be distributed or published, by the Issuer, the Guarantor or the Managers, in or from any country or jurisdiction, except in circumstances which will result in compliance with all applicable rules and regulations of any such country or jurisdiction and will not impose any obligations on the Issuer, the Guarantor or the Managers.

If a jurisdiction requires that the offering be made by a licensed broker or dealer and the Managers or any affiliate of the Managers is a licensed broker or dealer in that jurisdiction, the offering shall be deemed to be made by the Managers or such affiliate on behalf of the Issuer and the Guarantor in such jurisdiction.

### United States

The Bonds and the Class B Shares to be issued upon conversion of the Bonds have not been and will not be registered under the Securities Act and, subject to certain exceptions, may not be offered or sold within the United States.

The Bonds are being offered and sold outside of the United States in reliance on Regulation S.

In addition, until 40 days after the commencement of the offering of the Bonds, an offer or sale of the Bonds or Class B Shares to be issued upon conversion of the Bonds within the United States by any dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act.

**Hong Kong**

Each Manager has represented and agreed that:

**(i)** it has not offered or sold and will not offer or sell in Hong Kong, by means of any document, any Bonds other than (a) to "professional investors" as defined in the Securities and Futures Ordinance (Cap. 571) of Hong Kong (the "**SFO**") and any rules made under the SFO; or (b) in other circumstances which do not result in the document being a "prospectus" as defined in the Companies (Winding Up and Miscellaneous Provisions Ordinance (Cap. 32) of Hong Kong (the "**C(WUMP)O**") or which do not constitute an offer to the public within the meaning of the C(WUMP)O; and

**(ii)** it has not issued or had in its possession for the purposes of issue, and will not issue or have in its possession for the purposes of issue, whether in Hong Kong or elsewhere, any advertisement, invitation or document relating to the Bonds, which is directed at, or the contents of which are likely to be accessed or read by, the public of Hong Kong (except if permitted to do so under the securities laws of Hong Kong) other than with respect to Bonds which are or are intended to be disposed of only to persons outside Hong Kong or only to "professional investors" as defined in the SFO and any rules made under the SFO.

**United Kingdom**

Each Manager has represented and agreed that:

(a) it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of the Financial Services and Markets Act 2000 (the "**FSMA**")) received by it in connection with the issue or sale of any Bonds in circumstances in which Section 21(1) of the FSMA does not apply to the Issuer or the Guarantor; and

(b) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the Bonds in, from or otherwise involving the United Kingdom.

**Prohibition of Sales to EEA and UK Retail Investors**

Each Manager has represented and agreed that it has not offered, sold or otherwise made available and will not offer, sell or otherwise make available any Bond which are the subject of the offering contemplated by this Offering Circular in relation thereto to any retail investor in the European Economic Area or in the United Kingdom. For the purposes of this provision:

(a) the expression "retail investor" means a person who is one (or more) of the following:

    i. a retail client as defined in point (11) of Article 4(1) of MiFID II; or

    ii. a customer within the meaning of Directive (EU) 2016/97 (the "Insurance Distribution Directive"), where that customer would not qualify as a professional client as defined in point (10) of Article 4(1) of MiFID II; and

(b) the expression "offer" includes the communication in any form and by any means of sufficient information on the terms of the offer and the Bonds to be offered so as to enable an investor to decide to purchase or subscribe for the Bonds.

**Japan**

The Bonds have not been and will not be registered under the Financial Instruments and Exchange Act of Japan (Act No. 25 of 1948, as amended, the "**Financial Instruments and Exchange Act**"). Accordingly, each Manager has represented and agreed that is has not, directly or indirectly, offered or sold and will not, directly or indirectly, offer or sell any Bonds in Japan or to, or for the benefit of, any resident of Japan (which term as used herein means any person resident in Japan, including any corporation or other entity organized under the laws of Japan) or to others for re-offering or re-sale, directly or indirectly, in Japan or to, or for the benefit of, any resident of Japan except pursuant to an exemption from the registration requirements of, and otherwise in compliance with, the Financial Instruments and Exchange Act and other relevant laws and regulations of Japan.

**The People's Republic of China**

Each Manager has represented and agreed that the Bonds are not being offered or sold and may not be offered or sold, directly or indirectly, in the People's Republic of China (for such purposes, not including the Hong Kong and Macau Special Administrative Regions or Taiwan), except as permitted by applicable laws of the People's Republic of China.

**Singapore**

Each Manager has acknowledged that this Offering Circular has not been registered as a prospectus with the Monetary Authority of Singapore. Accordingly, each Manager has represented and agreed that it has not offered or sold any Bonds or caused the Bonds to be made the subject of an invitation for subscription or purchase and will not offer or sell any Bonds or cause the Bonds to be made the subject of an invitation for subscription or purchase, and has not circulated or distributed, nor will it circulate or distribute, this Offering Circular or any other document or material in connection with the offer or sale, or invitation for subscription or purchase, of the Bonds, whether directly or indirectly, to persons in Singapore other than (i) to an institutional investor (as defined in Section 4A of the Securities and Futures Act (Chapter 289) of Singapore (as modified or amended from time to time, the "**SFA**")) pursuant to Section 274 of the SFA, (ii) to a relevant person (as defined in Section 275(2) of the SFA) pursuant to Section 275(1) of the SFA, or any person pursuant to Section 275(1A) of the SFA, and in accordance with the conditions specified in Section 275 of the SFA, or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA.

Where the Bonds are subscribed or purchased under Section 275 of the SFA by a relevant person which is:

(a) a corporation (which is not an accredited investor (as defined in Section 4A of the SFA)) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or

(b) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary of the trust is an individual who is an accredited investor,

securities or securities-based derivatives contracts (each term as defined in Section 2(1) of the SFA) of that corporation or the beneficiaries' rights and interest (howsoever described) in that trust shall not be transferred within six months after that corporation or that trust has acquired the Bonds pursuant to an offer made under Section 275 of the SFA except:

(i) to an institutional investor or to a relevant person, or to any person arising from an offer referred to in Section 275 (1A) or Section 276(4)(i)(B) of the SFA;

(ii) where no consideration is or will be given for the transfer;

(iii) where the transfer is by operation of law;

(iv) as specified in Section 276(7) of the SFA; or

(v) as specified in Regulation 37A of the Securities and Future (Offers of Investments) (Securities and Securities-based Derivatives Contracts) Regulations 2018.

Singapore SFA Product Classification: In connection with Section 309B of the Securities and Futures Act (Chapter 289) of Singapore (the "**SFA**") and the Securities and Futures (Capital Markets Products) Regulations 2018 of Singapore (the "**CMP Regulations 2018**"), the Issuer has determined, and hereby notifies all relevant persons (as defined in Section 309A(1) of the SFA), that the Bonds are 'prescribed capital markets products' (as defined in the CMP Regulations 2018) and Excluded Investment Products (as defined in MAS Notice SFA 04-N12: Notice on the Sale of Investment Products and MAS Notice FAA-N16: Notice on Recommendations on Investment Products).

**The Cayman Islands**

Each Manager has represented, warranted and agreed that no offer of the Bonds will be made directly or indirectly to the public in the Cayman Islands.

## INDEPENDENT AUDITORS

Our audited consolidated financial statements as at and for the years ended December 31, 2017, 2018 and 2019 included in this Offering Circular have been extracted from the Guarantor's Audited Financial Statements and our unaudited but reviewed financial results as at and for the nine months ended September 30, 2019 and 2020 included in this Offering Circular have been extracted from the Guarantor's Interim Financial Results.

The Audited Financial Statements have been audited by PwC in accordance with International Standards on Auditing ("**ISAs**") and the Interim Financial Results have been reviewed by PwC in accordance with International Standard on Review Engagements 2410.

None of the Managers, the Trustee or the Agents or any of their respective holding companies, subsidiaries, affiliates, directors, officers, employees, representatives, agents or advisers or any person who controls any of them make any representation or warranty, express or implied, regarding the sufficiency of any unaudited figures in this offering circular. Potential investors must exercise caution when using such unaudited figures to evaluate the financial condition and results of operations of the Guarantor and its subsidiaries.

## GENERAL INFORMATION

1. **Clearing Systems**: The Bonds have been accepted for clearance through Euroclear and Clearstream under Common Code number 226911286 and the International Securities Identification Number for the Bonds is XS2269112863.

2. **Listing of Bonds**: Application will be made to the Hong Kong Stock Exchange for the listing of, and permission to deal in, the Bonds issued to Professional Investors only. It is expected that dealing in, and listing of, the Bonds on the Hong Kong Stock Exchange will commence on December 18, 2020.

3. **Listing of Class B Shares**: Application will be made to the Hong Kong Stock Exchange for the listing of, and permission to deal in, the Class B Shares arising on conversion of the Bonds. It is expected that dealing in, and listing of, such Class B Shares on the Hong Kong Stock Exchange will commence when they are issued.

4. **Authorizations**: The Issuer and the Guarantor have obtained all necessary consents, approvals and authorizations in connection with the issue and performance of the Bonds and the Guarantee. The issue of the Bonds was authorized by the board of directors of the Issuer on December 1, 2020 and the guarantee of the Bonds and the right of conversion into Class B Shares was authorized by the board of directors of the Guarantor on December 1, 2020. The Class B Shares to be issued upon conversion of the Bonds are to be issued pursuant to the general mandate granted to the Directors of the Guarantor at its annual general meeting held on June 23, 2020.

5. **No Material Adverse Change**: There has not occurred any material change (nor any development or event involving a prospective change), in our condition (financial or otherwise), prospects, results of operations, profitability, business, management, shareholders' equity, properties or general affairs since September 30, 2020, and there has not occurred any such material change in the Issuer since its incorporation.

6. **Litigation**: None of the Issuer, the Guarantor nor any of their respective subsidiaries is involved in any litigation or arbitration proceedings which are material in the context of the Bonds nor is the Issuer or the Guarantor aware that any such proceedings are pending or threatened, save as disclosed in this Offering Circular.

7. **Available Documents**: So long as any of the Bonds is outstanding, (i) copies of our latest annual report, our audited consolidated financial statements as at and for the year ended December 31, 2018 and 2019, as well as the Trust Deed and the Agency Agreement, will be available for inspection by Bondholders at the principal office of the Guarantor at Level 54, Hopewell Centre, 183 Queen's Road East, Hong Kong and (ii) copies of the Trust Deed and the Agency Agreement will be available for inspection by Bondholders at the principal place of business of the Trustee (being at the date of this Offering Circular at 20/F, Citi Tower, One Bay East, 83 Hoi Bun Road, Kwun Tong, Kowloon, Hong Kong) during normal office hours (being between 9:00 a.m. and 4:00 p.m.) on any weekday (except public holidays) following prior written request and proof of holding and identity to the satisfaction of the Trustee.

8. **Consolidated Financial Statements**: The Guarantor's Audited Financial Statements, which are included elsewhere in this Offering Circular, have been audited by PwC, the independent auditors of the Guarantor. The Guarantor's Interim Financial Results, which are included elsewhere in this Offering Circular, have been reviewed by PwC, the independent auditors of the Guarantor.

9. **Auditor's Consent**: The independent auditors of the Guarantor have agreed to the reproduction in this Offering Circular of, and all references to, (i) their name, (ii) their audit reports on the consolidated financial statements of the Guarantor for the year ended December 31, 2018 and 2019 and (iii) their reviewed report on the consolidated financial information of the Guarantor for the nine months ended September 30, 2020.

## INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

**Audited Consolidated Financial Statements as of and for the year ended December 31, 2018**



**Audited Consolidated Financial Statements as of and for the year ended December 31, 2019**



**Unaudited but reviewed consolidated financial results as of and for the nine months ended September 30, 2020**

# INDEPENDENT AUDITOR'S REPORT

pwc 羅兵咸永道

To the Shareholders of Xiaomi Corporation
(incorporated in the Cayman Islands with limited liability)

## Opinion

### What we have audited

The consolidated financial statements of Xiaomi Corporation (the "Company") and its subsidiaries (the "Group") set out on pages 169 to 309, which comprise:

- the consolidated balance sheet as of December 31, 2018;
- the consolidated income statement for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

### Our opinion

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as of December 31, 2018, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRSs") and have been properly prepared in compliance with the disclosure requirements of the Hong Kong Companies Ordinance.

## Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing ("ISAs"). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

# INDEPENDENT AUDITOR'S REPORT

### Independence

We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants ("IESBA Code"), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code.

## Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter identified in our audit is related to the classification and fair value determination for unlisted securities classified as "long-term investments measured at fair value through profit or loss".

| Key Audit Matter | How our audit addressed the Key Audit Matter |
|---|---|
| **The classification and fair value determination for unlisted securities classified as "long-term investments measured at fair value through profit or loss"**<br><br>Refer to Note 3.3 and Note 19 to the consolidated financial statements.<br><br>During the year ended December 31, 2018, the Group recognized fair value changes on the following investments in profits or losses: (i) equity investments in unlisted companies other than those accounted for using equity method, and (ii) convertible redeemable preferred shares or ordinary shares with preferential rights investments in unlisted companies (collectively the "Unlisted Securities"), amounting to RMB2,414,031,000 and RMB11,006,279,000, respectively. The total amount of Unlisted Securities as of December 31, 2018 was RMB13,420,310,000, accounting for 9% of the Group's total assets. | We understood and evaluated the key controls over the capturing, measurement and recording of the Unlisted Securities investments.<br><br>For the classification and initial recognition of the Unlisted Securities, we have performed the following procedures:<br><br>(1) We checked relevant legal documents such as shareholder agreements, share purchase agreements and articles of association of the investees on a sample basis to understand and evaluate the commercial reasonableness of these Unlisted Securities investments;<br><br>(2) We evaluated management's analysis on contract terms and assessed the reasonableness of management's accounting treatments on a sample basis. |

# INDEPENDENT AUDITOR'S REPORT

| Key Audit Matter | How our audit addressed the Key Audit Matter |
|---|---|
| The classification and initial recognition of the Unlisted Securities require management to analyze certain complex contract terms and make judgments to determine the classifications of the above financial assets, based on the Group's business models of managing these financial assets and the contractual terms of the cash flows. The Group identified its various rights and evaluated the financial impacts based on key terms from relevant legal documents.<br><br>Management engaged an external valuer to assist to determine the year-end fair value of these Unlisted Securities. The fair value determination of such Unlisted Securities required management to make judgments and estimates, including the appropriateness of using various unobservable inputs.<br><br>We focused on this area due to the significance of the balances of these investments and their related fair value gain or loss for the year, as well as management judgments, assumptions and estimations involved in the initial recognition and fair value determination of the Unlisted Securities. | For the assessment of fair value determination of the Unlisted Securities, we involved our internal valuation specialists to perform the following procedures:<br><br>(1) We assessed the objectivity, independence and competence of the external valuer engaged by the Group;<br><br>(2) We interviewed management and understood the underlying assumptions and inputs used in fair value determination of Unlisted Securities;<br><br>(3) We assessed the reasonableness of assumptions and inputs used in fair value determination of Unlisted Securities, including expected volatility, risk-free interest rate, discounted for lack of marketability;<br><br>(4) We recalculated the fair values of Unlisted Securities on a sample basis; and<br><br>(5) We tested the accuracy of the fair value changes on investments measured at fair value through profit or loss for the year on a sample basis.<br><br>We found the judgments, assumptions and estimations made by management in relation to the initial recognition and fair value determination of the Unlisted Securities to be supportable based on the available evidences. |

# INDEPENDENT AUDITOR'S REPORT

## Other Information

The directors of the Company are responsible for the other information. The other information comprises all of the information included in the annual report other than the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

## Responsibilities of Directors and the Audit Committee for the Consolidated Financial Statements

The directors of the Company are responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with IFRSs and the disclosure requirements of the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

The audit committee are responsible for overseeing the Group's financial reporting process.

## Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. We report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. Reasonable assurance is a high level

# INDEPENDENT AUDITOR'S REPORT

of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.

- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

# INDEPENDENT AUDITOR'S REPORT

We communicate with the audit committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the audit committee with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the audit committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Leung Wai Kin.

**PricewaterhouseCoopers**
Certified Public Accountants

Hong Kong, March 19, 2019

# CONSOLIDATED INCOME STATEMENT

For the year ended December 31, 2018

(Expressed in Renminbi ("RMB"))

| | Note | Year ended December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|---|
| **Revenue** | 6 | 174,915,425 | 114,624,742 |
| Cost of sales | 9 | (152,723,486) | (99,470,537) |
| **Gross profit** | | 22,191,939 | 15,154,205 |
| Selling and marketing expenses | 9 | (7,993,072) | (5,231,540) |
| Administrative expenses | 9 | (12,099,078) | (1,216,110) |
| Research and development expenses | 9 | (5,776,826) | (3,151,401) |
| Fair value changes on investments measured at fair value through profit or loss | 19(iv) | 4,430,359 | 6,371,098 |
| Share of losses of investments accounted for using the equity method | 12(b) | (614,920) | (231,496) |
| Other income | 7 | 844,789 | 448,671 |
| Other gains, net | 8 | 213,281 | 72,040 |
| **Operating profit** | | 1,196,472 | 12,215,467 |
| Finance income, net | 11 | 216,373 | 26,784 |
| Fair value changes of convertible redeemable preferred shares | 35 | 12,514,279 | (54,071,603) |
| **Profit/(loss) before income tax** | | 13,927,124 | (41,829,352) |
| Income tax expenses | 13 | (449,377) | (2,059,763) |
| **Profit/(loss) for the year** | | 13,477,747 | (43,889,115) |
| **Attributable to:** | | | |
| — Owners of the Company | | 13,553,886 | (43,826,016) |
| — Non-controlling interests | | (76,139) | (63,099) |
| | | 13,477,747 | (43,889,115) |
| **Earnings/(loss) per share (expressed in RMB per share):** | 14 | | |
| Basic | | 0.843 | (4.491) |
| Diluted | | 0.044 | (4.491) |

*The notes on pages 177 to 309 are an integral part of these consolidated financial statements.*

# CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended December 31, 2018

(Expressed in RMB)

| | Note | Year ended December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|---|
| **Profit/(loss) for the year** | | 13,477,747 | (43,889,115) |
| **Other comprehensive (loss)/income:** | | | |
| *Items that may be reclassified subsequently to profit or loss* | | | |
| Share of other comprehensive income/(loss) of investments accounted for using the equity method | 12(b) | 191,449 | (22,783) |
| Currency translation differences | | (648,746) | (137,124) |
| *Item that will not be reclassified subsequently to profit or loss* | | | |
| Currency translation differences | | (1,098,818) | 8,054,273 |
| **Other comprehensive (loss)/income for the year, net of tax** | | (1,556,115) | 7,894,366 |
| **Total comprehensive income/(loss) for the year** | | 11,921,632 | (35,994,749) |
| **Attributable to:** | | | |
| — Owners of the Company | | 11,989,243 | (35,922,124) |
| — Non-controlling interests | | (67,611) | (72,625) |
| | | 11,921,632 | (35,994,749) |

*The notes on pages 177 to 309 are an integral part of these consolidated financial statements.*

# CONSOLIDATED BALANCE SHEET

As of December 31, 2018

(Expressed in RMB)

| | Note | As of December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|---|
| **Assets** | | | |
| **Non-current assets** | | | |
| Land use rights | 15 | 3,402,968 | 3,416,359 |
| Property and equipment | 16 | 5,068,053 | 1,730,872 |
| Intangible assets | 17 | 2,061,192 | 2,274,352 |
| Investments accounted for using the equity method | 12(b) | 8,639,238 | 1,710,819 |
| Long-term investments measured at fair value through profit or loss | 19 | 18,636,208 | 18,856,961 |
| Deferred income tax assets | 34 | 1,312,245 | 591,576 |
| Other non-current assets | | 95,485 | 150,361 |
| | | 39,215,389 | 28,731,300 |
| **Current assets** | | | |
| Inventories | 23 | 29,480,685 | 16,342,928 |
| Trade receivables | 21 | 5,598,443 | 5,469,507 |
| Loan receivables | 20 | 10,293,645 | 8,144,493 |
| Prepayments and other receivables | 22 | 20,914,946 | 11,393,910 |
| Short-term investments measured at amortized cost | 19 | — | 800,000 |
| Short-term investments measured at fair value through profit or loss | 19 | 6,648,526 | 4,488,076 |
| Short-term bank deposits | 24(c) | 1,365,991 | 225,146 |
| Restricted cash | 24(b) | 1,480,178 | 2,711,119 |
| Cash and cash equivalents | 24(a) | 30,230,147 | 11,563,282 |
| | | 106,012,561 | 61,138,461 |
| **Total assets** | | 145,227,950 | 89,869,761 |
| **Equity and liabilities** | | | |
| **Equity attributable to owners of the Company** | | | |
| Share capital | 25 | 377 | 150 |
| Reserves | | 71,322,608 | (127,272,511) |
| | | 71,322,985 | (127,272,361) |
| **Non-controlling interests** | | (72,856) | 61,670 |
| **Total equity** | | 71,250,129 | (127,210,691) |

# CONSOLIDATED BALANCE SHEET

As of December 31, 2018

(Expressed in RMB)

| | Note | As of December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|---|
| **Liabilities** | | | |
| **Non-current liabilities** | | | |
| Borrowings | 33 | 7,856,143 | 7,251,312 |
| Deferred income tax liabilities | 34 | 777,645 | 1,018,651 |
| Warranty provision | | 559,016 | 191,404 |
| Convertible redeemable preferred shares | 35 | — | 161,451,203 |
| Other non-current liabilities | 29 | 2,844,859 | 35,211 |
| | | 12,037,663 | 169,947,781 |
| **Current liabilities** | | | |
| Trade payables | 30 | 46,287,271 | 34,003,331 |
| Other payables and accruals | 31 | 6,312,770 | 4,223,979 |
| Advance from customers | 32 | 4,479,522 | 3,390,650 |
| Borrowings | 33 | 3,075,194 | 3,550,801 |
| Income tax liabilities | | 661,816 | 421,113 |
| Warranty provision | | 1,123,585 | 1,542,797 |
| | | 61,940,158 | 47,132,671 |
| **Total liabilities** | | 73,977,821 | 217,080,452 |
| **Total equity and liabilities** | | 145,227,950 | 89,869,761 |

*The notes on pages 177 to 309 are an integral part of these consolidated financial statements.*

The consolidated financial statements on pages 169 to 309 were approved by the Board of Directors on March 19, 2019 and were signed on its behalf:

**Lei Jun**
*Director*

**Lin Bin**
*Director*

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended December 31, 2018

(Expressed in RMB)

| | | Attributable to owners of the Company | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Note | Share capital RMB'000 | Share premium RMB'000 | Other reserves RMB'000 | (Accumulated losses)/retained earnings RMB'000 | Sub-total RMB'000 | Non-controlling interests RMB'000 | Total Equity RMB'000 |
| **Balance at January 1, 2018** | | 150 | 742,760 | 947,420 | (128,962,691) | (127,272,361) | 61,670 | (127,210,691) |
| **Comprehensive income** | | | | | | | | |
| Profit for the year | | — | — | — | 13,553,886 | 13,553,886 | (76,139) | 13,477,747 |
| **Other comprehensive income** | | | | | | | | |
| *Items that may be reclassified subsequently to profit or loss* | | | | | | | | |
| Share of other comprehensive income of investments accounted for using the equity method | 12(b) | — | — | 191,449 | — | 191,449 | — | 191,449 |
| Currency translation differences | 26 | — | — | (657,274) | — | (657,274) | 8,528 | (648,746) |
| *Item that will not be reclassified subsequently to profit or loss* | | | | | | | | |
| Currency translation differences | 26 | — | — | (1,098,818) | — | (1,098,818) | — | (1,098,818) |
| **Total comprehensive income** | | — | — | (1,564,643) | 13,553,886 | 11,989,243 | (67,611) | 11,921,632 |
| **Transactions with owners in their capacity as owners** | | | | | | | | |
| Issuance of ordinary shares | 25 | 11 | 9,827,146 | — | — | 9,827,157 | — | 9,827,157 |
| Issuance of ordinary shares relating to initial public offering, net of underwriting commissions and other issuance costs | 25 | 27 | 23,248,593 | — | — | 23,248,620 | — | 23,248,620 |
| Release of ordinary shares from Share Scheme Trusts | 25 | 15 | 933,592 | (841,640) | — | 91,967 | — | 91,967 |
| Conversion of convertible redeemable preferred shares to ordinary shares | 35 | 174 | 151,100,334 | — | — | 151,100,508 | — | 151,100,508 |
| Share of other reserves of investments accounted for using the equity method | 12(b) | — | — | 62,657 | — | 62,657 | — | 62,657 |
| Employees share-based compensation scheme: — value of employee services | 28 | — | — | 2,358,720 | — | 2,358,720 | 102,805 | 2,461,525 |
| Acquisition of additional equity interests in non-wholly owned subsidiaries | 12(a) | — | 230,899 | (152,071) | (162,046) | (83,218) | (171,220) | (254,438) |
| Appropriation to statutory reserves | 26 | — | — | 57,808 | (57,808) | — | — | — |
| Share premium set off the accumulated losses and other reserves | 25 | — | (142,232,042) | 5,579,472 | 136,652,570 | — | — | — |
| Others | | — | — | (308) | — | (308) | 1,500 | 1,192 |
| **Total transactions with owners in their capacity as owners** | | 227 | 43,108,522 | 7,064,638 | 136,432,716 | 186,606,103 | (66,915) | 186,539,188 |
| **Balance at December 31, 2018** | | 377 | 43,851,282 | 6,447,415 | 21,023,911 | 71,322,985 | (72,856) | 71,250,129 |

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended December 31, 2018

(Expressed in RMB)

| | | Attributable to owners of the Company | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Note | Share capital RMB'000 | Share premium RMB'000 | Other reserves RMB'000 | Accumulated losses RMB'000 | Sub-total RMB'000 | Non-controlling interests RMB'000 | Total Equity RMB'000 |
| **Balance at January 1, 2017** | | 150 | 742,760 | (8,124,355) | (84,810,225) | (92,191,670) | 133,795 | (92,057,875) |
| **Comprehensive loss** | | | | | | | | |
| Loss for the year | | — | — | — | (43,826,016) | (43,826,016) | (63,099) | (43,889,115) |
| **Other comprehensive income** | | | | | | | | |
| *Items that may be reclassified subsequently to profit or loss* | | | | | | | | |
| Share of other comprehensive loss of investments accounted for using the equity method | 12(b) | — | — | (22,783) | — | (22,783) | — | (22,783) |
| Currency translation differences | 26 | — | — | (127,598) | — | (127,598) | (9,526) | (137,124) |
| *Item that will not be reclassified subsequently to profit or loss* | | | | | | | | |
| Currency translation differences | 26 | — | — | 8,054,273 | — | 8,054,273 | — | 8,054,273 |
| **Total comprehensive loss** | | — | — | 7,903,892 | (43,826,016) | (35,922,124) | (72,625) | (35,994,749) |
| **Transactions with owners in their capacity as owners** | | | | | | | | |
| Share of other reserves of investments accounted for using the equity method | 12(b) | — | — | 33,539 | — | 33,539 | — | 33,539 |
| Employees share-based compensation scheme: | | | | | | | | |
| — value of employee services | 28 | — | — | 807,894 | — | 807,894 | — | 807,894 |
| Appropriation to statutory reserves | 26 | — | — | 326,450 | (326,450) | — | — | — |
| Others | | — | — | — | — | — | 500 | 500 |
| **Total transactions with owners in their capacity as owners** | | — | — | 1,167,883 | (326,450) | 841,433 | 500 | 841,933 |
| **Balance at December 31, 2017** | | 150 | 742,760 | 947,420 | (128,962,691) | (127,272,361) | 61,670 | (127,210,691) |

*The notes on pages 177 to 309 are an integral part of these consolidated financial statements.*

# CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended December 31, 2018

(Expressed in RMB)

| | Note | Year ended December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Cash generated from operations | 36(a) | 122,171 | 527,321 |
| Income tax paid | | (1,536,742) | (1,522,990) |
| Net cash used in operating activities | | (1,414,571) | (995,669) |
| **Cash flows from investing activities** | | | |
| Capital expenditures | | (3,785,259) | (1,217,806) |
| Proceeds from disposal of property and equipment | 36(b) | 27,367 | 1,531 |
| Placement of short-term bank deposits | | (2,060,799) | (255,262) |
| Withdrawal of short-term bank deposits | | 903,504 | 448,690 |
| Purchase of short-term investments measured at fair value through profit or loss | | (140,955,400) | (104,284,000) |
| Receipt from maturity of short-term investments measured at fair value through profit or loss | | 139,154,171 | 103,254,537 |
| Purchase of short-term investments measured at amortized cost | | (3,500,000) | (10,641,000) |
| Receipt from maturity of short-term investments measured at amortized cost | | 4,300,000 | 9,921,000 |
| Interest income received | | 489,816 | 266,054 |
| Investment income received | | 335,695 | 162,702 |
| Purchase of long-term investments measured at fair value through profit or loss | | (1,999,752) | (813,175) |
| Proceeds from disposal of long-term investments measured at fair value through profit or loss | | 304,999 | 494,018 |
| Purchase of investments accounted for using the equity method | | (793,595) | (156,551) |
| Disposal of a subsidiary | | (25,655) | — |
| Acquisition of a subsidiary, net of cash acquired | | (34,936) | — |
| Dividends received | | 131,804 | 141,548 |
| Net cash used in investing activities | | (7,508,040) | (2,677,714) |

# CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended December 31, 2018

(Expressed in RMB)

| | Note | Year ended December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|---|
| **Cash flows from financing activities** | | | |
| Proceeds from issuance of convertible redeemable preferred shares | | — | 67,573 |
| Proceeds from borrowings | | 10,269,415 | 11,174,861 |
| Repayment of borrowings | | (10,505,637) | (4,531,248) |
| Finance expenses paid | | (243,966) | (207,384) |
| Placement of restricted cash | | (4,152,345) | (913,202) |
| Withdrawal of restricted cash | | 5,059,245 | 624,330 |
| Payment for acquisition of non-controlling interests in a non-wholly owned subsidiary | | (165,000) | — |
| Proceeds from fund investors | | 2,781,000 | — |
| Net proceeds from issuance of ordinary shares relating to the initial public offering | | 23,248,620 | — |
| Proceeds from release of ordinary shares from Share Scheme Trusts | | 91,967 | — |
| Others | | 190,873 | — |
| Net cash generated from financing activities | | 26,574,172 | 6,214,930 |
| **Net increase in cash and cash equivalents** | | 17,651,561 | 2,541,547 |
| Cash and cash equivalents at the beginning of the year | 24(a) | 11,563,282 | 9,230,320 |
| Effects of exchange rate changes on cash and cash equivalents | | 1,015,304 | (208,585) |
| **Cash and cash equivalents at the end of the year** | 24(a) | 30,230,147 | 11,563,282 |

*The notes on pages 177 to 309 are an integral part of these consolidated financial statements.*

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 1 General information

Xiaomi Corporation (formerly known as Top Elite Limited) (the "**Company**"), was incorporated in the Cayman Islands on January 5, 2010 as an exempted company with limited liability under the Companies Law, Cap. 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands. The address of the Company's registered office is at the offices of Maples Corporate Services Limited, PO Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands.

The Company is an investment holding company. The Company and its subsidiaries, including controlled structured entities (together, the "**Group**") are principally engaged in development and sales of smartphones, internet of things ("**IoT**") and lifestyle products, provision of internet services and investments holding in the People's Republic of China and other countries or regions.

Lei Jun is the ultimate controlling shareholder of the Company as of the date of approval of these consolidated financial statements.

The regulations in mainland China restrict foreign ownership of companies that provide internet services, e-commerce and value-added telecommunications services, etc., which include certain activities and services operated by the Group. In order to enable certain foreign companies to make investments into these businesses of the Group, the Company controls certain subsidiaries through contractual arrangements. On August 25, 2010, a wholly owned subsidiary of the Company, Xiaomi Communications Co., Ltd. ("**Xiaomi Communications**", a wholly foreign-owned enterprise) had entered into a series of contractual arrangements (the "**Contractual Arrangements**") with Xiaomi Inc. and its equity holders, which enable Xiaomi Communications and the Group to:

- govern the financial and operating policies of Xiaomi Inc.;
- exercise equity holders' voting rights of Xiaomi Inc.;
- receive substantially all of the economic interest returns generated by Xiaomi Inc. in consideration for the business support, technical and consulting services provided by Xiaomi Communications;
- obtain an irrevocable and exclusive right to purchase all or part of the equity interests in Xiaomi Inc. from the respective equity holders at a minimum purchase price when it is permitted under laws and regulations in mainland China. Xiaomi Communications may exercise such options at any time until it has acquired all equity interests of Xiaomi Inc.; and

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 1 General information (continued)

- obtain a pledge over the entire equity interests of Xiaomi Inc. from its respective equity holders as collateral security for all of Xiaomi Inc.'s payments due to Xiaomi Communications and to secure performance of Xiaomi Inc.'s obligation under the Contractual Arrangements.

As a result of the Contractual Arrangements, the Group has rights to exercise power over Xiaomi Inc. and its subsidiaries, receives variable returns from its involvement in Xiaomi Inc. and its subsidiaries, has the ability to affect those returns through its power over Xiaomi Inc. and its subsidiaries and is considered to control Xiaomi Inc. and its subsidiaries. Consequently, the Company regards Xiaomi Inc. and its subsidiaries as controlled structured entities and consolidated the assets, liabilities and results of operations of Xiaomi Inc. and its subsidiaries in the consolidated financial information of the Group.

Nevertheless, the Contractual Arrangements may not be as effective as direct legal ownership in providing the Group with direct control over Xiaomi Inc. and its subsidiaries. Uncertainties presented by the legal system in mainland China could impede the Group's beneficiary rights of the results, assets and liabilities of Xiaomi Inc. and its subsidiaries. The directors of the Company, based on the advice of its legal counsel, consider that the Contractual Arrangements among Xiaomi Communications, Xiaomi Inc. and its equity holders are in compliance with the relevant laws and regulations in mainland China and are legally binding and enforceable.

Other Contractual Arrangements were also executed for other operating companies in mainland China established by the Group similar to Xiaomi Inc. subsequently. All of these operating companies are treated as controlled structured entities of the Company and their financial statements have also been consolidated by the Company. See details in Note 12(a).

On July 9, 2018, the Company has successfully listed on the Main Board of The Stock Exchange of Hong Kong Limited (the "**Stock Exchange**") and made an offering of 2,179,585,000 Class B ordinary shares (excluding any Class B ordinary shares issued pursuant to the exercise of the over-allotment option) at a price at Hong Kong Dollar ("**HK$**") 17.00 per share. Additionally, the Company issued and allotted 201,486,000 Class B ordinary shares on July 20, 2018 pursuant to the full exercise of the over-allotment option as disclosed in the announcement of the Company dated July 18, 2018. The gross proceeds received by the Company was approximately HK$27,810,742,000 (equivalent to approximately RMB23,525,107,000), refer to Note 25(f) for details. All convertible redeemable preferred shares ("**Preferred Shares**") were converted into Class B ordinary shares upon completion of the initial public offering ("**IPO**") on July 9, 2018, refer to Note 35 for details.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied throughout all the years presented, unless otherwise stated.

### 2.1 Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with all applicable International Financial Reporting Standards ("**IFRSs**") issued by International Accounting Standards Board ("**IASB**") and disclosure requirements of the Hong Kong Companies Ordinance.

The Group has already adopted IFRS 9 "Financial Instruments" ("**IFRS 9**") and IFRS 15 "Revenue from Contracts with Customers" ("**IFRS 15**") upon its first time adoption of IFRSs from January 1, 2015.

The consolidated financial statements of the Group have been prepared under the historical cost convention, as modified by the revaluation of financial assets and financial liabilities which are carried at fair value.

The preparation of consolidated financial statements in conformity with IFRSs requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

### 2.2 Changes in accounting policy and disclosures

**(a) New standards and amendments to existing standards adopted by the Group**

The following interpretation, amendments and improvements to standards, which are relevant to the Group, are first effective from January 1, 2018.

- Annual Improvements to IFRSs 2014–2016 Cycle
- Amendments to IAS 40 Transfers of Investment Property
- IFRIC-Int 22 Foreign Currency Transactions and Advance Consideration
- Amendments to IFRS 2 Classification and Measurement of Share-based Payments Transactions

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.2 Changes in accounting policy and disclosures (continued)

(a) **New standards and amendments to existing standards adopted by the Group (continued)**

The adoption of these interpretation and amendments to standards has had no significant impact on the results and the financial position of the Group.

(b) **New standards and interpretations not yet adopted**

Standards, amendments and interpretations that have been issued but not yet effective and not been early adopted by the Group during the year are as follows:

| | | Effective for annual period beginning on or after |
|---|---|---|
| IFRS 16 | Leases | January 1, 2019 |
| IFRS 17 | Insurance contracts | January 1, 2021 |
| IFRIC 23 | Uncertainty over income tax treatments | January 1, 2019 |
| Amendments to IAS 19 | Employee benefits on plan amendment, curtailment or settlement | January 1, 2019 |
| Amendments to IFRS | Annual Improvements to IFRSs Standards 2015–2017 Cycle | January 1, 2019 |
| Amendment to IFRS 3 | Definition of a business | January 1, 2020 |
| Amendments to IAS 1 and IAS 8 | Definition of material | January 1, 2020 |
| Amendments to IAS 28 | Long-term interests in associates and joint ventures | January 1, 2019 |
| Amendment to IFRS 9 | Prepayment features with negative compensation | January 1, 2019 |

None of these is expected to have a significant effect on the consolidated financial statements of the Group, except for the following as set out below:

IFRS 16 "Leases" ("**IFRS 16**")

IFRS 16 was issued in January 2016. It will result in almost all leases being recognized on the balance sheet by lessees, as the distinction between operating and finance leases is removed. Under the new standard, an asset (the right to use the leased item) and a financial liability to pay rentals are recognized. The only exceptions are short-term and low-value leases.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.2 Changes in accounting policy and disclosures (continued)

**(b) New standards and interpretations not yet adopted (continued)**

The Group will apply the standard from its mandatory adoption date of January 1, 2019. The Group intends to apply the simplified transition approach and will not restate comparative amounts for the year prior to first adoption. All right-of-use assets will be measured at the amount of the lease liability on adoption (adjusted for any prepaid or accrued lease expenses).

The Group has reviewed all of the Group's leasing arrangements over the last year in light of the new lease accounting rules in IFRS 16. The standard will affect primarily the accounting for the Group's operating leases. As of December 31, 2018, the Group has non-cancellable operating lease commitments of RMB1,029,240,000. Of these commitments, approximately RMB258,968,000 relate to short-term leases which will be recognized on a straight-line basis as expense in profit or loss. For the remaining lease commitments of RMB770,272,000, the Group expects to recognize right-of-use assets and lease liabilities (adjusted for any prepaid or accrued lease expense) on January 1, 2019, respectively.

### 2.3 Subsidiaries

**2.3.1 Consolidation**

A subsidiary is an entity (including a structured entity) over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases.

Intra-group transactions, balances and unrealized gains on transactions between group companies are eliminated. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the transferred asset. When necessary, amounts reported by subsidiaries have been adjusted to conform with the Group's accounting policies.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.3 Subsidiaries (continued)

#### 2.3.1 Consolidation (continued)

**(a) Subsidiaries controlled through Contractual Arrangements**

There are entities controlled by the Group under Contractual Arrangements. The Group does not have legal ownership in equity of these structured entities or their subsidiaries. Nevertheless, under Contractual Arrangements entered into with the registered owners of these structured entities, the Company and its other legally owned subsidiaries control these companies by way of controlling the voting rights, governing their financial and operating policies, appointing or removing the majority of the members of their controlling authorities, and casting the majority of votes at meetings of such authorities. Accordingly, the Group has rights to exercise power over these structured entities, receives variable returns from its involvement in these structured entities, and has the ability to affect those returns through its power over these structured entities. As a result, they are presented as controlled structured entities of the Group.

**(b) Business combination**

The Group applies the acquisition method to account for business combinations except for business combination under common control. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date.

The Group recognizes any non-controlling interest in the acquiree on an acquisition-by-acquisition basis either at fair value or at the non-controlling interest's proportionate share of the acquiree's net identifiable assets.

Acquisition-related costs are expensed as incurred.

If the business combination is achieved in stages, the acquisition date carrying value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date; any gains or losses arising from such remeasurement are recognized in profit or loss.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.3 Subsidiaries (continued)

#### 2.3.1 Consolidation (continued)

**(b) Business combination (continued)**

Any contingent consideration to be transferred by the Group is recognized at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration that is deemed to be an asset or liability is recognized in accordance with IFRS 9 in profit or loss. Contingent consideration that is classified as equity is not remeasured, and its subsequent settlement is accounted for within equity.

The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired is recorded as goodwill. If those amounts are less than the fair value of the net assets of the business acquired in the case of a bargain purchase, the difference is recognized directly in the profit or loss.

An acquisition of a business which is a business combination under common control is accounted for in a manner similar to a uniting of interests whereby the assets and liabilities acquired are accounted for at carryover predecessor values to the other party to the business combination within all periods presented as if the operations of the Group and the business acquired have always been combined. The difference between the consideration paid by the Group and the net assets or liabilities of the business acquired is adjusted against equity.

**(c) Changes in ownership interests in subsidiaries without change of control**

Transactions with non-controlling interests that do not result in a loss of control are accounted for as equity transactions—that is, as transactions with the owners of the subsidiary in their capacity as owners. The difference between fair value of any consideration paid and the relevant share acquired of the carrying amount of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

**(d) Disposal of subsidiaries**

When the Group ceases to have control, any retained interest in the entity is re-measured to its fair value at the date when control is lost, with the change in carrying amount recognized in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognized in other comprehensive income in respect of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities. It means the amounts previously recognized in other comprehensive income ("**OCI**") are reclassified to profit or loss, or transferred to another category of equity as specified/permitted by applicable IFRSs.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.3 Subsidiaries (continued)

#### 2.3.2 Separate financial statements

Investments in subsidiaries (including controlled structured entities) are accounted for at cost less impairment. Cost includes direct attributable costs of investment. The results of subsidiaries are accounted for by the Company on the basis of dividend received and receivable.

Impairment testing of the investments in subsidiaries is required upon receiving a dividend from these investments if the dividend exceeds the total comprehensive income of the subsidiary in the period the dividend is declared or if the carrying amount of the investment in the separate financial statements exceeds the carrying amount in the consolidated financial information of the investee's net assets including goodwill.

### 2.4 Associates

An associate is an entity over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights.

#### (a) Investments in associates in the form of ordinary shares

Investments in associates in the form of ordinary shares are accounted for using the equity method of accounting in accordance with IAS 28 "Investments in Associates and Joint Ventures". Under the equity method, the investment is initially recognized at cost, and the carrying amount is increased or decreased to recognize the investor's share of the profit or loss of the investee after the date of acquisition. The Group's investments in these associates include goodwill identified on acquisition, net of any accumulated impairment loss. Upon the acquisition of the ownership interest in an associate, any difference between the cost of the associate and the Group's share of the net fair value of the associate's identifiable assets and liabilities is accounted for as goodwill.

If the ownership interest in an associate in the form of ordinary shares is reduced but significant influence is retained, only a proportionate share of the amounts previously recognized in other comprehensive income is reclassified to consolidated income statement where appropriate.

The Group's share of the associates' post-acquisition profit or loss is recognized in the consolidated income statement, and its share of post-acquisition movements in other comprehensive income is recognized in other comprehensive income. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognize further losses, unless it has incurred legal or constructive obligations or made payments on behalf of the associate.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.4 Associates (continued)

#### (a) Investments in associates in the form of ordinary shares (continued)

The Group determines at each reporting date whether there is any objective evidence that the investments in the associate are impaired. If this is the case, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and includes the amount in "other gains, net" in the consolidated income statement.

Profits and losses resulting from upstream and downstream transactions between the Group and its associate are recognized in the Group's financial statements only to the extent of unrelated investor's interests in the associates. Unrealized losses are eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

Gain or losses on dilution of equity interest in associates are recognized in the consolidated income statement.

#### (b) Investments in associates in the form of ordinary shares with preferential rights or convertible redeemable preferred shares

Investments in associates in the form of ordinary shares with preferential rights or convertible redeemable preferred shares are accounted as financial assets measured at fair value through profit or loss (Note 2.11).

### 2.5 Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker ("**CODM**"). The CODM, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Chief Executive Officer that makes strategic decisions.

### 2.6 Foreign currency translation

#### (a) Functional and presentation currency

Items included in the financial information of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "**functional currency**"). The functional currency of the Company is United States dollar ("**US$**"). The Company's primary subsidiaries were incorporated in mainland China and these subsidiaries considered RMB as their functional currency. As the major operations of the Group are within mainland China, the Group determined to present its consolidated financial statements in RMB (unless otherwise stated).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.6 Foreign currency translation (continued)

**(b) Transactions and balances**

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where items are re-measured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the consolidated income statement. Foreign exchange gains and losses are presented in the consolidated income statement within "other gains, net".

Translation differences on non-monetary financial assets and liabilities are recognized in profit or loss as part of the fair value changes.

**(c) Group companies**

The results and financial position of all the Group entities (none of which has the currency of a hyper-inflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions); and
- all resulting currency translation differences are recognized in other comprehensive income.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate. Currency translation differences arising are recognized in other comprehensive income.

**(d) Disposal of foreign operation and partial disposal**

On the disposal of a foreign operation (that is, a disposal of the Group's entire interest in a foreign operation, or a disposal involving loss of control over a subsidiary that includes a foreign operation, a disposal involving loss of joint control over a joint venture that includes a foreign operation, or a disposal involving loss of significant influence over an associate that includes a foreign operation), all of the currency translation differences accumulated in equity in respect of that operation attributable to the owners of the Company are reclassified to profit or loss.

## 2 Summary of significant accounting policies (continued)

### 2.6 Foreign currency translation (continued)

**(d) Disposal of foreign operation and partial disposal (continued)**

In the case of a partial disposal that does not result in the Group losing control over a subsidiary that includes a foreign operation, the proportionate share of accumulated currency translation differences are re-attributed to non-controlling interests and are not recognized in profit or loss. For all other partial disposals (that is, reductions in the Group's ownership interest in associates or joint ventures that do not result in the Group losing significant influence or joint control), the proportionate share of the accumulated exchange difference is reclassified to profit or loss.

### 2.7 Property and equipment

Property and equipment are stated at historical cost less accumulated depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are charged to profit or loss during the financial period in which they are incurred.

Depreciation on property and equipment is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

| | |
|---|---|
| — Leasehold improvements | Estimated useful lives or remaining lease terms, whichever is shorter |
| — Electronic equipment | 3 years |
| — Office equipment | 3–5 years |

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

Construction in progress mainly represents office buildings under construction, which is stated at actual construction cost less accumulated impairment losses. Construction in progress is transferred to appropriate categories of property and equipment upon the completion of their respective construction and depreciated over their respective estimated useful lives.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2.10).

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognized within "other gains, net" in the consolidated income statement.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.8 Land use rights

Land use rights represent prepayments for the land use rights in mainland China and are stated at cost initially and expensed on a straight-line basis over the periods of the leases.

### 2.9 Intangible assets

**(a) Goodwill**

Goodwill arises from the acquisition of subsidiaries represents the excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identified net assets acquired.

For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the cash-generating units ("**CGUs**"), or groups of CGUs, that is expected to benefit from the synergies of the combination. Each unit or group of units to which the goodwill is allocated represents the lowest level within the entity at which the goodwill is monitored for internal management purposes. Goodwill is monitored at the operating segment level.

Goodwill impairment reviews are undertaken annually or more frequently if events or changes in circumstances indicate a potential impairment. The carrying value of the CGU containing the goodwill is compared to the recoverable amount, which is the higher of value in use and the fair value less costs of disposal. Any impairment is recognized immediately as an expense and is not subsequently reversed.

**(b) License**

License includes third-party payment license and other licenses. Third-party payment license represents the license issued by the People's Republic of China government authorities that enable the Group to operate third-party payment business. Other licenses mainly include the licenses to use certain intellectual properties purchased from third parties. These acquired licenses are shown at historical cost. License that have an indefinite useful life are tested annually for impairment and carried at cost less accumulated impairment losses. Others are amortized over their estimated useful lives of 1 to 10 years using straight-line method.

**(c) Trademarks, patents and domain name**

Separately acquired trademarks, patents and domain name are shown at historical cost. Trademarks, patents and domain name acquired in a business combination are recognized at fair value at the acquisition date. Trademarks, patents and domain name have a finite useful life and are carried at cost less accumulated amortization. Amortization is calculated using the straight-line method to allocate the cost of trademarks, patents and domain name over their estimated useful lives of 1 to 16 years.

## 2 Summary of significant accounting policies (continued)

### 2.9 Intangible assets (continued)

**(d) Other intangible assets**

Other intangible assets mainly include computer software. They are initially recognized and measured at costs incurred to acquire and bring them to use. Other intangible assets are amortized on a straight-line basis over their estimated useful lives, and recorded in amortization within operating expenses in the consolidated income statement.

**(e) Research and development expenditures**

Research expenditure is recognized as an expense as incurred. Costs incurred on development projects (relating to the design and testing of new or improved products) are capitalized as intangible assets when recognition criteria are fulfilled. These criteria include:

- it is technically feasible to complete the software product so that it will be available for use;
- management intends to complete the software product and use or sell it;
- there is an ability to use or sell the software product;
- it can be demonstrated how the software product will generate probable future economic benefits;
- adequate technical, financial and other resources to complete the development and to use or sell the software product are available; and
- the expenditure attributable to the software product during its development can be reliably measured.

Other development expenditures that do not meet these criteria are recognized as an expense as incurred.

### 2.10 Impairment of non-financial assets

Intangible assets that have an indefinite useful life are not subject to amortization and are tested annually for impairment. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.11 Financial assets

#### 2.11.1 Classification

The Group classifies its financial assets in the following measurement categories:

- those to be measured subsequently at fair value (either through other comprehensive income, or through profit or loss), and
- those to be measured at amortized cost.

The classification depends on the Group's business model for managing the financial assets and the contractual terms of the cash flows.

For assets measured at fair value, gains and losses will either be recorded in profit or loss or other comprehensive income. For investments in debt instruments, this will depend on the business model in which the investment is held. For investments in equity instruments that are not held for trading, this will depend on whether the Group has made an irrevocable election at the time of initial recognition to account for the equity investment at fair value through other comprehensive income.

See Note 18 for details of each type of financial asset.

The Group reclassifies debt investments when and only when its business model for managing those assets changes.

#### 2.11.2 Measurement

At initial recognition, the Group measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at fair value through profit or loss are recorded in profit or loss.

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

## 2 Summary of significant accounting policies (continued)

### 2.11 Financial assets (continued)

#### 2.11.2 Measurement (continued)

*Debt instruments*

Subsequent measurement of debt instruments depends on the Group's business model for managing the asset and the cash flow characteristics of the asset. There are three measurement categories into which the Group classifies its debt instruments:

- Amortized cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortized cost. A gain or loss on a debt investment that is subsequently measured at amortized cost and is not part of a hedging relationship is recognized in profit or loss when the asset is derecognized or impaired. Interest income from these financial assets is included in finance income using the effective interest method.

- Fair value through other comprehensive income ("**FVOCI**"): Assets that are held for collection of contractual cash flows and for selling the financial assets, where the assets' cash flows represent solely payments of principal and interest, are measured at FVOCI. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest income and foreign exchange gains and losses which are recognized in profit or loss. When the financial asset is derecognized, the cumulative gain or loss previously recognized in OCI is reclassified from equity to profit or loss and recognized in other gains, net. Interest income from these financial assets is included in finance income using the effective interest rate method. Foreign exchange gains and losses are presented in other gains, net.

- Fair value through profit or loss ("**FVPL**"): Assets that do not meet the criteria for amortized cost or FVOCI are measured at FVPL. A gain or loss on a debt investment that is subsequently measured at FVPL and is not part of a hedging relationship is recognized in profit or loss and presented net in the statement of profit or loss within other gains, net in the period in which it arises.

*Equity instruments*

The Group subsequently measures all equity investments at fair value. Where the Group's management has elected to present fair value gains and losses on equity investments in OCI, there is no subsequent reclassification of fair value gains and losses to profit or loss following the derecognition of the investment. Dividends from such investments continue to be recognized in profit or loss as other income when the Group's right to receive payments is established.

Changes in the fair value of financial assets at FVPL are recognized in the consolidated income statement. Impairment losses (and reversal of impairment losses) on equity investments measured at FVOCI are not reported separately from other changes in fair value.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.11 Financial assets (continued)

#### 2.11.3 Impairment

The Group has types of financial assets subject to IFRS 9's new expected credit loss model:

- loan receivables from internet finance business;
- trade receivables for sales of goods or provision of services; and
- other receivables

The Group assesses on a forward looking basis the expected credit losses associated with its debt instruments carried at amortized cost including loan receivables, and with the exposure arising from financial guarantee contracts. The impairment methodology applied depends on whether there has been a significant increase in credit risk. Note 3.1(b) details how the Group determines whether there has been a significant increase in credit risk.

For trade receivables, the Group applies the simplified approach permitted by IFRS 9, which requires expected lifetime losses to be recognized from initial recognition of the receivables.

Impairment on other receivables is measured as either 12-month expected credit losses or lifetime expected credit loss, depending on whether there has been a significant increase in credit risk since initial recognition. If a significant increase in credit risk of a receivable has occurred since initial recognition, then impairment is measured as lifetime expected credit losses.

#### 2.11.4 Derecognition

*Financial assets*

The Group derecognizes a financial asset, if the part being considered for derecognition meets one of the following conditions: (i) the contractual rights to receive the cash flows from the financial asset expire; or (ii) the contractual rights to receive the cash flows of the financial asset have been transferred, the Group transfers substantially all the risks and rewards of ownership of the financial asset; or (iii) the Group retains the contractual rights to receive the cash flows of the financial asset, but assumes a contractual obligation to pay the cash flows to the eventual recipient in an agreement that meets all the conditions of de-recognition of transfer of cash flows ("pass through" requirements) and transfers substantially all the risks and rewards of ownership of the financial asset.

## 2 Summary of significant accounting policies (continued)

### 2.11 Financial assets (continued)

#### 2.11.4 Derecognition (continued)

*Financial assets (continued)*

Where a transfer of a financial asset in its entirety meets the criteria for derecognition, the difference between the two amounts below is recognized in profit or loss:

- the carrying amount of the financial asset transferred; and
- the sum of the consideration received from the transfer and any cumulative gain or loss that has been recognized directly in equity.

If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group continues to recognize the asset to the extent of its continuing involvement and recognizes an associated liability.

*Asset-backed securities*

As part of its operations, the Group securitizes financial assets, generally through the sale of these assets to special purpose vehicles which issue securities to investors. Further details on prerequisites for derecognition of financial assets are set out above. When the securitization of financial assets that qualify for derecognition, the relevant financial assets are derecognized in their entirety and a new financial asset or liabilities is recognized regarding the interest in the unconsolidated securitization vehicles that the Group acquired. When the securitization of financial assets that do not qualify for derecognition, the relevant financial assets are not derecognized, and the consideration paid by third parties are recorded as a financial liability; when the securitization of financial assets that partially qualify for derecognition, the book value of the transferred asset should be recognized between the derecognized portion and the retained portion based on their respective relative fair values, and the difference between the book value of the derecognized portion and the total consideration paid for the derecognized portion shall be recorded in profit or loss.

*Other financial liabilities*

A financial liability is derecognized when the obligation under the liability is discharged, canceled, or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and a recognition of a new liability, and the difference between the respective carrying amounts is recognized in profit or loss.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.12 Financial guarantee contracts

Financial guarantee contracts are recognized as a financial liability at the time the guarantee is issued. The liability is initially measured at fair value and subsequently at the higher of

- the amount determined in accordance with the expected credit loss model under IFRS 9 and
- the amount initially recognized less, where appropriate, the cumulative amount of income recognized in accordance with the principles of IFRS 15.

The fair value of financial guarantees is determined based on the present value of the difference in cash flows between the contractual payments required under the debt instrument and the payments that would be required without the guarantee, or the estimated amount that would be payable to a third party for assuming the obligations.

Where guarantees in relation to loans or other payables of associates are provided for no compensation, the fair values are accounted for as contributions and recognized as part of the cost of the investment.

### 2.13 Inventories

Inventories are stated at the lower of cost and net realizable value. Cost is determined using the weighted average method. The cost of finished goods and work in progress comprises raw materials, assembly cost and other direct costs. It excludes borrowing costs. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs to completion, applicable variable selling expense and related tax.

### 2.14 Trade and other receivables

Trade receivables are amounts due from customers for products sold or services performed in the ordinary course of business. Majority of other receivables are amounts due from outsourcing partners for raw material delivered in the ordinary course of business and value-added tax and other tax recoverable. If collection of trade and other receivables is expected in one year or less (or in the normal operating cycle of the business if longer), they are classified as current assets. If not, they are presented as non-current assets.

Trade and other receivables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method, less provision for impairment. See Note 2.11.3 for a description of the Group's impairment policy for trade and other receivables.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.15 Loan receivables

Loan receivables held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are recognized initially at fair value plus transaction costs that are attributable to the acquisition of the assets and subsequently measured at amortized cost using the effective interest method, less provision for impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and includes fees or costs that are an integral part of the effective interest rate. The effective interest rate amortization is included in the profit or loss. The loss arising from impairment is recognized in profit or loss. See Note 2.11.3 for a description of the Group's impairment policy for loan receivables.

### 2.16 Cash and cash equivalents

In the consolidated statements of cash flows, cash and cash equivalents includes cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less.

### 2.17 Share capital

Ordinary shares are classified as equity. Convertible redeemable preferred shares are classified as liabilities (see Note 2.19).

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction from the proceeds.

### 2.18 Trade payables

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Trade payables are classified as current liabilities if payment is due within one year (or in the normal operating cycle of the business if longer). If not, they are presented as non-current liabilities.

Trade payables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.19 Convertible redeemable preferred shares

Convertible redeemable preferred shares issued by the Company are redeemable at the option of the holders at any time commencing on the redemption start date of December 23, 2019. This instrument can be converted into Class B ordinary shares of the Company at the option of a holder after July 3, 2015, or automatically converted into ordinary shares upon occurrence of (i) the closing of a Qualified Public Offering ("**QPO**", as defined in Note 35), or (ii) with written consent of holders of more than fifty percent (50%) of the issued and outstanding Series A Preferred Shares, or written consent of holders of more than two thirds (2/3) of the issued and outstanding Preferred Shares (other than Series A Preferred Shares), as detailed in Note 35.

The Group designated the Preferred Shares as financial liabilities at fair value through profit or loss. They are initially recognized at fair value. Any directly attributable transaction costs are recognized as finance costs in the consolidated income statement.

Subsequent to initial recognition, the Preferred Shares are carried at fair value with changes in fair value recognized in the consolidated income statement.

The Preferred Shares are classified as non-current liabilities if the Preferred Shares holders cannot demand the Company to redeem the Preferred Shares for at least 12 months after the end of the reporting period.

### 2.20 Borrowings

Borrowings are recognized initially at fair value, net of transaction costs incurred. Borrowings are subsequently carried at amortized cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the consolidated income statement over the period of the borrowings using the effective interest method.

Fees paid on the establishment of loan facilities are recognized as transaction costs of the loan to the extent that it is probable that some or all of the facility will be drawn down. In this case, the fee is deferred until the draw-down occurs. To the extent there is no evidence that it is probable that some or all of the facility will be drawn down, the fee is capitalized as a pre-payment for liquidity services and amortized over the period of the facility to which it relates.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the end of the reporting period.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.21 Borrowing costs

General and specific borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalization.

All other borrowing costs are recognized in profit or loss in the period in which they are incurred.

### 2.22 Dividend distribution

Dividend distribution to the Company's shareholders is recognized as a liability in the Group's financial statements in the period in which the dividends are approved by the Company's shareholders or directors, where appropriate.

### 2.23 Current and deferred income tax

The income tax expense for the period comprises current and deferred tax. Income tax is recognized in the consolidated income statement, except to the extent that it relates to items recognized in other comprehensive income or directly in equity. In this case, the income tax is also recognized in other comprehensive income or directly in equity, respectively.

#### (a) Current income tax

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the Company and its subsidiaries operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.23 Current and deferred income tax (continued)

(b) **Deferred income tax**

*Inside basis differences*

Deferred income tax is recognized, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax liabilities are not recognized if they arise from the initial recognition of goodwill, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred income tax assets are recognized only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

*Outside basis differences*

Deferred income tax liabilities are provided on taxable temporary differences arising from investments in subsidiaries, associates and joint arrangements, except for deferred income tax liability where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future. Generally the Group is unable to control the reversal of the temporary difference for associates. Only when there is an agreement in place that gives the Group the ability to control the reversal of the temporary difference in the foreseeable future, deferred tax liability in relation to taxable temporary differences arising from the associate's undistributed profits is not recognized.

Deferred income tax assets are recognized on deductible temporary differences arising from investments in subsidiaries and associates only to the extent that it is probable the temporary difference will reverse in the future and there is sufficient taxable profit available against which the temporary difference can be utilized.

(c) **Offsetting**

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current income tax assets against current income tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.24 Employee benefits

(a) **Pension obligations**

The Group operates a mandatory provident fund scheme ("**MPF Scheme**") for the eligible employees in Hong Kong. The MPF Scheme is a defined contribution scheme, the assets of which are held in separate trustee — administered funds. The Group's contributions to MPF Scheme are expensed as incurred.

The Group's subsidiaries operating in mainland China have to make contribution to staff retirement scheme managed by local government authorities in accordance with the relevant rules and regulations. Contributions to these schemes are charged to the consolidated income statement as and when incurred. The Group has no legal or constructive obligations to pay further contributions.

(b) **Employee leave entitlements**

Employee entitlements to annual leave are recognized when they accrue to employees. A provision is made for the estimated liability for annual leave as a result of services rendered by employees up to the balance sheet date. Employee entitlements to sick leave and maternity leave are not recognized until the time of leave.

(c) **Bonus plans**

The expected cost of bonuses is recognized as a liability when the Group has a present legal or constructive obligation for payment of bonus as a result of services rendered by employees and a reliable estimate of the obligation can be made. Liabilities for bonus plans are expected to be settled within 1 year and are measured at the amounts expected to be paid when they are settled.

### 2.25 Share-based payment

(a) **Equity-settled share-based payment transactions**

The Group operates share incentive plan, under which it receives services from employees as consideration for equity instruments (restricted shares units ("**RSUs**") and options) of the Company. The fair value of the services received in exchange for the grant of the equity instruments (RSUs and options) is recognized as an expense on the consolidated income statement with a corresponding increase in equity.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.25 Share-based payment (continued)

#### (a) Equity-settled share-based payment transactions (continued)

In terms of the RSUs and options awarded to employees, the total amount to be expensed is determined by reference to the fair value of equity instruments (RSUs and options) granted:

- including any market performance conditions;
- excluding the impact of any service and non-market performance vesting conditions; and
- including the impact of any non-vesting conditions.

Service and non-marketing performance conditions are included in calculation of the number of RSUs and options that are expected to vest. The total amount expensed is recognized over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied.

At the end of each reporting period, the Group revises its estimates of the number of RSUs and options that are expected to vest based on the non-marketing performance and service conditions. It recognizes the impact of the revision to original estimates, if any, in the consolidated income statement, with a corresponding adjustment to equity.

In some circumstances, employees may provide services in advance of the grant date and therefore the grant date fair value is estimated for the purposes of recognizing the expense during the period between service commencement period and grant date.

When the options are exercised, the Company issues new ordinary shares. The proceeds received net of any directly attributable transaction costs are credited to share capital and share premium.

#### (b) Cash-settled share-based payment transactions

The cost of cash-settled transactions is measured initially at fair value at the grant date. This fair value is with recognition of a corresponding liability. The liability is re-measured at each reporting date up to and at the date of settlement, with any changes in fair value recognized in profit or loss for the year.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.26 Provisions

Provisions are recognized when the Group has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognized for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognized even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

**(a) Warranty provision**

The Group records warranty liabilities at the time of sale for the estimated costs that will be incurred under its basic limited warranty. The specific warranty terms and conditions vary depending upon the product and the country in which it was sold, but generally includes technical support, repair parts and labor associated with warranty repair and service actions. The period ranges from one to three years. The Group revaluates its estimates on an annual basis to assess the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary.

### 2.27 Revenue recognition

The Group principally derives revenue from sales of products and provision of internet services.

Revenue is measured at the fair value of the consideration received or receivable, and represents amounts receivable for goods sold or services performed, stated net of discounts, returns and value-added taxes. The Group recognizes revenue when the specific criteria have been met for each of the Group's activities, as described below.

**(a) Sales of products**

Revenue from the sales of products (mainly including smartphones, IoT and lifestyle products) directly to customers, is recognized when control of the goods has transferred, being when the products are accepted by the customers. The customers have full discretion over the products, and there is no unfulfilled obligation that could affect the customers' acceptance of the products.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.27 Revenue recognition (continued)

**(a) Sales of products (continued)**

Customers in mainland China have an unconditional right to return the products purchased online within 7 days. The Group bases its estimates of sales return on historical results, taking into consideration the type of customers, the type of transactions and the specifics of each arrangement.

**(b) Internet services**

Internet services mainly comprise advertising services and internet value-added services.

***(i) Advertising services***

Advertising revenues comprise mainly display-based and performance-based advertisements.

Revenue from display-based advertisements to the users of smartphones and other devices is recognized on a straight-line basis over the contracted period with customers in which the advertisements are displayed.

Revenue from performance-based advertisements is recognized based on actual performance measurement. The Group recognizes the revenue from the delivery of (i) per-click when the users click on the content, (ii) per-impression when the advertising contents are displayed to users, or (iii) per-download when the third parties' apps are downloaded by users.

***(ii) Internet value-added services***

The Group recognizes the internet value-added services revenue (including online game) on a gross or net basis depending on whether the Group is acting as a principal or an agent in the transaction. The Group also defers the related revenue, over the estimated user relationship periods, given there is an explicit or implicit obligation of the Group to maintain the relevant applications and allow users to have access to them.

## 2 Summary of significant accounting policies (continued)

### 2.27 Revenue recognition (continued)

Determining whether revenue of the Group should be reported gross or net is based on a continuing assessment of various factors. When determining whether the Group is acting as the principal or agent in offering goods or services to the customer, the Group needs to first identify who controls the specified goods or services before they are transferred to the customer. The Group is a principal if the Group obtains control through any of the following: (i) a good or another asset from the other party that the Group then transfers to the customer; (ii) a right to a service to be performed by the other party, which gives the Group the ability to direct that party to provide the service to the customer on the Group's behalf; (iii) a good or service from the other party that the Group then combines with other goods or services in providing the specified good or service to the customer. If control is unclear, when the Group is primarily obligated in a transaction, is subject to inventory risk, has latitude in establishing prices and selecting suppliers, or has several but not all of these indicators, the Group records revenues on a gross basis. Otherwise, the Group records the net amount earned as commissions from products sold or services provided.

The Group does not expect to have any contracts where the period between the transfer of the promised goods or services to the customer and payment by the customer exceeds one year. As a consequence, the Group does not adjust any of the transaction prices for the time value of money.

### 2.28 Interest income

Interest income from financial assets at FVPL is included in investment income as part of other income.

Interest income on financial assets at amortized cost calculated using the effective interest method is recognized in the statement of profit or loss as part of other income.

Interest income is presented as finance income where it is earned from financial assets that are held for cash management purposes.

Interest income is calculated by applying the effective interest rate to the gross carrying amount of a financial asset except for financial assets that subsequently become credit-impaired. For credit-impaired financial assets the effective interest rate is applied to the net carrying amount of the financial asset (after deduction of the loss allowance).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.29 Earnings per share

(i) **Basic earnings per share**

Basic earnings per share is calculated by dividing:

- the profit attributable to owners of the Company, excluding any costs of servicing equity other than ordinary shares.

by the weighted average number of ordinary shares outstanding during the financial year, adjusted for bonus elements in ordinary shares issued during the year and excluding treasury shares.

(ii) **Diluted earnings per share**

Diluted earnings per share adjusts the figures used in the determination of basic earnings per share to take into account:

- the after income tax effect of interest and other financing costs associated with dilutive potential ordinary shares, and

- the weighted average number of additional ordinary shares that would have been outstanding assuming the conversion of all dilutive potential ordinary shares.

### 2.30 Dividend income

Dividends are received from financial assets measured at FVPL and at FVOCI. Dividends are recognized as other income in profit or loss when the right to receive payment is established. This applies even if they are paid out of pre-acquisition profits, unless the dividend clearly represents a recovery of part of the cost of an investment. In this case, the dividend is recognized in OCI if it relates to an investment measured at FVOCI. However, the investment may need to be tested for impairment as a consequence.

### 2.31 Government grants

Grants from government are recognized at their fair value where there is a reasonable assurance that the grants will be received and the Group will comply with all attached conditions.

Government grants relating to costs are deferred and recognized in the consolidated income statement over the period necessary to match them with the costs that they are intended to compensate. Government grants relating to the property and equipment, and other non-current assets are included in the liabilities and are credited to consolidated income statement on a straight-line basis over the expected lives of the related assets.

## 2 Summary of significant accounting policies (continued)

### 2.32 Operating leases

Leases of plant and equipment and office where the Group, as lessee, has substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalized at the lease's inception at the fair value of the leased property or, if lower, the present value of the minimum lease payments. The corresponding rental obligations, net of finance charges, are included in other short-term and long-term payables. Each lease payment is allocated between the repayment of lease liability and finance cost. The finance cost is charged to the profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The property and equipment acquired under finance leases is depreciated over the asset's useful life or over the shorter of the asset's useful life and the lease term if there is no reasonable certainty that the Group will obtain ownership at the end of the lease term.

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the consolidated income statement on a straight-line basis over the period of the lease.

## 3 Financial risk management

### 3.1 Financial risk factors

The Group's activities expose it to a variety of financial risks: market risk (including foreign exchange risk, interest rate risk and price risk), credit risk and liquidity risk. The Group's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Group's financial performance. Risk management is carried out by the senior management of the Group.

(a) Market risk

*(i) Foreign exchange risk*

The transactions of the Company are denominated and settled in its functional currency, US$. The Group's subsidiaries operate in mainland China and overseas, and they are exposed to foreign exchange risk arising from various currency exposures, primarily with respect to US$ and RMB. Therefore, foreign exchange risk primarily arose from recognized assets and liabilities in the Group's subsidiaries in mainland China when receiving or to receive foreign currencies from, or paying or to pay foreign currencies to overseas business partners, and recognized assets and liabilities in the Group's overseas subsidiaries when receiving or to receive foreign currencies from, or paying or to pay foreign currencies to business partners in mainland China.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

#### (a) Market risk (continued)

*(i) Foreign exchange risk (continued)*

For the Group's subsidiaries whose functional currency is RMB, if RMB had strengthened/weakened by 5% against US$ with all other variables held constant, the profit before income tax for the year ended December 31, 2018 would have been approximately RMB148,939,000 higher/lower (2017: RMB124,351,000 lower/higher), as a result of net foreign exchange gains (2017: net foreign exchange losses) on translation of net monetary liabilities (2017: net monetary assets) denominated in US$.

For the Company and the Group's subsidiaries whose functional currency is US$, if RMB had strengthened/weakened by 5% against US$ with all other variables held constant, the profit before income tax for the year ended December 31, 2018 would have been approximately RMB213,622,000 (2017: RMB40,187,000) lower/higher, as a result of net foreign exchange losses on translation of net monetary liabilities denominated in RMB.

*(ii) Interest rate risk*

The Group's interest rate risk primarily arose from borrowings with floating and fixed rates (details of which has been disclosed in Note 33), short-term investments measured at amortized cost, loan receivables, short-term bank deposits and cash and cash equivalents. Those carried at floating rates expose the Group to cash flow interest rate risk whereas those carried at fixed rates expose the Group to fair value interest rate risk.

If the interest rate of borrowings with floating rate had been 50 basis points higher/lower, the profit before income tax for the year ended December 31, 2018 would have been approximately RMB17,158,000 (2017: RMB16,336,000) lower/higher. This analysis does not include the effect of interest capitalized.

If the interest rate of cash and cash equivalents had been 50 basis points higher/lower, the profit before income tax for the year ended December 31, 2018 would have been RMB151,151,000 (2017: RMB57,816,000) higher/lower.

The Group regularly monitors its interest rate risk to ensure there is no undue exposure to significant interest rate movements.

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

#### (a) Market risk (continued)

*(iii) Price risk*

The Group is exposed to price risk in respect of the long-term investments and short-term investments measured at fair value through profit or loss held by the Group. The Group is not exposed to commodity price risk. To manage its price risk arising from the investments, the Group diversifies its portfolio. Each investment is managed by senior management on a case by case basis. The sensitivity analysis is performed by management, see Note 3.3 for detail.

#### (b) Credit risk

The Group is exposed to credit risk in relation to its cash and cash equivalents, short-term bank deposits, restricted cash, short-term investments, loan receivables, trade receivables, other receivables, and financial guarantee contracts. The carrying amounts of each class of the above financial assets represent the Group's maximum exposure to credit risk in relation to financial assets.

To manage risk arising from cash and cash equivalents, short-term bank deposits, restricted cash, short-term investments, the Group only transacts with state-owned or reputable financial institutions in mainland China and reputable international financial institutions outside of mainland China. There has been no recent history of default in relation to these financial institutions.

To manage risk arising from trade receivables, the Group has policies in place to ensure that credit terms are made to counterparties with an appropriate credit history and the management performs ongoing credit evaluations of its counterparties. The credit period granted to the customers is usually no more than 180 days and the credit quality of these customers is assessed, which takes into account their financial position, past experience and other factors. In view of the sound collection history of receivables due from them, management believes that the credit risk inherent in the Group's outstanding trade receivable balances due from them is not significant.

For other receivables, management makes periodic collective assessments as well as individual assessment on the recoverability of other receivables based on historical settlement records and past experiences. In view of the history of cooperation with debtors and the sound collection history of receivables due from them, management believes that the credit risk inherent in the Group's outstanding other receivable balances due from them is not significant.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

#### (b) Credit risk (continued)

For the financial guarantee contracts, the Group has taken measures to manage credit risk, including credit examination, fraud examination and risk monitoring alert. The maximum credit risk from financial guarantee contracts is RMB4,391,098,000 as of December 31, 2018 (2017: RMB2,175,086,000), the majority of which are not credit-impaired on initial recognition and no significant increase in credit risk subsequently (as explained in Note 3.1(b)). The Group has recognized loss allowance for such losses at each of the reporting date.

To manage risk arising from loan receivables, the Group performs standardized credit management procedures. For pre-approval investigation, the Group uses its platform and systems using big data technology to optimize the review process, including credit analysis, assessment of collectability of borrowers, possibility of misconduct and fraudulent activities. In terms of credit examining management, the Group has established specific policies and procedures to assess loans offering. For subsequent monitoring, the Group has implemented credit examination on each borrower every three months. For unqualified borrowers, credit facilities granted previously could be terminated immediately. Once the loan was issued, all borrowers would be assessed by fraud examination model to prevent fraudulent behaviors. In post-loan supervision, the Group has established risk monitoring alert system through periodical monitoring, system alert, and corresponding solutions to identify impaired loans. The estimation of credit exposure for risk management purposes is complex and requires the use of models, as the exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties. The Group measures credit risk using Probability of Default ("**PD**"), Exposure at Default ("**EAD**") and Loss Given Default ("**LGD**"). This is similar to the approach used for the purposes of measuring Expected Credit Loss ("**ECL**") under IFRS 9.

*(b1) Expected credit loss model for loan receivables, as summarized below:*

- The loan receivables that are not credit-impaired on initial recognition are classified in 'Stage 1' and have their credit risk continuously monitored by the Group. The expected credit loss is measured on a 12-month basis.

- If a significant increase in credit risk (as defined below) since initial recognition is identified, the financial instrument is moved to 'Stage 2' but is not yet deemed to be credit-impaired. The expected credit loss is measured on lifetime basis.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

#### (b) Credit risk (continued)

***(b1) Expected credit loss model for loan receivables, as summarized below (continued):***

- If the financial instrument is credit-impaired (as defined below), the financial instrument is then moved to 'Stage 3'. The expected credit loss is measured on lifetime basis.

- In Stages 1 and 2, interest income is calculated on the gross carrying amount (without deducting the loss allowance). If a financial asset subsequently becomes credit-impaired (Stage 3), the Group is required to calculate the interest income by applying the effective interest method in subsequent reporting periods to the amortized cost of the financial asset (the gross carrying amount net of loss allowance) rather than the gross carrying amount.

The impairment of loan receivables was provided based on the 'three-stages' model by referring to the changes in credit quality since initial recognition.

The key judgments and assumptions adopted by the Group in addressing the requirements of the standard are discussed below:

(1) Significant increase in credit risk (SICR)

The Group considers loan receivables to have experienced a significant increase in credit risk when backstop criteria has been met. A backstop is applied and the loan receivables considered to have experienced a significant increase in credit risk if the borrower is more than 1 day past due on its contractual payments.

(2) Definition of default and credit-impaired assets

The Group defines a financial instrument as in default, when the borrower is more than 90 days past due on its contractual payments. This has been applied to all loan receivables held by the Group.

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

#### (b) Credit risk (continued)

*(b1) Expected credit loss model for loan receivables, as summarized below (continued):*

(3) Measuring ECL — Explanation of inputs, assumptions and estimation techniques

The expected credit loss is measured on either a 12-month ("**12M**") or Lifetime basis depending on whether a significant increase in credit risk has occurred since initial recognition or whether an asset is considered to be credit-impaired. Expected credit losses are the discounted product of the PD, EAD and LGD.

The ECL is determined by projecting the PD, LGD and EAD for each future month and for each portfolio. These three components are multiplied together and adjusted for the likelihood of survival (i.e. the exposure has not prepaid or defaulted in an earlier month). This effectively calculates an ECL for each future month, which is then discounted back to the reporting date and summarized. The discount rate used in the ECL calculation is the original effective interest rate or an approximation thereof.

(4) Forward-looking information incorporated in the ECL models

The calculation of ECL incorporate forward-looking information. The Group has performed historical analysis and identified the per capita disposable income of urban residents as the key economic variables impacting credit risk and expected credit losses.

As with any economic forecasts, the projections and likelihoods of occurrence are subject to a high degree of inherent uncertainty and therefore the actual outcomes may be significantly different to those projected. The Group considers these forecasts to represent its best estimate of the possible outcomes and has analyzed the non-linearities and asymmetries within the Group's different portfolios to establish that the chosen scenarios are appropriately representative of the range of possible scenarios.

(5) Grouping of instruments for losses measured on a collective basis

For expected credit loss provisions modeled on a collective basis, a grouping of exposures is performed on the basis of shared risk characteristics, such that risk exposures within a group are homogeneous.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Expressed in RMB unless otherwise indicated)

# 3 Financial risk management (continued)

## 3.1 Financial risk factors (continued)

### (b) Credit risk (continued)

#### *(b2) Loss allowance*

The loss allowance recognized in the year is impacted by a variety of factors, as described below:

- Transfers between Stage 1 and Stages 2 or 3 due to loan receivables experiencing significant increases (or decreases) of credit risk in the year, and the subsequent "step up" (or "**step down**") between 12-month and Lifetime ECL;
- Additional allowances for new financial instruments recognized, as well as releases for loan receivables derecognized in the year;
- Loan receivables derecognized and write-offs of allowances related to assets that were written off during the year.

The following tables explain the changes in the loss allowance for loan receivables between the beginning and the end of the year due to these factors:

| | Stage 1 RMB'000 | Stage 2 RMB'000 | Stage 3 RMB'000 | Total RMB'000 |
|---|---|---|---|---|
| **Loss allowance as of January 1, 2018** | 122,584 | 50,757 | 100,327 | 273,668 |
| *Transfers:* | | | | |
| Transfer from Stage 1 to Stage 2 | (74) | 2,630 | — | 2,556 |
| Transfer from Stage 1 to Stage 3 | (2,502) | — | 168,584 | 166,082 |
| Transfer from Stage 2 to Stage 1 | — | (13) | — | (13) |
| Transfer from Stage 2 to Stage 3 | — | (38,453) | 84,121 | 45,668 |
| Transfer from Stage 3 to Stage 1 | — | — | (9) | (9) |
| Transfer from Stage 3 to Stage 2 | — | 1 | (2) | (1) |
| Change in PDs/LGDs/EADs | (17) | 4 | 2,711 | 2,698 |
| Loan receivables derecognized during the year | (108,910) | (15,333) | (25,239) | (149,482) |
| New loan receivables originated | 90,540 | 89,678 | 316,746 | 496,964 |
| Write-offs | — | — | (136,266) | (136,266) |
| **Loss allowance as of December 31, 2018** | 101,621 | 89,271 | 510,973 | 701,865 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

**(b) Credit risk (continued)**

***(b2) Loss allowance (continued)***

| | Stage 1<br>RMB'000 | Stage 2<br>RMB'000 | Stage 3<br>RMB'000 | Total<br>RMB'000 |
|---|---|---|---|---|
| **Loss allowance as of January 1, 2017** | 10,592 | 746 | 3,860 | 15,198 |
| *Transfers:* | | | | |
| Transfer from Stage 1 to Stage 2 | (5) | 278 | — | 273 |
| Transfer from Stage 1 to Stage 3 | (229) | — | 20,859 | 20,630 |
| Transfer from Stage 2 to Stage 3 | — | (390) | 11,616 | 11,226 |
| Change in PDs/LGDs/EADs | — | — | 3,407 | 3,407 |
| Loan receivables derecognized during the year | (15,247) | (357) | (512) | (16,116) |
| New loan receivables originated | 127,473 | 50,480 | 61,097 | 239,050 |
| **Loss allowance as of December 31, 2017** | 122,584 | 50,757 | 100,327 | 273,668 |

Significant changes in the gross carrying amount of loan receivables that contributed to changes in the loss allowance were as follows:

The high volume of new loan receivables originated during the year ended December 31, 2018, aligned with the Group's organic growth objective, increased the gross carrying amount of the loan receivables by 128% (2017: 519%) with a corresponding RMB90,540,000 (2017: RMB127,473,000) increase in loss allowance measured on a 12-month basis.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

# 3 Financial risk management (continued)

## 3.1 Financial risk factors (continued)

### (b) Credit risk (continued)

*(b2) Loss allowance (continued)*

The gross carrying amount of the loan receivables explains their significance to the changes in the loss allowance as discussed above:

| | Stage 1 RMB'000 | Stage 2 RMB'000 | Stage 3 RMB'000 | Total RMB'000 |
|---|---|---|---|---|
| **Gross carrying amount as of January 1, 2018** | 8,172,340 | 133,327 | 112,494 | 8,418,161 |
| *Transfers:* | | | | |
| Transfer from Stage 1 to Stage 2 | (5,381) | 5,381 | — | — |
| Transfer from Stage 1 to Stage 3 | (183,244) | — | 183,244 | — |
| Transfer from Stage 2 to Stage 1 | 25 | (25) | — | — |
| Transfer from Stage 2 to Stage 3 | — | (91,436) | 91,436 | — |
| Transfer from Stage 3 to Stage 1 | 10 | — | (10) | — |
| Transfer from Stage 3 to Stage 2 | — | 3 | (3) | — |
| Loan receivables derecognized during the year other than write-offs | (7,976,884) | (41,810) | (28,232) | (8,046,926) |
| New loan receivables originated | 10,220,612 | 202,200 | 353,886 | 10,776,698 |
| Write-offs | — | — | (152,423) | (152,423) |
| **Gross carrying amount as of December 31, 2018** | 10,227,478 | 207,640 | 560,392 | 10,995,510 |
| **Gross carrying amount as of January 1, 2017** | 1,579,666 | 24,885 | 8,710 | 1,613,261 |
| *Transfers:* | | | | |
| Transfer from Stage 1 to Stage 2 | (554) | 554 | — | — |
| Transfer from Stage 1 to Stage 3 | (23,332) | — | 23,332 | — |
| Transfer from Stage 2 to Stage 3 | — | (12,993) | 12,993 | — |
| Loan receivables derecognized during the year other than write-offs | (1,555,780) | (11,891) | (1,155) | (1,568,826) |
| New loan receivables originated | 8,172,340 | 132,772 | 68,614 | 8,373,726 |
| **Gross carrying amount as of December 31, 2017** | 8,172,340 | 133,327 | 112,494 | 8,418,161 |

There is no originated credit-impaired loan receivables of the Group during the year.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

#### (b) Credit risk (continued)

##### *(b3) Write-off policy*

The Group writes off loan receivables, in whole or in part, when it has exhausted all practical recovery efforts and has concluded there is no reasonable expectation of recovery. Indicators that there is no reasonable expectation of recovery include ceasing enforcement activity.

The Group may write-off loan receivables that are still subject to enforcement activity. The outstanding contractual amounts of loan receivables written off during the year ended December 31, 2018 was RMB152,423,000 (2017: Nil). The Group still seeks to recover amounts it is legally owed in full, but which have been written off due to no reasonable expectation of full recovery.

##### *(b4) Modification*

The Group rarely modifies the terms of loans provided to customers due to commercial renegotiations, or for distressed loans, with a view to maximizing recovery. The Group considers the impact from such modification is not significant.

#### (c) Liquidity risk

The Group aims to maintain sufficient cash and cash equivalents. Due to the dynamic nature of the underlying business, the policy of the Group is to regularly monitor the Group's liquidity risk and to maintain adequate cash and cash equivalents or adjust financing arrangements to meet the Group's liquidity requirements. There are loan covenants terms for certain borrowings. As of December 31, 2018, there is no non-compliance with such loan covenants (2017: Nil).

The table below analyzes the Group's non-derivative financial liabilities and off-balance sheet guarantee liabilities into relevant maturity grouping based on the remaining year at each balance sheet date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

#### (c) Liquidity risk (continued)

| | Less than 1 year RMB'000 | Between 1 year and 2 years RMB'000 | Between 2 years and 5 years RMB'000 | Over 5 years RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|
| Group | | | | | |
| At December 31, 2018 | | | | | |
| Borrowings | 3,075,194 | 6,145,202 | 450,308 | 1,260,633 | 10,931,337 |
| Trade payables | 46,287,271 | — | — | — | 46,287,271 |
| Other payables | 5,312,834 | 206,488 | 201,689 | 217,965 | 5,938,976 |
| Investment from fund investors | — | — | — | 2,823,504 | 2,823,504 |
| Off-balance sheet guarantee liabilities | 4,325,961 | — | — | — | 4,325,961 |
| At December 31, 2017 | | | | | |
| Borrowings | 3,550,801 | 2,820,105 | 3,717,184 | 714,023 | 10,802,113 |
| Trade payables | 34,003,331 | — | — | — | 34,003,331 |
| Other payables | 3,568,286 | 206,935 | 216,496 | 143,953 | 4,135,670 |
| Off-balance sheet guarantee liabilities | 2,152,169 | — | — | — | 2,152,169 |

Details of the description of Preferred Shares are presented in Note 35.

### 3.2 Capital management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to enhance shareholders' value in the long-term.

The Group monitors capital (including share capital, share premium and Preferred Shares on an as-if-converted basis) by regularly reviewing the capital structure. As a part of this review, the Group considers the cost of capital and the risks associated with the issued share capital. The Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or repurchase the Company's shares. In the opinion of the directors of the Company, the Group has operating profits and a low level of indebtedness. As a result, capital risk is not significant for the Group and measurement of capital management is not a tool currently used in the internal management reporting procedures of the Group.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.3 Fair value estimation

The table below analyzes the Group's financial instruments carried at fair value as of each balance sheet date, by level of the inputs to valuation techniques used to measure fair value. Such inputs are categorized into three levels within a fair value hierarchy as follows:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1);
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2); and
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (level 3).

The following table presents the Group's assets that are measured at fair value at December 31, 2018:

| | Level 1 RMB'000 | Level 2 RMB'000 | Level 3 RMB'000 | Total RMB'000 |
|---|---|---|---|---|
| **Assets** | | | | |
| Long-term investments measured at fair value through profit or loss (Note 19) | 5,215,898 | — | 13,420,310 | 18,636,208 |
| Short-term investments measured at fair value through profit or loss (Note 19) | — | — | 6,648,526 | 6,648,526 |
| | 5,215,898 | — | 20,068,836 | 25,284,734 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.3 Fair value estimation (continued)

The following table presents the Group's assets and liabilities that are measured at fair value at December 31, 2017:

| | Level 1 RMB'000 | Level 2 RMB'000 | Level 3 RMB'000 | Total RMB'000 |
|---|---|---|---|---|
| **Assets** | | | | |
| Long-term investments measured at fair value through profit or loss (Note 19) | 5,764,532 | — | 13,092,429 | 18,856,961 |
| Short-term investments measured at fair value through profit or loss (Note 19) | — | — | 4,488,076 | 4,488,076 |
| | 5,764,532 | — | 17,580,505 | 23,345,037 |
| **Liabilities** | | | | |
| Convertible redeemable preferred shares (Note 35) | — | — | 161,451,203 | 161,451,203 |

(a) **Financial instruments in level 1**

The fair value of financial instruments traded in active markets is based on quoted market prices at each of the reporting dates. A market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service, or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. The quoted market price used for financial assets held by the Group is the current bid price. These instruments are included in level 1.

(b) **Financial instruments in level 2**

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. These valuation techniques maximize the use of observable market data where it is available and rely as little as possible on entity specific estimates. If all significant inputs required to fair value of an instrument are observable, the instrument is included in level 2.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.3 Fair value estimation (continued)

**(c) Financial instruments in level 3**

If one or more of the significant inputs is not based on observable market data, the instrument is included in level 3.

Specific valuation techniques used to value financial instruments include:

- Quoted market prices or dealer quotes for similar instruments;
- Discounted cash flow model and unobservable inputs mainly including assumptions of expected future cash flows and discount rate; and
- A combination of observable and unobservable inputs, including risk-free rate, expected volatility, discount rate for lack of marketability, market multiples, etc.

Level 3 instruments of the Group's assets and liabilities include long-term investments measured at fair value through profit or loss, short-term investments measured at fair value through profit or loss and convertible redeemable preferred shares.

The changes in level 3 instruments of Preferred Shares for the years ended December 31, 2018 and 2017 are presented in the Note 35.

# 3 Financial risk management (continued)

## 3.3 Fair value estimation (continued)

### (c) Financial instruments in level 3 (continued)

The following table presents the changes in level 3 instruments of long-term investments measured at fair value through profit or loss for the years ended December 31, 2018 and 2017:

| | Year ended December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| At the beginning of the year | 13,092,429 | 9,046,509 |
| Addition | 1,727,614 | 858,150 |
| Disposal | (146,908) | (428,468) |
| Changes in fair value | 6,566,513 | 4,136,955 |
| Transfer to long-term investments accounted for using the equity method | (6,523,539) | — |
| Transfer to level 1 financial instruments | (1,467,599) | — |
| Currency translation differences | 171,800 | (520,717) |
| At the end of the year | 13,420,310 | 13,092,429 |
| Net unrealized gains for the year | 4,047,551 | 3,945,459 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.3 Fair value estimation (continued)

#### (c) Financial instruments in level 3 (continued)

The following table presents the changes in level 3 instruments of short-term investments measured at fair value through profit or loss for the years ended December 31, 2018 and 2017:

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| At the beginning of the year | 4,488,076 | 3,437,537 |
| Addition | 140,955,400 | 104,284,000 |
| Disposal | (139,154,171) | (103,417,239) |
| Changes in fair value | 359,221 | 183,778 |
| At the end of the year | 6,648,526 | 4,488,076 |
| Net unrealized gains for the year | 23,526 | 21,076 |

The Group has a team that manages the valuation of level 3 instruments for financial reporting purposes. The team manages the valuation exercise of the investments on a case by case basis. At least once every year, the team would use valuation techniques to determine the fair value of the Group's level 3 instruments. External valuation experts will be involved when necessary.

The valuation of the level 3 instruments mainly included Preferred Shares (Note 35), long-term investments measured at fair value through profit or loss in unlisted companies (Note 19) and short-term investments measured at fair value through profit or loss (Note 19). As these instruments are not traded in an active market, their fair values have been determined by using various applicable valuation techniques, including discounted cash flows and market approach etc. Major assumptions used in the valuation for Preferred Shares are presented in Note 35.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.3 Fair value estimation (continued)

#### (c) Financial instruments in level 3 (continued)

The following table summarizes the quantitative information about the significant unobservable inputs used in recurring level 3 fair value measurements.

| Description | Fair values | | Significant unobservable inputs | Range of inputs | | Relationship of unobservable inputs to fair values |
|---|---|---|---|---|---|---|
| | As of December 31, | | | As of December 31, | | |
| | 2018 | 2017 | | 2018 | 2017 | |
| | RMB'000 | RMB'000 | | | | |
| Investments in unlisted companies measured at fair value through profit or loss | 13,420,310 | 13,092,429 | Expected volatility | 32%–62% | 26%–63% | The higher the expected volatility, the lower the fair value |
| | | | Discount for lack of marketability ("DLOM") | 5%–25% | 2%–25% | The higher the DLOM, the lower the fair value |
| | | | Risk-free rate | 2%–4% | 0%–4% | The higher the risk-free rate, the higher the fair value |
| Short-term investments measured at fair value through profit or loss | 6,648,526 | 4,488,076 | Expected rate of return | 2%–5% | 2%–5% | The higher the expected rate of return, the higher the fair value |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.3 Fair value estimation (continued)

#### (c) Financial instruments in level 3 (continued)

If the fair values of the long-term investments and short-term investments measured at fair value through profit or loss held by the Group had been 10% higher/lower, the profit before income tax for the year ended December 31, 2018 would have been approximately RMB2,528,473,000 (2017: RMB2,334,504,000) higher/lower.

Fair value of Preferred Shares is affected by changes in the Company's equity value. If the Company's equity value had increased/decreased by 10% with all other variables held constant, the profit before income tax for the year ended December 31, 2017 would have been approximately RMB16,145,120,000 lower/higher. There would be no impact for the year ended December 31, 2018 as the Preferred Shares had been transferred out of level 3 of fair value hierarchy classifications due to the conversion to Class B ordinary shares as the result of the initial public offering of the investments.

There were no material transfers between level 1, 2 and 3 of fair value hierarchy classifications during the year ended December 31, 2018, except that certain financial assets and liabilities were transferred out of level 3 of fair value hierarchy classifications.

The carrying amounts of the Group's financial assets including cash and cash equivalents, restricted cash, short-term bank deposits, short-term investments measured at amortized cost, trade receivables, loan receivables and other receivables, and the Group's financial liabilities, including borrowing, trade payables, investment from fund investors and other payables, approximate their fair values.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Expressed in RMB unless otherwise indicated)

## 4 Critical accounting estimates and judgments

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are addressed below.

### (a) Fair value of financial assets

Fair value of financial assets, in the absence of an active market, is estimated by using appropriate valuation techniques. Such valuations were based on certain assumptions about credit risk, volatility and liquidity risks associated with the instruments, which are subject to uncertainty and might materially differ from the actual results. Further details are included in Note 3.3.

### (b) Impairment of loan receivables

The Group follows the guidance of IFRS 9 to determine when a loan receivable is impaired. This determination requires significant judgment and estimation. In making this judgment and estimation, the Group evaluates, among other factors, the duration of receivables and the financial health collection history of individual debtors and expected future change of credit risks, including the consideration of factors such as general economy measure, changes in macroeconomic indicators etc. Further details are included in Note 3.1 to the consolidated financial statements.

### (c) Fair value of Preferred Shares

The Preferred Shares issued by the Company are not traded in an active market and the respective fair value is determined by using valuation techniques. The Group has used the discounted cash flow method to determine the underlying equity value of the Company and adopted equity allocation model to determine the fair value of the Preferred Shares. Key assumptions, such as discount rate, risk-free interest rate, lack of marketability discount and volatility are disclosed in Note 35.

All Preferred Shares had been converted into Class B ordinary shares upon the IPO on July 9, 2018 (Note 35).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 4 Critical accounting estimates and judgments (continued)

### (d) Current and deferred income taxes

The Group is subject to income taxes in different jurisdictions. Significant judgment is required in determining the worldwide provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain. The Group recognizes liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current and deferred income tax assets and liabilities in the period in which such determination is made.

For temporary differences which give rise to deferred tax assets, the Group assesses the likelihood that the deferred income tax assets could be recovered. Deferred tax assets are recognized based on the Group's estimates and assumptions that they will be recovered from taxable income arising from continuing operations in the foreseeable future.

### (e) Inventory provision

Inventories are stated at the lower of cost and net realizable value. Management makes provision for inventories based on historical experience and estimation of future market condition and sales. Management will adjust the provision where actual net realizable value is higher or lower than previously estimated. This requires significant judgment and estimation.

### (f) Recoverability of non-financial assets and investments accounted for using the equity method

The recoverable amount of non-financial assets and investments accounted for using the equity method is the greater of its fair value less costs of disposal and value-in-use. In assessing value-in-use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset, which requires significant judgment relating to level of revenue and amount of operating costs.

The Group uses all readily available information in determining an amount that is a reasonable estimation of the recoverable amount, including estimates based on reasonable and supportable assumptions and projections of revenue and operating costs. Changes in these estimates could have a significant impact on the carrying value of the assets and could result in further impairment charge or reversal of impairment in future periods. Additional information for the impairment assessment of investments accounted for using the equity method is disclosed in Note 12(b).

## 4 Critical accounting estimates and judgments (continued)

### (g) Warranty provision

Warranty provision is based on the estimated cost of product warranties when revenue is recognized. Factors that affect the Group's warranty liability include the number of products sold under warranty, historical and anticipated rates of warranty claims on those products, and cost per claim to satisfy the warranty obligation. The estimation basis is reviewed on an on-going basis and revised where appropriate.

### (h) Revenue

Application of various accounting principles related to the measurement and recognition of revenue requires the Group to make judgments and estimates. Specifically, significant judgments include determining whether the Group is acting as the principal in a transaction. The Group is a principal in a transaction if the Group obtains control of the products sold or services provided before they are transferred to customers. If control is unclear, when the Group is primarily obligated in a transaction, is subject to inventory risk, has latitude in establishing prices and selecting suppliers, or has several but not all of these indicators, the Group records revenues on a gross basis. Otherwise, the Group records the net amount earned as commissions from products sold or services provided.

## 5 Segment information

The Group's business activities, for which discrete financial statements are available, are regularly reviewed and evaluated by the CODM. The CODM, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Chief Executive Officer that makes strategic decisions. As a result of this evaluation, the Group determined that it has operating segments as follows:

- Smartphones
- IoT and lifestyle products
- Internet services
- Others

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 5 Segment information (continued)

The CODM assesses the performance of the operating segments mainly based on segment revenue and gross profit of each operating segment. The selling and marketing expenses, administrative expenses and research and development expenses are not included in the measure of the segments' performance which is used by CODM as a basis for the purpose of resource allocation and assessment of segment performance. Fair value changes on investments measured at fair value through profit or loss, share of losses of investments accounted for using the equity method, other income, other gains-net, finance income-net, fair value changes of convertible redeemable preferred shares, and income tax expense are also not allocated to individual operating segments.

The revenues from external customers reported to CODM are measured as segment revenue, which is the revenue derived from the customers in each segment. Revenues from smartphones segment are derived from the sale of smartphones. Revenues from the IoT and lifestyle products segment primarily comprise revenues from sales of (i) the Group's other in-house products, including smart TVs, laptops, AI speakers and smart routers, and (ii) the Group's ecosystem products, including certain IoT and other smart hardware products, as well as certain lifestyle products. Revenues from internet services segment are derived from advertising services and internet value-added services. Others segment primarily comprises revenue from the Group's hardware repair services for products.

The Group's cost of sales for smartphones segment and IoT and lifestyle products segment primarily consist of (i) procurement cost of raw materials and components for the Group's in-house products, (ii) assembly cost charged by the Group's outsourcing partners for the Group's in-house products, (iii) royalty fees for certain technologies embedded in the Group's in-house products, (iv) costs, in the forms of production costs and profit-sharing, paid to the Group's partners for procuring ecosystem products, (v) warranty expenses, and (vi) provision for impairment of inventories. The Group's cost of sales for internet services segment primarily consist of (i) content fees to game developers, and (ii) bandwidth, server custody and cloud service related costs. Cost of sales for others segment primarily consists of hardware repair costs. Other information, together with the segment information, provided to the CODM, is measured in a manner consistent with that applied in the consolidated financial statements. There were no separate segment assets and segment liabilities information provided to the CODM, as CODM does not use this information to allocate resources or to evaluate the performance of the operating segments.

There were no material inter-segment sales during the years ended December 31, 2018 and 2017. The revenues from external customers reported to the CODM are measured in a manner consistent with that applied in the consolidated income statement.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 5 Segment information (continued)

The segment results for the years ended December 31, 2018 and 2017 are as follows:

| | Year ended December 31, 2018 | | | | |
|---|---|---|---|---|---|
| | Smartphones RMB'000 | IoT and lifestyle products RMB'000 | Internet services RMB'000 | Others RMB'000 | Total RMB'000 |
| Segment revenues | 113,800,386 | 43,816,885 | 15,955,558 | 1,342,596 | 174,915,425 |
| Cost of sales | (106,757,127) | (39,306,134) | (5,683,856) | (976,369) | (152,723,486) |
| Gross profit | 7,043,259 | 4,510,751 | 10,271,702 | 366,227 | 22,191,939 |

| | Year ended December 31, 2017 | | | | |
|---|---|---|---|---|---|
| | Smartphones RMB'000 | IoT and lifestyle products RMB'000 | Internet services RMB'000 | Others RMB'000 | Total RMB'000 |
| Segment revenues | 80,563,594 | 23,447,823 | 9,896,389 | 716,936 | 114,624,742 |
| Cost of sales | (73,462,255) | (21,496,958) | (3,935,638) | (575,686) | (99,470,537) |
| Gross profit | 7,101,339 | 1,950,865 | 5,960,751 | 141,250 | 15,154,205 |

The reconciliation of gross profit to profit/(loss) before income tax is shown in the consolidated income statement.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 5 Segment information (continued)

The Company is domiciled in the Cayman Islands while the Group mainly operates its businesses in mainland China. For the years ended December 31, 2018 and 2017, the geographical information on the total revenues is as follows:

| | Year ended December 31, | | | |
|---|---|---|---|---|
| | 2018 | | 2017 | |
| | RMB'000 | % | RMB'000 | % |
| Mainland China | 104,944,803 | 60.0 | 82,543,462 | 72.0 |
| Rest of the world (Note (a)) | 69,970,622 | 40.0 | 32,081,280 | 28.0 |
| | 174,915,425 | | 114,624,742 | |

Note:

(a) Revenues outside mainland China are mainly from India, Indonesia and Western Europe.

The major customers which contributed more than 10% of the total revenue of the Group for the years ended December 31, 2018 and 2017 are listed as below:

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | % | % |
| Customer A | 10.9 | 13.5 |

All the revenues derived from other single external customer were less than 10% of the Group's total revenues during the year.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 6 Revenue

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Smartphones | 113,800,386 | 80,563,594 |
| IoT and lifestyle products | 43,816,885 | 23,447,823 |
| Internet services | 15,955,558 | 9,896,389 |
| Others | 1,342,596 | 716,936 |
| | 174,915,425 | 114,624,742 |

## 7 Other income

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Government grants | 274,584 | 121,151 |
| Value-added tax and other tax refunds | 82,507 | 3,738 |
| Dividend income | 131,804 | 106,291 |
| Investment income from short-term investments measured at fair value through profit or loss | 335,695 | 162,702 |
| Interest income from short-term investments measured at amortized cost | 20,199 | 54,789 |
| | 844,789 | 448,671 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 8 Other gains, net

| | Year ended December 31, | |
|---|---|---|
| | 2018<br>RMB'000 | 2017<br>RMB'000 |
| Remeasurement of investments transferring from financial assets measured at fair value through profit or loss to investments accounted for using the equity method (Note 12(b)) | 126,614 | — |
| Net gains on disposals of long-term investments measured at fair value through profit or loss | 28,176 | 192,008 |
| Gains on disposal of an investment accounted for using the equity method | — | 91,429 |
| Foreign exchanges losses, net | (14,550) | (144,265) |
| Others | 73,041 | (67,132) |
| | 213,281 | 72,040 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 9 Expenses by nature

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Cost of inventories sold | 138,237,733 | 89,468,462 |
| Provision for impairment of inventories (Note 23) | 3,006,525 | 652,560 |
| Royalty fees | 4,263,421 | 3,447,479 |
| Employee benefit expenses (Note 10) | 17,114,892 | 4,050,084 |
| Depreciation of property and equipment (Note 16) | 219,523 | 166,515 |
| Amortization of intangible assets (Note 17) | 528,693 | 194,441 |
| Promotion and advertising expenses | 2,486,350 | 1,921,590 |
| Content fees to game developers and video providers | 1,629,144 | 1,383,626 |
| Provision for loan receivables | 607,180 | 258,470 |
| Consultancy and professional service fees | 903,076 | 447,612 |
| Cloud service, bandwidth and server custody fees | 1,725,218 | 929,872 |
| Office rental expenses | 529,497 | 314,388 |
| Warranty expenses | 1,068,252 | 1,828,622 |
| Auditor's remuneration | 51,803 | 36,929 |

During the year, the Group incurred expenses for the purpose of research and development of approximately RMB5,776,826,000 (2017: RMB3,151,401,000), which comprised employee benefits expenses of RMB4,043,476,000 (2017: RMB2,239,765,000). No significant development expenses had been capitalized for the years ended December 31, 2018 and 2017.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 10 Employee benefit expense

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Wages, salaries and bonuses | 3,565,209 | 2,428,247 |
| Share-based compensation expenses (Note (a) and Note 28) | 12,380,668 | 909,155 |
| Contributions to pension plans | 481,686 | 300,765 |
| Other social security costs, housing benefits and other employee benefits | 687,329 | 411,917 |
| | 17,114,892 | 4,050,084 |

Note:

(a) Share-based compensation expenses contain the expenses for share-based awards granted to the Group's employees and the expenses for Xiaomi Development Fund ("**Employee Fund**").

### (a) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group include one director during the year ended December 31, 2018 (2017: Nil). The emoluments payable to the five highest paid individuals during the years ended December 31, 2018 and 2017 are as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Wages, salaries and bonuses | 9,398 | 8,148 |
| Share-based compensation expenses | 10,208,783 | 187,572 |
| Contributions to pension plans | 71 | 146 |
| Other social security costs, housing benefits and other employee benefits | 70 | 203 |
| | 10,218,322 | 196,069 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 10 Employee benefit expense (continued)

### (a) Five highest paid individuals (continued)

The emoluments fell within the following bands:

| | Number of individuals Year ended December 31, 2018 | 2017 |
|---|---|---|
| HK$10,000,001 to HK$30,000,000 | — | 2 |
| HK$30,000,001 to HK$100,000,000 | 4 | 2 |
| HK$100,000,001 to HK$150,000,000 | — | 1 |
| HK$150,000,001 to HK$15,000,000,000 | 1 | — |

### (b) Benefits and interests of directors

| Name of Director | Fees HK$'000 | Salary HK$'000 | Discretionary bonuses HK$'000 | Allowances and benefits in kind HK$'000 | Employer's contribution to a retirement benefit scheme HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|
| **Executive Directors** | | | | | | |
| LEI, Jun | — | — | — | — | — | — |
| LIN, Bin | — | — | — | — | — | — |
| **Non-executive Directors** | | | | | | |
| KOH, Tuck Lye | — | — | — | — | — | — |
| LIU, Qin | — | — | — | — | — | — |
| **Independent non-executive Directors** | | | | | | |
| CHEN, Dongsheng | 500 | — | — | — | — | 500 |
| LEE, Ka Kit | 500 | — | — | — | — | 500 |
| WONG, Shun Tak | 500 | — | — | — | — | 500 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 10 Employee benefit expense (continued)

### (b) Benefits and interests of directors (continued)

During the year ended December 31, 2018, certain share based awards were granted to Lei Jun (Note 28). No benefits and interests of directors subsisted as of December 31, 2017 or at any time during the year then ended.

### (c) Directors' termination benefits

No director's termination benefit subsisted as of December 31, 2018 and 2017 or at any time during all the years presented.

### (d) Consideration provided to third parties for making available directors' services

No consideration provided to third parties for making available directors' services subsisted as of December 31, 2018 and 2017 or at any time during all the years presented.

### (e) Information about loans, quasi-loans and other dealings in favor of directors, controlled bodies corporate by and connected entities with such directors

No loans, quasi-loans and other dealings in favor of directors, controlled bodies corporate by and connected entities with such directors subsisted as of December 31, 2018 and 2017 or at any time during all the years presented.

### (f) Directors' material interests in transactions, arrangements or contracts

No significant transactions, arrangements and contracts in relation to the Group's business to which the Company was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted as of December 31, 2018 and 2017 or at any time during all the years presented.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 11 Finance income, net

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| **Finance income:** | | |
| Interest income from bank deposits | 601,065 | 242,518 |

Interest income mainly represents interest income from bank deposits, including bank balance and term deposits.

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| **Finance costs:** | | |
| Interest expense from financial liability measured at amortized cost (Note 29) | 42,504 | — |
| Interest expenses | 415,465 | 258,235 |
| Less: amount capitalized | (73,277) | (42,501) |
| | 384,692 | 215,734 |

Interest and related expenses mainly arise from the borrowings disclosed in Notes 33.

Finance costs have been capitalized on qualifying assets at average interest rates of 5.35% per annum for the year ended December 31, 2018 (2017: 5.39%).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12(a) Major subsidiaries and controlled structured entities

As of December 31, 2018 and 2017, the Company had the following major subsidiaries (including controlled structured entities):

| Name | Place of incorporation/ establishment and kind of legal entity | Date of incorporation/ establishment | Particulars of issued/ paid-in capital | Effective interest held: As of December 31, 2018 | Effective interest held: As of December 31, 2017 | Effective interest held: As of the date of this report | Principal activities |
|---|---|---|---|---|---|---|---|
| **Subsidiaries** | | | | | | | |
| **Directly held:** | | | | | | | |
| Xiaomi H.K. Limited | Hong Kong, limited liability company | April 7, 2010 | HK$10,000 | 100% | 100% | 100% | Wholesale and retail of smartphones and ecosystem partners' products |
| Fast Pace Limited | British Virgin Islands, limited liability company | January 8, 2013 | US$2 | 100% | 100% | 100% | Investment holding and investment activities |
| Xiaomi Ventures Limited | British Virgin Islands, limited liability company | March 21, 2013 | US$1 | 100% | 100% | 100% | Investment holding and investment activities |
| Xiaomi Singapore Pte. Ltd. | Singapore, limited liability company | December 23, 2013 | Singapore Dollar ("**SGD**")1 and US$149,000,000 | 100% | 100% | 100% | Sales of smart hardware |
| Xiaomi Finance Inc. | Cayman Islands, limited liability company | February 15, 2018 | US$1 | 100% | NA | 100% | Investment holding and investment activities |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12(a) Major subsidiaries and controlled structured entities (continued)

As of December 31, 2018 and 2017, the Company had the following major subsidiaries (including controlled structured entities) (continued):

| | | | | Effective interest held | | | |
|---|---|---|---|---|---|---|---|
| Name | Place of incorporation/ establishment and kind of legal entity | Date of incorporation/ establishment | Particulars of issued/ paid-in capital | As of December 31, 2018 | 2017 | As of the date of this report | Principal activities |
| **Subsidiaries** | | | | | | | |
| **Indirectly held:** | | | | | | | |
| Xiaomi Communications Co., Ltd. | Mainland China, limited liability company | August 25, 2010 | US$130,000,000 | 100% | 100% | 100% | Sales of smartphones, sales of ecosystem partners' products and provision of customer services |
| Beijing Xiaomi Electronics Co., Ltd. | Mainland China, limited liability company | January 9, 2012 | US$27,000,000 | 100% | 100% | 100% | Sales of smart hardware |
| Taiwan Xiaomi Communications Co., Ltd. | Taiwan, limited liability company | April 25, 2000 | New Taiwan Dollar ("**NTD**") 5,000,000 | 100% | 100% | 100% | Sales of smart hardware |
| Chongqing Xiaomi Microcredit Co., Ltd. | Mainland China, limited liability company | June 12, 2015 | US$450,000,000 | 100% | 100% | 100% | Internet finance and consumer loan services |
| Beijing Xiaomi Mobile Software Co., Ltd. | Mainland China, limited liability company | May 8, 2012 | RMB288,000,000 | 100% | 100% | 100% | Software and hardware development and provision of software related services |
| Zhuhai Xiaomi Communications Co., Ltd. | Mainland China, limited liability company | January 25, 2013 | RMB2,000,000 | 100% | 100% | 100% | Procurement and sales of smartphones, ecosystem partners' products and spare parts, procurement of raw materials |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12(a) Major subsidiaries and controlled structured entities (continued)

As of December 31, 2018 and 2017, the Company had the following major subsidiaries (including controlled structured entities) (continued):

| | | | | Effective interest held | | | |
|---|---|---|---|---|---|---|---|
| | | | | As of December 31, | | | |
| Name | Place of incorporation/ establishment and kind of legal entity | Date of incorporation/ establishment | Particulars of issued/ paid-in capital | 2018 | 2017 | As of the date of this report | Principal activities |
| **Subsidiaries Indirectly held (continued):** | | | | | | | |
| Guangdong Xiaomi Inc. | Mainland China, limited liability company | September 21, 2015 | RMB1,000,000,000 | 100% | 100% | 100% | Provision of software and technology service |
| Guangzhou Xiaomi Communications Co., Ltd. | Mainland China, limited liability company | September 22, 2016 | RMB1,000,000 | 100% | 100% | 100% | Sales of smart hardware |
| Timi Personal Computing Co., Ltd. (Note (d)) | Mainland China, limited liability company | July 28, 2015 | RMB550,000 | 100% | 78% | 100% | Sales of smart hardware |
| Xiaomi Communications and Logistics India Private Limited (Note (e)) | India, limited liability company | April 1, 2015 | Indian Rupees ("**INR**")30,000,000 | 100% | 100% | 100% | Provision of logistics services |
| Xiaomi Technology India Private Limited | India, limited liability company | October 7, 2014 | INR100,000 | 100% | 100% | 100% | Sales of smartphones and ecosystem partners' products |
| Guangzhou Xiaomi Information Service Co., Ltd. | Mainland China, limited liability company | December 29, 2016 | RMB1,000,000 | 100% | 100% | 100% | Provision of advertising and technology services |
| Xiaomi Home Commercial Co., Ltd. | Mainland China, limited liability company | June 27, 2017 | RMB100,000,000 | 100% | 100% | 100% | Operation of retail stores |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12(a) Major subsidiaries and controlled structured entities (continued)

As of December 31, 2018 and 2017, the Company had the following major subsidiaries (including controlled structured entities) (continued):

| | | | | Effective interest held | | | |
|---|---|---|---|---|---|---|---|
| Name | Place of incorporation/ establishment and kind of legal entity | Date of incorporation/ establishment | Particulars of issued/ paid-in capital | As of December 31, 2018 | As of December 31, 2017 | As of the date of this report | Principal activities |
| **Subsidiaries Indirectly held (continued):** | | | | | | | |
| Beijing Xiaomi Digital Technology Co., Ltd. | Mainland China, limited liability company | December 21, 2010 | US$7,900,000 | 100% | 100% | 100% | Research and development of computer software and information technology |
| Red Better Limited | British Virgin Islands, limited liability company | October 8, 2013 | – | 100% | 100% | 100% | Investment activities |
| Green Better Limited | British Virgin Islands, limited liability company | December 9, 2013 | US$1 | 100% | 100% | 100% | Investment activities |
| People Better Limited | British Virgin Islands, limited liability company | April 22, 2014 | – | 100% | 100% | 100% | Investment activities |
| Xiaomi Home Technology Co., Ltd. | Mainland China, limited liability company | January 20, 2017 | RMB80,000,000 | 100% | 100% | 100% | Operation of retail stores |
| Beijing Zilin Real Estate Co., Ltd. | Mainland China, limited liability company | November 29, 2018 | – | 95% | NA | 95% | Property management |
| Xiaomi Commercial Factoring (Tianjin) Co., Ltd. | Mainland China, limited liability company | March 21, 2018 | US$380,000,000 | 100% | NA | 100% | Commercial factoring business |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12(a) Major subsidiaries and controlled structured entities (continued)

As of December 31, 2018 and 2017, the Company had the following major subsidiaries (including controlled structured entities) (continued):

| Name | Place of incorporation/ establishment and kind of legal entity | Date of incorporation/ establishment | Particulars of issued/ paid-in capital | Effective interest held As of December 31, 2018 | Effective interest held As of December 31, 2017 | Effective interest held As of the date of this report | Principal activities |
|---|---|---|---|---|---|---|---|
| **Controlled structured entities (Note (a)):** | | | | | | | |
| Xiaomi Inc. | Mainland China, limited liability company | March 3, 2010 | RMB1,850,000,000 | 100% | 100% | 100% | E-commerce business |
| Tianjin Jinxing Venture Investment Co., Ltd. | Mainland China, limited liability company | December 26, 2013 | RMB1,200,000,000 | 100% | 100% | 100% | Investment activities |
| Sichuan Silver Mi Technology Co., Ltd. | Mainland China, limited liability company | October 26, 2005 | RMB2,000,000,000 | 100% | 100% | 100% | Research and development of computer software and market research |
| Jiefu Ruitong Inc. (Note (b)) | Mainland China, limited liability company | January 11, 2011 | RMB100,000,000 | 100% | 65% | 100% | Provision of electronic payment services |
| Beijing Duokan Technology Co., Ltd. | Mainland China, limited liability company | February 10, 2010 | RMB10,000,000 | 100% | 100% | 100% | Sales of e-book |
| Beijing Wali Internet Technologies Co., Ltd. | Mainland China, limited liability company | June 1, 2009 | RMB2,100,000 | 100% | 100% | 100% | Provision of internet services |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12(a) Major subsidiaries and controlled structured entities (continued)

As of December 31, 2018 and 2017, the Company had the following major subsidiaries (including controlled structured entities) (continued):

| Name | Place of incorporation/ establishment and kind of legal entity | Date of incorporation/ establishment | Particulars of issued/ paid-in capital | Effective interest held: As of December 31, 2018 | Effective interest held: As of December 31, 2017 | Effective interest held: As of the date of this report | Principal activities |
|---|---|---|---|---|---|---|---|
| **Controlled structured entities (Note (a)) (continued):** | | | | | | | |
| Tianjin Gold Mi Investment Partners (Limited Partnership) | Mainland China, limited partnership | July 16, 2014 | RMB1,132,400,000 | 100% | 100% | 100% | Investment activities |
| Hubei Xiaomi Yangtze River Industry Investment Fund Partners (Limited Partnership) (Note (g)) | Mainland China, limited partnership | December 7, 2017 | RMB3,384,000,000 | 18% | 100% | 18% | Investment activities |

Notes:

(a) The Company does not have directly or indirectly legal ownership in equity of these structured entities or their subsidiaries. Nevertheless, under certain Contractual Arrangements entered into with the registered owners of these structured entities, the Company and its other legally owned subsidiaries control these companies by way of controlling the voting rights, governing their financial and operating policies, appointing or removing the majority of the members of their controlling authorities, and casting the majority of votes at meetings of such authorities. Accordingly, the Group has rights to exercise power over these structured entities, receives variable returns from its involvement in these structured entities, and has the ability to affect those returns through its power over these structured entities. As a result, they are presented as structured entities of the Company.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12(a) Major subsidiaries and controlled structured entities (continued)

Notes (continued):

(b) Jiefu Ruitong Inc. was established in mainland China on January 11, 2011 and was subsequently acquired by the Group on June 14, 2016. In July 2018, the Group agreed to pay RMB332,000,000 as consideration in exchange for certain indirect equity interests in Jiefu Ruitong Inc. to acquire the remaining equity interests in this subsidiary.

(c) The Company considered that the non-wholly owned subsidiaries with non-controlling interests are not significant to the Group, therefore, no summarized financial information of these non-wholly owned subsidiaries is presented separately.

(d) In March 2018, the Group issued Class B ordinary shares as consideration in exchange for certain indirect equity interests in Timi Personal Computing Co., Ltd. to acquire the remaining equity interests in this subsidiary.

(e) Xiaomi Communications and Logistics India Private Limited, incorporated in India and owned by Xiaomi Singapore Pte. Ltd. as to 99.9967% and Jain Manu Kumar, who is a director of Xiaomi Technology India Private Limited, as to 0.0033%.

(f) The English names of the subsidiaries are direct translation or transliteration of their Chinese registered names.

(g) Two subsidiaries of the Group together with other limited partners newly launched a RMB fund named Hubei Xiaomi Yangtze River Industry Investment Fund Partners (Limited Partnership) (湖北小米長江產業基金合夥企業(有限合夥)) (the "**Hubei Fund**") in Wuhan, Hubei province in mainland China in 2017. The size of the Hubei Fund is RMB12,000,000,000. During the year ended December 31, 2018, the Hubei Fund raised RMB2,781,000,000 from third party investors, and as a result, the Group's shareholding interest in the Hubei Fund changed from 100% to 18%.

## 12(b) Investments accounted for using the equity method

| | As of December 31, | |
|---|---|---|
| | **2018** | 2017 |
| | **RMB'000** | RMB'000 |
| Investments in associate accounted for using the equity method | | |
| — Listed entities | **6,198,681** | 386,490 |
| — Unlisted entities | **2,440,557** | 1,324,329 |
| | **8,639,238** | 1,710,819 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12(b)Investments accounted for using the equity method (continued)

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| At the beginning of the year | 1,710,819 | 1,852,563 |
| Additions (Note (a), (b), (c), (d), (e)) | 7,289,333 | 156,551 |
| Disposal and transfer | (100) | (42,298) |
| Share of losses | (614,920) | (231,496) |
| Share of other comprehensive income/(loss) | 191,449 | (22,783) |
| Share of changes of other reserves | 62,657 | 33,539 |
| Dividends | — | (35,257) |
| At the end of the year | 8,639,238 | 1,710,819 |

Notes:

(a) In February 2018, Huami Corp. ("**Huami**"), an investment for which was previously accounted as long-term investments measured at fair value through profit or loss underwent initial public offering on the New York Stock Exchange, following which Huami was re-designated as investment accounted for using the equity method due to the conversion of the preference shares into ordinary shares upon its initial public offering.

(b) In February 2018, the Group obtained significant influence over Ourpalm Co., Ltd. ("**Ourpalm**") through board representation, which was previously accounted for as long-term investments measured at fair value through profit or loss. Accordingly, the Group reclassified the investment in associate measured at fair value through profit or loss to an investment accounted for using the equity method.

(c) On March 29, 2018, iQIYI, Inc. ("**iQIYI**"), an investment engaging in the provision of internet video streaming services in mainland China, for which the Group accounted as long-term investments measured at fair value through profit or loss, underwent initial public offering on the NASDAQ Stock Exchange. The conversion of the preference shares in iQIYI owned by the Group into ordinary shares was completed on April 2, 2018, following which the Group reclassified the investment in associate measured at fair value through profit or loss to an investment accounted for using the equity method.

(d) On September 25, 2018, Viomi Technology Co., Ltd. ("**VIOT**"), an investment engaging in the operation of developing and selling IoT-enabled smart home products in the People's Republic of China, for which the Group accounted as long-term investments measured at fair value through profit or loss, underwent initial public offering on the NASDAQ Stock Exchange. The conversion of the preference shares in VIOT owned by the Group into ordinary shares was completed on the same day, following which the Group reclassified the investment in associate measured at fair value through profit or loss to an investment accounted for using the equity method.

(e) In October 2018, the Group acquired newly issued shares of a company which is engaged in sales of mobile devices for a consideration of RMB500,000,000. The investment was previously accounted for by the Group as an associate of the Group accounted for using the equity method with share interest of 21.94%. Following the addition, the Group owned 46.44% interest in the company which remained as an associate of the Group accounted for using the equity method.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12(b) Investments accounted for using the equity method (continued)

Management has assessed the level of influence that the Group exercises on these associates, with a total carrying amount of RMB8,639,238,000 as of December 31, 2018 (2017: RMB1,710,819,000), and determined that it has significant influence through the board representation, even though the respective shareholding of some investments is below 20%. Accordingly, these investments have been classified as associates.

Set out below are the material associates of the Group as of December 31, 2018 and 2017. The associates as listed below are ordinary shares investment, which held directly by the Group. Mainland China is their principal place of business.

| | | | | Quoted fair value | | Carrying amount | |
|---|---|---|---|---|---|---|---|
| | | | | As of December 31, | | As of December 31, | |
| | Place of | % of Ownership | Principal | 2018 | 2017 | 2018 | 2017 |
| Name of entity | incorporation | interest | activities | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| Xunlei Limited ("**Xunlei**") | Cayman Islands | 27.9 | Provision of cloud computing service | **597,770** | 1,883,586 | **304,667** | 386,490 |
| Sichuan Xin Wang Bank Co., Ltd. ("**XW Bank**") | Mainland China | 29.5 | Provision of internet banking service | **NA** | NA | **936,908** | 827,534 |
| iQIYI | Cayman Islands | 6.8 | Provision of internet video streaming services | **4,984,330** | NA | **4,377,472** | NA |

The associates of the Group have been accounted by using the equity method based on the financial information of the associates prepared under the accounting policies consistent with the Group.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12(b) Investments accounted for using the equity method (continued)

Set out below are the summarized financial information of material associates.

| | Xunlei | | XW Bank | | iQIYI |
|---|---|---|---|---|---|
| | As of December 31, | | As of December 31, | | As of December 31, |
| | 2018 | 2017 | 2018 | 2017 | 2018 |
| | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| **Summarized consolidated balance sheets** | | | | | |
| Current assets | 2,490,648 | 2,814,823 | 28,137,561 | 15,074,511 | 19,853,443 |
| Non-current assets | 798,511 | 970,525 | 8,021,166 | 1,241,408 | 35,736,050 |
| Current liabilities | 741,466 | 925,870 | 28,454,306 | 13,003,685 | 19,812,356 |
| Non-current liabilities | 62,933 | 133,121 | 4,528,463 | 507,034 | 9,499,228 |
| Non-controlling interests | (7,659) | (14,114) | — | — | 118,632 |
| Equity attributable to owners of the Company | 2,492,419 | 2,740,471 | 3,175,958 | 2,805,200 | 26,159,277 |
| **Reconciliation to carrying amounts:** | | | | | |
| Group's share of net assets attributable to owners of the associates | 694,637 | 776,460 | 936,908 | 827,534 | 1,768,039 |
| Adjustment | | | | | |
| — Goodwill | 424,233 | 424,233 | — | — | 2,609,433 |
| — Impairment provision | (814,203) | (814,203) | — | — | — |
| Carrying amount | 304,667 | 386,490 | 936,908 | 827,534 | 4,377,472 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12(b) Investments accounted for using the equity method (continued)

| | Xunlei | | XW Bank | | iQIYI |
|---|---|---|---|---|---|
| | Year ended December 31, | | Year ended December 31, | | Year ended December 31, |
| | 2018 | 2017 | 2018 | 2017 | 2018 |
| | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| **Summarized consolidated income statements and consolidated statements of comprehensive income** | | | | | |
| Revenues | **1,529,102** | 1,364,373 | **1,160,403** | 342,366 | **24,989,116** |
| (Loss)/profit from operations | **(399,034)** | (366,252) | **461,099** | (241,967) | **(8,420,635)** |
| (Loss)/profit before tax | **(367,587)** | (313,998) | **460,343** | (226,174) | **(9,096,829)** |
| Net (loss)/profit | **(368,127)** | (255,487) | **371,470** | (169,569) | **(9,175,630)** |
| Other comprehensive (loss)/income | **(11,482)** | (59,220) | **(711)** | 712 | **(1,786,820)** |
| Total comprehensive (loss)/income | **(379,609)** | (314,707) | **370,759** | (168,857) | **(10,962,450)** |

In addition to the interests in associates disclosed above, the Group also has interests in a number of individually immaterial associates that are accounted for using the equity method.

| | As of December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Aggregate carrying amount of individually immaterial associates | **3,020,191** | 496,795 |
| Aggregate amounts of the Group's share of: | | |
| Profit/(loss) from continuing operations | **6,249** | (67,244) |
| Other comprehensive income/(loss) | **19,864** | (6,214) |
| Total comprehensive income/(loss) | **26,113** | (73,458) |

There are no contingent liabilities relating to the Group's interests in the associates.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 13 Income tax expenses

The income tax expenses of the Group during the years ended December 31, 2018 and 2017 are analyzed as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Current income tax | 1,414,602 | 1,644,674 |
| Deferred income tax (Note 34) | (965,225) | 415,089 |
| **Income tax expenses** | 449,377 | 2,059,763 |

The tax on the Group's profit/(loss) before income tax differs from the theoretical amount that would arise using the statutory tax rate of 25% in mainland China, being the tax rate applicable to the majority of consolidated entities as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Profit/(Loss) before income tax | 13,927,124 | (41,829,352) |
| Tax calculated at statutory income tax rate of 25% in mainland China (Note (a)) | 3,481,781 | (10,457,338) |
| Tax effects of: | | |
| — Effect of different tax rates in other jurisdictions (Note (b),(c),(d)) | (2,037,227) | 12,646,524 |
| — Preferential income tax rates applicable to subsidiaries (Note (e)) | (1,017,178) | (393,879) |
| — Tax losses and temporary differences for which no deferred income tax assets was recognized | 115,452 | 199,363 |
| — Expenses not deductible for income tax purposes | 588,839 | 209,721 |
| — Utilization of previously unrecognized deductible tax losses and temporary differences | (89,626) | (5,010) |
| — Super Deduction for research and development expenses (Note (f)) | (166,794) | (127,993) |
| — Income not subject to tax | (157,306) | (26,537) |
| — Tax refund (Note (e)) | (270,757) | — |
| — Others | 2,193 | 14,912 |
| **Income tax expenses** | 449,377 | 2,059,763 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 13 Income tax expenses (continued)

Notes:

(a) Enterprise income tax in mainland China ("**EIT**")

The income tax provision of the Group in respect of its operations in mainland China was calculated at tax rate of 25% on the assessable profits for the periods presented, based on the existing legislation, interpretations and practices in respect thereof.

(b) Cayman Islands and British Virgin Islands income tax

The Company is incorporated in the Cayman Islands as an exempted company with limited liability under the Companies Law of the Cayman Islands and accordingly, is exempted from Cayman Islands income tax. As such, the operating results reported by the Company, including the fair value gain/(loss) of Preferred Shares (Note 35) and the share-based awards (Note 28), are not subject to any income tax.

The Group entities established under the International Business Companies Acts of British Virgin Islands ("**BVI**") are exempt from BVI income taxes.

(c) Hong Kong income tax

Entities incorporated in Hong Kong are subject to Hong Kong profits tax at a rate of 16.5% on the assessable profits for the years presented, based on the existing legislation, interpretations and practices in respect thereof.

(d) India income tax

The income tax provision for India entities were calculated at corporate income tax rates of 30% to 35% on the assessable profits for the years presented, based on the existing legislation, interpretations and practices in respect thereof.

(e) Preferential EIT rate

Certain subsidiaries are entitled to preferential tax rates ranging from 10% to 15%. Main subsidiaries with preferential EIT rates are as follows:

Beijing Xiaomi Mobile Software Co., Ltd. ("**Xiaomi Mobile**") was qualified as a "High and New Technology Enterprise" and enjoyed a preferential income tax rate of 15% for the year ended December 31, 2017. It was qualified as a "Key Software Enterprise" in the third quarter of 2018, hence it enjoys a preferential income tax rate of 10% retroactively from January 1, 2017. Accordingly, Xiaomi Mobile was entitled to tax refund for the income tax paid in 2017 and such tax refund was received by Xiaomi Mobile from local tax bureau in December 2018. Therefore, Xiaomi Mobile is subject to an EIT rate of 10% for the year ended December 31, 2018 (2017: 15%).

(f) Super Deduction for research and development expense

According to the relevant laws and regulations promulgated by the State Council of the People's Republic of China that was effective from 2008 onwards, enterprises engaging in research and development activities were entitled to claim 150% of their research and development expenses so incurred as tax deductible expenses when determining their assessable profits for that year ("**Super Deduction**"). The State Taxation Administration of The People's Republic of China announced in September 2018 that enterprises engaging in research and development activities would entitle to claim 175% of their research and development expenses as Super Deduction from January 1, 2018 to December 31, 2020. The Group has made its best estimate for the Super Deduction to be claimed for the Group's entities in ascertaining their assessable profits during the year.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 13 Income tax expenses (continued)

Notes (continued):

(g) Withholding tax in mainland China ("**WHT**")

According to the New Corporate Income Tax Law ("**New EIT Law**"), distribution of profits earned by companies in mainland China since January 1, 2008 to foreign investors is subject to withholding tax of 5% or 10%, depending on the country of incorporation of the foreign investors, upon the distribution of profits to overseas-incorporated immediate holding companies.

The Group does not have any plan in the foreseeable future to require its subsidiaries in mainland China to distribute their retained earnings and intends to retain them to operate and expand its business in mainland China. Accordingly, no deferred income tax liability related to WHT on undistributed earnings was accrued as of the end of each reporting period.

## 14 Earnings/(loss) per share

On June 17, 2018, pursuant to the shareholders' resolution, each existing issued and unissued share of US$0.000025 each in the share capital of the Company were subdivided into 10 shares of US$0.0000025 each ("**Share Subdivision**"). Following the Share Subdivision, the weighted average number of ordinary shares for the purpose of basic and diluted earnings per share for the years ended December 31, 2018 and 2017 has been retrospectively adjusted.

### (a) Basic

Basic earnings or loss per share for the years ended December 31, 2018 and 2017 are calculated by dividing the profit or loss attributable to the Company's owners by the weighted average number of ordinary shares in issue during the year.

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Net profit/(loss) attributable to the owners of the Company | 13,553,886 | (43,826,016) |
| Weighted average number of ordinary shares in issue (Note (a)) (thousand shares) | 16,069,770 | 9,758,173 |
| Basic earnings/(loss) per share (Note (a)) (expressed in RMB per share) | 0.843 | (4.491) |

Note:

(a) Weighted average number of ordinary shares in issue and basic earnings/(loss) per share were calculated taken into account the effect of the Share Subdivision.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 14 Earnings/(loss) per share (continued)

### (a) Basic (continued)

As of December 31, 2018, 24,000,000 ordinary shares were issued to several employees. However, the shareholders' rights of these shares were restricted and would be vested over certain service periods. Accordingly, these shares were accounted for as restricted stock units (RSUs). The Group did not include these ordinary shares in the calculation of basic earnings/(loss) per share for the years ended December 31, 2018 and 2017 as these shares are not considered outstanding for earnings/(loss) per share calculation purposes.

### (b) Diluted

Diluted earnings or loss per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares.

As the Group incurred losses for the year ended December 31, 2017, the potential ordinary shares were not included in the calculation of dilutive loss per share, as their inclusion would be anti-dilutive. Accordingly, diluted loss per share for the year ended December 31, 2017 is same as basic loss per share.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 14 Earnings/(loss) per share (continued)

### (b) Diluted (continued)

For the year ended December 31, 2018, diluted earnings or loss per share was calculated by considering that the impact of share options of Xiaomi Finance Inc., a wholly owned subsidiary of the Company ("**Xiaomi Finance**") granted to Lei Jun were not dilutive, as Xiaomi Finance was in loss position for the year ended December 31, 2018.

| | Year ended December 31, 2018 RMB'000 | Year ended December 31, 2017 RMB'000 |
|---|---|---|
| Net profit/(loss) attributable to the owners of the Company | 13,553,886 | (43,826,016) |
| Less: Fair value gain of Preferred Shares | (12,514,279) | — |
| Net profit/(loss) used to determine diluted earnings/(loss) per share | 1,039,607 | (43,826,016) |
| Weighted average number of ordinary shares in issue (Note (a)) (thousand shares) | 16,069,770 | 9,758,173 |
| Adjustments for Preferred Shares (Note (a)) (thousand shares) | 5,468,315 | — |
| Adjustments for RSUs and share options granted to employees (Note (a)) (thousand shares) | 2,024,845 | — |
| Weighted average number of ordinary shares for calculation of diluted earnings/(loss) per share (Note (a)) (thousand shares) | 23,562,930 | 9,758,173 |
| Diluted earnings/(loss) per share (Note (a)) (expressed in RMB per share) | 0.044 | (4.491) |

Note:

(a) Weighted average number of ordinary shares in issue, adjustments for Preferred Shares, adjustments for RSUs and share options granted to employees, weighted average number of ordinary shares for calculation of diluted earnings/(loss) per share and diluted earnings/(loss) per share were calculated taken into account the effect of the Share Subdivision.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 15 Land use rights

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Opening net book amount | 3,416,359 | 3,494,041 |
| Additions | 64,832 | — |
| Amortization | (78,223) | (77,682) |
| Closing net book amount | 3,402,968 | 3,416,359 |

The Group had an aggregate amount of approximately RMB3,402,968,000 (2017: RMB3,416,359,000) of land use rights for office buildings being constructing. During the year ended December 31, 2018, the Group newly acquired a land use right in mainland China at a consideration of RMB64,832,000. The estimated useful lives of the land use rights were 40 to 50 years. The new office buildings are under construction during the year (Note 16).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 16 Property and equipment

| | Electronic equipment RMB'000 | Office equipment RMB'000 | Leasehold improvements RMB'000 | Construction in progress RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|
| **At January 1, 2018** | | | | | |
| Cost | 422,515 | 14,317 | 331,083 | 1,473,761 | 2,241,676 |
| Accumulated depreciation | (297,588) | (11,870) | (201,346) | — | (510,804) |
| **Net book amount** | 124,927 | 2,447 | 129,737 | 1,473,761 | 1,730,872 |
| **Year ended December 31, 2018** | | | | | |
| Opening net book amount | 124,927 | 2,447 | 129,737 | 1,473,761 | 1,730,872 |
| Currency translation differences | (330) | (13) | (1,010) | 13 | (1,340) |
| Additions | 242,843 | 19,612 | 243,364 | 3,119,183 | 3,625,002 |
| Disposals/transfer | (17,071) | (1) | — | (49,886) | (66,958) |
| Depreciation charge (Note 9) | (87,245) | (3,740) | (128,538) | — | (219,523) |
| **Closing net book amount** | 263,124 | 18,305 | 243,553 | 4,543,071 | 5,068,053 |
| **At December 31, 2018** | | | | | |
| Cost | 642,723 | 33,932 | 564,076 | 4,543,071 | 5,783,802 |
| Accumulated depreciation | (379,599) | (15,627) | (320,523) | — | (715,749) |
| **Net book amount** | 263,124 | 18,305 | 243,553 | 4,543,071 | 5,068,053 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Expressed in RMB unless otherwise indicated)

## 16 Property and equipment (continued)

| | Electronic equipment RMB'000 | Office equipment RMB'000 | Leasehold improvements RMB'000 | Construction in progress RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|
| **At January 1, 2017** | | | | | |
| Cost | 372,970 | 15,450 | 163,103 | 642,581 | 1,194,104 |
| Accumulated depreciation | (212,314) | (10,401) | (123,012) | — | (345,727) |
| **Net book amount** | 160,656 | 5,049 | 40,091 | 642,581 | 848,377 |
| **Year ended December 31, 2017** | | | | | |
| Opening net book amount | 160,656 | 5,049 | 40,091 | 642,581 | 848,377 |
| Currency translation differences | (23) | (6) | (1) | — | (30) |
| Additions | 50,880 | 17 | 167,981 | 831,180 | 1,050,058 |
| Disposals | (131) | (887) | — | — | (1,018) |
| Depreciation charge (Note 9) | (86,455) | (1,726) | (78,334) | — | (166,515) |
| **Closing net book amount** | 124,927 | 2,447 | 129,737 | 1,473,761 | 1,730,872 |
| **At December 31, 2017** | | | | | |
| Cost | 422,515 | 14,317 | 331,083 | 1,473,761 | 2,241,676 |
| Accumulated depreciation | (297,588) | (11,870) | (201,346) | — | (510,804) |
| **Net book amount** | 124,927 | 2,447 | 129,737 | 1,473,761 | 1,730,872 |

Construction in progress as of December 31, 2018 and 2017 mainly comprises new office buildings being constructed in mainland China.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 16 Property and equipment (continued)

Depreciation expenses have been charged to the consolidated income statement as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Administrative expenses | 61,216 | 56,191 |
| Selling and marketing expenses | 98,941 | 62,763 |
| Research and development expenses | 59,366 | 47,561 |
| | 219,523 | 166,515 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 17 Intangible assets

| | Goodwill (Note (a)) RMB'000 | License RMB'000 | Trademarks, patents and domain name RMB'000 | Others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|
| **At January 1, 2018** | | | | | |
| Cost | 248,167 | 1,343,686 | 1,003,239 | 107,792 | 2,702,884 |
| Accumulated amortization | — | (63,735) | (280,034) | (84,763) | (428,532) |
| **Net book amount** | 248,167 | 1,279,951 | 723,205 | 23,029 | 2,274,352 |
| **Year ended December 31, 2018** | | | | | |
| Opening net book amount | 248,167 | 1,279,951 | 723,205 | 23,029 | 2,274,352 |
| Currency translation differences | — | — | (10,049) | (106) | (10,155) |
| Additions | 33,923 | 71,723 | 110,283 | 116,949 | 332,878 |
| Disposals | — | (7,190) | — | — | (7,190) |
| Amortization charge (Note 9) | — | (332,071) | (155,520) | (41,102) | (528,693) |
| **Closing net book amount** | 282,090 | 1,012,413 | 667,919 | 98,770 | 2,061,192 |
| **At December 31, 2018** | | | | | |
| Cost | 282,090 | 1,408,219 | 1,084,466 | 224,578 | 2,999,353 |
| Accumulated amortization | — | (395,806) | (416,547) | (125,808) | (938,161) |
| **Net book amount** | 282,090 | 1,012,413 | 667,919 | 98,770 | 2,061,192 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 17 Intangible assets (continued)

| | Goodwill (Note (a)) RMB'000 | License RMB'000 | Trademarks, patents and domain name RMB'000 | Others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|
| **At January 1, 2017** | | | | | |
| Cost | 248,167 | 375,940 | 643,389 | 88,034 | 1,355,530 |
| Accumulated amortization | — | (4,361) | (168,575) | (62,461) | (235,397) |
| **Net book amount** | 248,167 | 371,579 | 474,814 | 25,573 | 1,120,133 |
| **Year ended December 31, 2017** | | | | | |
| Opening net book amount | 248,167 | 371,579 | 474,814 | 25,573 | 1,120,133 |
| Currency translation differences | — | — | (14,942) | (1) | (14,943) |
| Additions | — | 967,746 | 376,098 | 19,759 | 1,363,603 |
| Amortization charge (Note 9) | — | (59,374) | (112,765) | (22,302) | (194,441) |
| **Closing net book amount** | 248,167 | 1,279,951 | 723,205 | 23,029 | 2,274,352 |
| **At December 31, 2017** | | | | | |
| Cost | 248,167 | 1,343,686 | 1,003,239 | 107,792 | 2,702,884 |
| Accumulated amortization | — | (63,735) | (280,034) | (84,763) | (428,532) |
| **Net book amount** | 248,167 | 1,279,951 | 723,205 | 23,029 | 2,274,352 |

Note:

(a) For the purpose of impairment tests of goodwill, goodwill is allocated to groups of cash-generating units. Such groups of cash-generating units represent the lowest level within the Group for which the goodwill is monitored for internal management purpose.

Impairment review on the goodwill of the Group has been conducted by the management as of December 31, 2018 and 2017 according to IAS 36 "Impairment of assets". For the purposes of impairment review, the recoverable amount of goodwill is determined based on value-in-use calculations by using the discounted cash flow method. Management forecasted the average annual revenue growth rate in five-year period is 5%, and the cash flows beyond the five-year period were extrapolated using the estimated annual growth rates of 2%. Pre-tax discount rate of 20% was used to reflect market assessment of time value and the specific risks relating to the CGUs.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 17 Intangible assets (continued)

Note (continued):

Based on the result of the goodwill impairment testing, the estimated recoverable amount was approximately RMB2,162,337,000 as of December 31, 2018 (2017: RMB1,501,601,000). As the recoverable amount was significantly above the carrying amount, no impairment was identified in respect of the goodwill as of December 31, 2018 and 2017.

The Group has performed a sensitivity analysis on key assumptions used in management's annual impairment test of goodwill. Had the estimated revenue growth rate during the forecast period been 1% percentage lower, the recoverable amount would be decreased to RMB2,011,412,000 as of December 31, 2018 (2017: RMB1,368,728,000). Reasonably possible changes in key assumptions would not lead to impairment as of December 31, 2018 and 2017.

Amortization charges were expensed off in the following categories in the consolidated income statement:

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Administrative expenses | 77,468 | 105,162 |
| Selling and marketing expenses | 648 | 668 |
| Research and development expenses | 450,577 | 88,611 |
| | 528,693 | 194,441 |

The Group tests annually whether goodwill and other intangible assets with an indefinite useful life have suffered any impairment. During the years ended December 31, 2018 and 2017, no goodwill or other identifiable intangible assets have been impaired.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Expressed in RMB unless otherwise indicated)

## 18 Financial instruments by category

| | As of December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| **Assets as per balance sheet** | | |
| Financial assets measured at fair value through profit or loss: | | |
| — Long-term investments measured at fair value through profit or loss (Note 19) | 18,636,208 | 18,856,961 |
| — Short-term investments measured at fair value through profit or loss (Note 19) | 6,648,526 | 4,488,076 |
| Financial assets measured at amortized costs: | | |
| — Trade receivables (Note 21) | 5,598,443 | 5,469,507 |
| — Loan receivables (Note 20) | 10,293,645 | 8,144,493 |
| — Other receivables | 12,408,170 | 7,506,631 |
| — Short-term investments measured at amortized cost (Note 19) | — | 800,000 |
| — Short-term bank deposits (Note 24(c)) | 1,365,991 | 225,146 |
| — Restricted cash (Note 24(b)) | 1,480,178 | 2,711,119 |
| — Cash and cash equivalents (Note 24(a)) | 30,230,147 | 11,563,282 |
| | 86,661,308 | 59,765,215 |
| **Liabilities as per balance sheet** | | |
| Financial liabilities measured at amortized cost: | | |
| — Trade payables (Note 30) | 46,287,271 | 34,003,331 |
| — Other payables (excluding staff payroll and welfare payables, government grants and other taxes payables) | 4,805,101 | 3,076,153 |
| — Borrowings (Note 33) | 10,931,337 | 10,802,113 |
| — Investment from fund investors (Note 29) | 2,823,504 | — |
| Financial liabilities measured at fair value through profit or loss: | | |
| — Convertible redeemable preferred shares (Note 35) | — | 161,451,203 |
| | 64,847,213 | 209,332,800 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 19 Investments

| | As of December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| **Current assets** | | |
| Short-term investments measured at | | |
| — Amortized cost | — | 800,000 |
| — Fair value through profit or loss (i) | 6,648,526 | 4,488,076 |
| | 6,648,526 | 5,288,076 |
| **Non-current assets** | | |
| Long-term investments measured at fair value through profit or loss | | |
| — Equity investments (ii) | 7,629,929 | 7,448,251 |
| — Preferred shares investments (iii) | 11,006,279 | 11,408,710 |
| | 18,636,208 | 18,856,961 |

### (i) Short-term investments measured at fair value through profit or loss

The short-term investments measured at fair value through profit or loss are wealth management products, denominated in RMB, with expected rates of return ranging from 2.20% to 5.15% per annum for the years ended December 31, 2018 (2017: 2.00% to 5.10%). The returns on all of these wealth management products are not guaranteed, hence their contractual cash flows do not qualify for solely payments of principal and interest. Therefore they are measured at fair value through profit or loss. None of these investments are past due.

The fair values are based on cash flow discounted using the expected return based on management judgment and are within level 3 of the fair value hierarchy.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 19 Investments (continued)

### (ii) Equity investments

| | As of December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| Listed | **5,215,898** | 5,764,532 |
| Unlisted | **2,414,031** | 1,683,719 |
| | **7,629,929** | 7,448,251 |

The fair values of the listed securities are determined based on the closing prices quoted in active markets. They are accounted for using their fair values based on quoted market prices (level 1: quoted price (unadjusted) in active markets) without any deduction for transaction costs. And as of December 31, 2018, the Group has not elected to recognize the fair value gains or losses on equity investments in OCI.

The fair values of unlisted securities are measured using a valuation technique with unobservable inputs and hence classified as Level 3 of the fair value hierarchy. The major assumptions used in the valuation for investment in private companies refer to Note 3.3.

### (iii) Preferred shares investments

During the year ended December 31, 2018, the Group made aggregate preferred shares investments of RMB1,102,118,000 (2017: RMB369,975,000). These investees are principally engaged in sales of goods and provision of internet services.

All of these investments are convertible redeemable preferred shares or ordinary shares with preferential rights. The Group has the right to require and demand the investees to redeem all of the shares held by the Group at guaranteed predetermined fixed amount upon redemption events which are out of control of issuers. Hence, these investments are accounted for as debt instruments and are measured at financial assets at fair value through profit or loss.

The conversion of the preference shares in Huami, iQIYI and VIOT owned by the Group into ordinary shares was completed on February 8, 2018, April 2, 2018 and September 25, 2018, respectively, following which the Group reclassifies the associates to the investments accounted for using the equity method (Note 12(b)).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 19 Investments (continued)

### (iv) Amounts recognized in profit or loss

| | Year ended December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| Fair value changes on equity investments | (1,386,967) | 2,569,974 |
| Fair value changes on preferred shares investments | 5,793,800 | 3,780,048 |
| Fair value changes on short-term investments measured at fair value through profit or loss | 23,526 | 21,076 |
| | 4,430,359 | 6,371,098 |

## 20 Loan receivables

| | As of December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| Unsecured loan | 10,995,510 | 8,418,161 |
| Less: allowance for impairment | (701,865) | (273,668) |
| | 10,293,645 | 8,144,493 |

Loan receivables are loans derived from subsidiaries of the Group which engages in the internet finance business. Such amounts are recorded at the principal amount less allowance for doubtful accounts. The loan periods granted by the Group to the individuals generally range from 3 months to 12 months. Loan receivables are mainly denominated in RMB.

Detail of the credit risk assessment of loan receivables is disclosed in Note 3.1.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 21 Trade receivables

Trade receivables analysis is as follows:

| | As of December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Third parties | 5,302,432 | 5,337,711 |
| Related parties | 364,608 | 188,616 |
| | 5,667,040 | 5,526,327 |
| Less: allowance for impairment | (68,597) | (56,820) |
| | 5,598,443 | 5,469,507 |

The carrying amounts of the Group's trade receivables are denominated in the following currencies:

| | As of December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| RMB | 3,285,845 | 2,787,885 |
| INR | 1,464,621 | 2,389,901 |
| US$ | 795,971 | 264,912 |
| Others | 52,006 | 26,809 |
| | 5,598,443 | 5,469,507 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 21 Trade receivables (continued)

Movements on the Group's allowance for impairment of trade receivables are as follows:

| | Year ended December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| At the beginning of the year | **(56,820)** | (40,048) |
| Provision for doubtful receivables | **(19,451)** | (24,467) |
| Reversal of provision for previous impaired receivables | **7,674** | 7,502 |
| Receivables written off during the year as uncollectable | **—** | 193 |
| At the end of the year | **(68,597)** | (56,820) |

(a) The Group generally allows a credit period within 180 days to its customers. Aging analysis of trade receivables based on invoice date is as follows:

| | As of December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| **Trade receivables** | | |
| Up to 3 months | **5,094,390** | 5,099,590 |
| 3 to 6 months | **392,868** | 302,354 |
| 6 months to 1 year | **116,279** | 39,028 |
| 1 to 2 years | **16,630** | 53,613 |
| Over 2 years | **46,873** | 31,742 |
| | **5,667,040** | 5,526,327 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 21 Trade receivables (continued)

(b) The Group applies the simplified approach to providing for expected credit losses prescribed by IFRS 9, which permits the use of the lifetime expected loss provision for all trade receivables. To measure the expected credit losses, trade receivables have been grouped based on shared credit risk characteristics and the days past due. The expected credit losses below also incorporate forward looking information. The loss allowance provisions as of December 31, 2018 and 2017 are determined as follows:

| | Current | Up to 3 months past due | 3 to 6 months past due | Over 6 months past due | Total |
|---|---|---|---|---|---|
| **December 31, 2018:** | | | | | |
| Expected loss rate | 0.01% | 0.99% | 34.22% | 52.85% | |
| Gross carrying amount (in thousand) | 4,992,793 | 532,901 | 64,006 | 77,340 | 5,667,040 |
| Loss allowance provision (in thousand) | 562 | 5,261 | 21,902 | 40,872 | 68,597 |
| **December 31, 2017:** | | | | | |
| Expected loss rate | 0.01% | 0.96% | 37.27% | 41.59% | |
| Gross carrying amount (in thousand) | 4,951,616 | 444,031 | 50,435 | 80,245 | 5,526,327 |
| Loss allowance provision (in thousand) | 383 | 4,270 | 18,797 | 33,370 | 56,820 |

As of December 31, 2018 and 2017, the majority of the balance of receivables are due from certain channel distributors and customers in mainland China and India who usually settle the amounts due by them within 180 days.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 22 Prepayments and other receivables

| | As of December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Receivables from subcontractors for outsourcing of raw materials and amounts paid for third parties | 10,043,378 | 5,663,419 |
| Recoverable value-added tax and other taxes | 7,811,161 | 3,387,401 |
| Prepayments to suppliers | 467,418 | 304,286 |
| Deposits to suppliers | 569,598 | 96,913 |
| Receivables from market development fund | 822,809 | 199,751 |
| Prepaid fees for establishing loan facilities and other prepaid expenses | 228,197 | 195,592 |
| Receivables from import and export agents | 52,263 | 644,766 |
| Receivables from employees related to Employee Fund (Note (a)) | 110,950 | 114,850 |
| Interest receivables | 231,819 | 104,521 |
| Receivables from disposal of investments | 35,226 | 108,056 |
| Loans to related parties (Note (b)) | 7,979 | 62,143 |
| Others | 534,148 | 512,212 |
| | 20,914,946 | 11,393,910 |

Notes:

(a) Receivables from employees related to Employee Fund is interest bearing and repayable when the employee resign from the Group. Further detail included in Note 28.

(b) Loans to related parties were unsecured, repayable on demand and carried interest rate at ceiling of 8% per annum (2017: 8%).

As of December 31, 2018 and 2017, the carrying amounts of other receivables were primarily denominated in RMB and US$ and approximated their fair value at each of the reporting dates. Other receivables that are measured at amortized costs included receivables from subcontractors for outsourcing of raw materials and amounts paid for third parties, receivables from import and export agents, receivables from market development fund, receivables from employees related to Employee Fund, receivables from disposal of investments, interest receivables, loans to related parties and others were considered to be of low credit risk, and thus the impairment provision recognized during the year ended December 31, 2018 and 2017 was limited to 12 months expected losses.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 23 Inventories

| | As of December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Raw materials | 7,343,118 | 5,117,285 |
| Finished goods | 19,112,105 | 8,461,798 |
| Work in progress | 2,068,834 | 1,352,886 |
| Spare parts | 1,156,825 | 1,569,040 |
| Others | 1,651,854 | 510,061 |
| | 31,332,736 | 17,011,070 |
| Less: provision for impairment (Note (a)) | (1,852,051) | (668,142) |
| | 29,480,685 | 16,342,928 |

Note:

(a) Provision for impairment was recognized for the amount by which the carrying amount of the inventories exceeds its net realizable value, and was recorded in "cost of sales" in the consolidated income statement. The provision for impairment expense of inventory amounted to RMB3,006,525,000 for the year ended December 31, 2018 (2017: RMB652,560,000).

Provision for impairment movements for the years ended December 31, 2018 and 2017 are as below:

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| At the beginning of the year | (668,142) | (283,159) |
| Provision for impairment | (3,006,525) | (652,560) |
| Transfer to cost of sales upon sold | 1,822,616 | 267,577 |
| At the end of the year | (1,852,051) | (668,142) |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 24 Cash and bank balances

### (a) Cash and cash equivalents

| | As of December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Cash at bank and in hand | 10,958,910 | 7,598,660 |
| Short-term bank deposits with initial terms within three months | 19,271,237 | 3,964,622 |
| | 30,230,147 | 11,563,282 |

Cash and cash equivalents are denominated in the following currencies:

| | As of December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| US$ | 22,189,594 | 3,625,567 |
| RMB | 7,192,491 | 5,372,675 |
| INR | 532,838 | 2,384,434 |
| Others | 315,224 | 180,606 |
| | 30,230,147 | 11,563,282 |

The weighted average effective interest rate for the short-term bank deposits with initial terms within three months was 3.24% per annum for the year ended December 31, 2018 (2017: 2.78%).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 24 Cash and bank balances (continued)

### (b) Restricted cash

As of December 31, 2018, among of the restricted cash, RMB1,083,723,000 was held at bank to meet requirements of People's Bank of China for reserves of payment institutions. US$20,000,000 (equivalent to approximately RMB137,264,000) was held at the Agricultural Bank of China as guarantee for purchase contract with Samsung.

### (c) Short-term bank deposits

An analysis of the Group's short-term bank deposits as of December 31, 2018 and 2017 are listed as below:

| | As of December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Short-term bank deposits denominated in RMB | 460,000 | 20,000 |
| Short-term bank deposits denominated in INR | 49 | 205,146 |
| Short-term bank deposits denominated in US$ | 905,942 | — |
| | 1,365,991 | 225,146 |

Short-term bank deposits are bank deposits with original maturities over three months and redeemable on maturity.

The effective interest rate of the short-term bank deposits of the Group ranges from 2.25% to 6.00% per annum for the year ended December 31, 2018 (2017: from 2.25% to 7.45%).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 25 Share capital

Authorized:

| | Note | Number of ordinary shares '000 | Nominal value of ordinary shares US$'000 | Number of Preferred Shares '000 | Nominal value of Preferred Shares US$'000 |
|---|---|---|---|---|---|
| **As of January 1, 2017** | | 3,489,594 | 87 | 1,050,755 | 26 |
| Issuance of Series F1 Preferred Shares | | — | — | 496 | — |
| **As of December 31, 2017** | | 3,489,594 | 87 | 1,051,251 | 26 |
| Effect of Share Subdivision | (a) | 31,406,344 | — | 9,461,254 | — |
| Conversion of Preferred Shares to ordinary shares | (b) | 10,512,505 | 26 | (10,512,505) | (26) |
| Increase of authorized ordinary shares | (c) | 224,591,557 | 561 | — | — |
| **As of December 31, 2018** | | **270,000,000** | **674** | **—** | **—** |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 25 Share capital (continued)

Issued:

| | Note | Number of ordinary shares '000 | Nominal value of ordinary shares US$'000 | Equivalent nominal value of ordinary shares RMB'000 | Share premium RMB'000 |
|---|---|---|---|---|---|
| **As of January 1, 2017 and December 31, 2017** | | 978,217 | 24 | 150 | 742,760 |
| Acquisition of additional equity interests in non-wholly owned subsidiaries | (d) | 1,500 | — | — | 230,899 |
| Issuance of ordinary shares | (e) | 63,960 | 2 | 11 | 9,827,146 |
| Effect of Share Subdivision | (a) | 9,393,092 | — | — | — |
| Issuance of ordinary shares relating to initial public offering, net of underwriting commissions and other issuance costs | (f) | 1,635,926 | 4 | 27 | 23,248,593 |
| Conversion of Preferred Shares to ordinary shares | (b) | 10,504,922 | 26 | 174 | 151,100,334 |
| Release of ordinary shares from Share Scheme Trusts | (g) | — | 2 | 15 | 933,592 |
| Issuance of ordinary shares to Share Scheme Trusts | (g) | 1,048,806 | — | — | — |
| Share premium set off the accumulated losses and other reserves | (h) | — | — | — | (142,232,042) |
| **As of December 31, 2018** | | **23,626,423** | **58** | **377** | **43,851,282** |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 25 Share capital (continued)

Notes:

(a) On June 17, 2018, pursuant to the shareholders' resolution, each existing issued and unissued share of US$0.000025 each in the share capital of the Company were subdivided into 10 shares of US$0.0000025 each.

(b) Upon completion of the IPO, each issued Preferred Share converted into one Class B ordinary share by re-designation and reclassification of every Preferred Share in issue as an Class B ordinary share on a one for one basis and all the unissued and authorized Preferred Shares were re-designated and reclassified as Class B ordinary shares. As a result, the financial liabilities for Preferred Shares were derecognized and recorded as share capital and share premium.

(c) Upon completion of the re-designation and reclassification noted in (b), the authorized share capital of the Company increased 63,116,143,000 Class A ordinary shares of nominal value of US$0.0000025 each and 161,475,414,000 Class B ordinary shares of nominal value of US$0.0000025 each.

(d) Pursuant to the shareholders' resolution passed on March 30, 2018, 1,500,000 Class B ordinary shares (or 15,000,000 Class B ordinary shares following the Share Subdivision) were issued as consideration shares in exchange for certain indirect equity interests in subsidiary Timi Personal Computing Co., Ltd (Note 12(a)).

(e) On April 2, 2018, the Company issued 63,959,619 Class B ordinary shares (or 639,596,190 Class B ordinary shares following the Share Subdivision) at par value to Smart Mobile Holdings Limited, an entity whose interest is held on trust for the benefit of Lei Jun and his family members, to reward Lei Jun for his contribution to the Company. Accordingly, RMB9,827,157,000 was recognized as share-based compensation expenses on April 2, 2018 by the Group.

(f) Upon completion of the IPO, the Company issued 1,635,926,000 new shares at par value of US$0.0000025 each for cash consideration of HK$17.00 each, and raised gross proceeds of approximately HK$27,810,742,000 (equivalent to RMB23,525,107,000). The respective share capital amount was approximately RMB27,000 and share premium arising from the issuance was approximately RMB23,248,593,000, net of the share issuance costs. The share issuance costs paid and payable mainly include share underwriting commissions, lawyers' fees, reporting accountant's fee and other related costs, which are incremental costs directly attributable to the issuance of the new shares. These costs amounting to RMB276,487,000 were treated as a deduction against the share premium arising from the issuance.

(g) During the year ended December 31, 2018, the Company issued ordinary shares with respect to the share options under the share option scheme exercised by certain grantees of the Company before December 31, 2018 to trusts, which were established to hold the shares for and on behalf of the grantees (collectively, "**Share Scheme Trusts**").

(h) On December 27, 2018, the Board of Directors passed a resolution that the sum of approximately of RMB142,232,042,000 standing to the credit of the share premium account of the Company was applied to set off the accumulated losses and other reserves of the Company. The accumulated losses of RMB136,652,570,000 was set off and the related currency translation difference of RMB5,579,472,000 was released.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 26 Other reserves

| | Share-based compensation reserve RMB'000 | Currency translation differences RMB'000 | Statutory surplus reserve RMB'000 | Capital reserve RMB'000 | Others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|
| At January 1, 2018 | 3,816,153 | (3,779,938) | 805,180 | 33,501 | 72,524 | 947,420 |
| Appropriation to statutory reserves (Note (a)) | — | — | 57,808 | — | — | 57,808 |
| Employees share-based compensation scheme: | | | | | | |
| — value of employee services (Note (c) and Note 28) | 2,358,720 | — | — | — | — | 2,358,720 |
| Share of other comprehensive income of investments accounted for using the equity method (Note 12(b)) | — | — | — | — | 191,449 | 191,449 |
| Share of other reserves of investments accounted for using the equity method (Note 12(b)) | — | — | — | 62,657 | — | 62,657 |
| Acquisition of additional equity interests in non-wholly owned subsidiaries | — | — | — | (152,071) | — | (152,071) |
| Currency translation differences (Note (b)) | — | (1,756,092) | — | — | — | (1,756,092) |
| Share premium set off the accumulated losses and other reserves (Note 25(h)) | — | 5,579,472 | — | — | — | 5,579,472 |
| Release of ordinary shares from Share Scheme Trusts (Note 25(g)) | (841,640) | — | — | — | — | (841,640) |
| Others | — | — | (308) | — | — | (308) |
| At December 31, 2018 | 5,333,233 | 43,442 | 862,680 | (55,913) | 263,973 | 6,447,415 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 26 Other reserves (continued)

| | Share-based compensation reserve RMB'000 | Currency translation differences RMB'000 | Statutory surplus reserve RMB'000 | Capital reserve RMB'000 | Others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|
| **At January 1, 2017** | 3,008,259 | (11,706,613) | 478,730 | (38) | 95,307 | (8,124,355) |
| Appropriation to statutory reserves (Note (a)) | — | — | 326,450 | — | — | 326,450 |
| Employees share-based compensation scheme: | | | | | | |
| — value of employee services (Note (c) and Note 28) | 807,894 | — | — | — | — | 807,894 |
| Share of other comprehensive loss of investments accounted for using the equity method (Note 12(b)) | — | — | — | — | (22,783) | (22,783) |
| Share of other reserves of investments accounted for using the equity method (Note 12(b)) | — | — | — | 33,539 | — | 33,539 |
| Currency translation differences (Note (b)) | — | 7,926,675 | — | — | — | 7,926,675 |
| **At December 31, 2017** | 3,816,153 | (3,779,938) | 805,180 | 33,501 | 72,524 | 947,420 |

Notes:

(a) In accordance with the Company Law of the People's Republic of China and the stipulated provisions of the articles of association of subsidiaries with limited liabilities in mainland China, appropriation of net profits (after offsetting accumulated losses from prior years) should be made by these companies to their respective statutory surplus reserve funds and discretionary reserve funds before distributions are made to the owners. The percentage of appropriation to statutory surplus reserve fund is 10%. The amount to be transferred to discretionary reserve fund is determined by the equity owners of these companies. When the balance of the statutory surplus reserve fund reaches 50% of the registered capital, such transfer needs not to be made. Both statutory surplus reserve fund and discretionary reserves fund can be capitalized as capital of an enterprise, provided that the remaining statutory surplus reserve fund shall not be less than 25% of the registered capital.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 26 Other reserves (continued)

Notes (continued):

In addition, in accordance with the Law of the People's Republic of China on Enterprises with Foreign Investments and the stipulated provisions of the articles of association of wholly owned foreign subsidiaries in mainland China, appropriation from net profits (after offsetting accumulated losses brought forward from prior years) should be made by these companies to their respective reserve fund. The percentage of net profit to be appropriated to the reserve fund is not less than 10% of the net profit. When the balance of the reserve fund reaches 50% of the registered capital, such transfer needs not be made. With approvals obtained from respective boards of directors of these companies, the Reserve Fund can be used to offset accumulated deficit or to increase capital.

(b) Foreign currency translation reserve represents the difference arising from the translation of the financial statements of companies within the Group that have a functional currency different from the presentation currency of RMB for the financial statements of the Company and the Group.

A majority of the currency translation differences are arising from the Company when it translates the financial statements from the functional currency of US$ to presentation currency of RMB.

(c) Share-based compensation reserve arises from share-based payments granted to employees of the Group, see Note 28 for detail.

## 27 Dividends

No dividends have been paid or declared by the Company during the years ended December 31, 2018 and 2017.

## 28 Share-based payments

On May 5, 2011, the Board of Directors of the Company approved the establishment of the "Xiaomi Corporation 2011 Employee Stock Option Plan" ("**2011 Plan**") with the purpose of attracting, motivating, retaining and rewarding certain employees and directors. The 2011 Plan is valid and effective for 10 years from the approval of the Board of Directors. The maximum number of shares that may be issued under 2011 Plan shall be 35,905,172 Class B ordinary shares (which were adjusted to 1,436,206,880 shares after the 1 to 4 share split on March 14, 2014 and further 1 to 10 Share Subdivision on June 17, 2018). The 2011 Plan permits the awards of options and RSUs.

Subsequently in August 2012, the 2011 Plan was superseded in its entirety as the "2012 Employee Stock Incentive Plan" ("**Pre-IPO ESOP**"). The purpose of Pre-IPO ESOP is same as the 2011 Plan. The Pre-IPO ESOP is valid and effective for 10 years from the approval of the Board of Directors. Through Pre-IPO ESOP, the Company may grant equity-based incentive up to 45,905,172 Class B ordinary shares initially (which were adjusted to 1,836,206,880 shares after the 1 to 4 share split on March 14, 2014 and further 1 to 10 Share Subdivision on June 17, 2018). The aggregate number of reserved Class B ordinary shares approved was 2,512,694,900 and 251,307,455 (which were adjusted to 2,513,074,550 shares after the Share Subdivision on June 17, 2018) as of December 31, 2018 and 2017, respectively. The Pre-IPO ESOP permits the awards of options and RSUs.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 28 Share-based payments (continued)

On June 17, 2018, the Board of Directors of the Company adopted the principal terms of the Post-IPO Share Option Scheme ("Post-IPO ESOP"). The purpose of Post-IPO ESOP is to provide selected participants with the opportunity to acquire proprietary interests in the Company and to encourage selected participants to work towards enhancing the value of the Company and its shares for the benefit of the Company and its shareholders as a whole. The total number of Class B ordinary shares available for grant under Post-IPO ESOP was 2,237,613,083 Class B ordinary shares. As of December 31, 2018, no option has been granted or agreed to be granted pursuant to Post-IPO ESOP.

Upon the Share Subdivision became effective, pro-rata adjustments have been made to the number of outstanding awarded shares, so as to give the participants the same proportion of the equity capital as that they were entitled to before the effect of the Share Subdivision. However, the number of share options, average exercise price per share option, fair value of share options, key assumptions of fair value of share options, number of RSUs and weighted average grant date fair value per RSU stated below were before the adjustment for the Share Subdivision.

### Share options granted to employees

The share options have graded vesting terms, and vest in different schedules from the grant date over one year, 2 years, 4 years, 5 years and 10 years, on condition that employees remain in service without any performance requirements. For vesting schedule as one year, all granted share options are vested on the first anniversary of the grant date. For vesting schedule as 2 years, 50% of the aggregate number of granted share options are vested on the first anniversary of the grant date, and remaining granted share options are vested in equal tranches every month over the next twelve months. For vesting schedule as 4 years, 50% of granted share options are vested on the second anniversary of the grant date, 25% of granted share options are vested on the third anniversary of the grant date, the remaining granted share options are vested on the fourth anniversary of the grant date. For vesting schedule as 5 years, 40% of granted share options are vested on the second anniversary of the grant date, and every 20% of granted share options are vested on the third, fourth and fifth anniversary of the grant date respectively. For vesting schedule as 10 years, the granted share options are vested through 10 years with 6% to 15% shares vested each year unequally.

Under Pre-IPO ESOP, the Company also granted performance-based share options to certain employees, which are generally vested over a 10-year term. The performance goals are determined by the Board of Directors. For those awards, evaluations are made as of each reporting period to assess the likelihood of performance criteria being met. Share-based compensation expenses are then adjusted to reflect the revision of original estimates.

The options may be exercised at any time and from time to time only after the closing of the QPO or upon the approval of Board of Directors for all or any portion of the share options that have become vested.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 28 Share-based payments (continued)

### Share options granted to employees (continued)

Movements in the number of share options granted to employees and their related weighted average exercise prices are as below:

| | Number of share options | Average exercise price per share option (US$) |
|---|---|---|
| Outstanding as of January 1, 2018 (Note (a)) | 189,755,311 | 1.05 |
| Granted during the year (Note (a)) | 42,500,561 | 1.98 |
| Forfeited during the year (Note (a)) | (3,857,990) | 3.26 |
| Transferred to Share Scheme Trusts (Note (a), Note 25(g)) | (85,038,091) | 1.58 |
| Effect of Share Subdivision (Note (b)) | 1,290,238,122 | — |
| Outstanding as of December 31, 2018 | 1,433,597,913 | 0.10 |
| Exercisable as of December 31, 2018 | 703,071,315 | 0.09 |
| Outstanding as of January 1, 2017 (Note (a)) | 162,831,760 | 0.88 |
| Granted during the year (Note (a)) | 31,940,400 | 2.26 |
| Forfeited during the year (Note (a)) | (5,016,849) | 3.07 |
| Outstanding as of December 31, 2017 | 189,755,311 | 1.05 |
| Exercisable as of December 31, 2017 | 146,410,089 | 0.37 |

Notes:

(a) The numbers of shares were presented as before the effect of the Share Subdivision.

(b) It represented the effects of adjustments made to the numbers of shares as a result of the Share Subdivision.

The weighted-average remaining contract life for outstanding share options was 6.60 years as of December 31, 2018 (2017: 5.17 years).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 28 Share-based payments (continued)

### *Fair value of share options*

Prior to the completion of IPO on July 9, 2018, the Group has used the discounted cash flow method to determine the underlying equity fair value of the Company and adopted equity allocation model to determine the fair value of the underlying ordinary shares. Key assumptions, such as discount rate and projections of future performance, are determined by the Group with best estimate.

Based on fair value of the underlying ordinary shares, the Group has used Binomial option-pricing model to determine the fair value of the share option as of the grant date. Key assumptions are set as below:

| | Year ended December 31, | |
|---|---|---|
| | **2018** | 2017 |
| Fair value per share (Note (a)) | **US$22.99–24.48** | US$13.93–22.25 |
| Exercise price (Note (a)) | **US$1.02–3.44** | US$0–3.44 |
| Risk-free interest rate | **3.12%–3.68%** | 2.88%–3.22% |
| Dividend yield | **—** | — |
| Expected volatility | **41.57%–43.21%** | 42.70%–44.20% |
| Expected terms | **10 years** | 10 years |

Note:

(a) The fair value per share and the exercise price presented were before the effect of the Share Subdivision.

The weighted-average fair value of granted shares was US$21.80 (which was adjusted to US$2.18 after the Share Subdivision on June 17, 2018) per share for the year ended December 31, 2018 (2017: US$16.33 (which was adjusted to US$1.63 after the Share Subdivision on June 17, 2018)).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Expressed in RMB unless otherwise indicated)

## 28 Share-based payments (continued)

### RSUs granted to employees

The Company also granted RSUs to the Company's employees under Pre-IPO ESOP. The RSUs granted would vest on the second anniversary from the grant date, and in equal tranches over the remaining years of total vesting period as four or five years, on condition that employees remain in service without any performance requirements.

The RSUs may be settled at any time and from time to time only after the closing of the QPO or upon the approval of Board of Directors for all or any portion of the RSUs that have become vested.

Movements in the number of RSUs granted to the Company's employees and the respective weighted-average grant date fair value are as follows:

| | Number of RSUs | Weighted average grant date fair value per RSU (US$) |
|---|---|---|
| Outstanding as of January 1, 2018 (Note (a)) | 24,492,747 | 2.94 |
| Granted during the year (Note (a)) | — | — |
| Forfeited during the year (Note (a)) | (3,776,549) | 6.36 |
| Effect of Share Subdivision (Note (b)) | 186,445,782 | — |
| Outstanding as of December 31, 2018 | 207,161,980 | 0.23 |
| Vested as of December 31, 2018 | 206,921,978 | 0.23 |
| Outstanding as of January 1, 2017 (Note (a)) | 41,094,870 | 4.84 |
| Granted during the year (Note (a)) | 500,000 | 14.73 |
| Forfeited during the year (Note (a)) | (17,102,123) | 7.85 |
| Outstanding as of December 31, 2017 | 24,492,747 | 2.94 |
| Vested as of December 31, 2017 | 22,209,185 | 2.46 |

Notes:

(a) The numbers of shares were presented as before the effect of the Share Subdivision.

(b) It represented the effects of adjustments made to the numbers of shares as a result of the Share Subdivision.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 28 Share-based payments (continued)

### RSUs granted to employees (continued)

The weighted-average remaining contract life for outstanding RSUs was 4.26 years as of December 31, 2018 (2017: 5.48 years).

Prior to the completion of IPO on July 9, 2018, the Group has used the discounted cash flow method to determine the underlying equity fair value of the Company and adopted equity allocation model to determine the fair value of the underlying ordinary share. Key assumptions, such as discount rate and projections of future performance, are required to be determined by the Group with best estimate.

The fair value of each RSU at the grant dates were determined by reference to the fair value of the ordinary shares of the Company that issued to its shareholders.

The total expenses recognized in the consolidated income statement for aforementioned share-based awards granted to the Group's employees are RMB2,358,917,000 for the year ended December 31, 2018 (2017: RMB807,894,000).

### Share based awards granted to Lei Jun

On April 2, 2018, the Company issued 63,959,619 Class B ordinary shares (or 639,596,190 Class B ordinary shares following the Share Subdivision) at par value to Smart Mobile Holdings Limited, an entity whose interest is held on trust for the benefit of Lei Jun and his family members, to reward Lei Jun for his contribution to the Company. Accordingly, RMB9,827,157,000 was recognized as share-based compensation expenses on April 2, 2018 by the Group.

On June 17, 2018, Lei Jun was granted 42,070,000 share options in Xiaomi Finance pursuant to the first share option scheme adopted by Xiaomi Finance. Such share options were vested immediately and Lei Jun can exercise these share options with exercise price of RMB3.8325 for each share option for the following 20 years commencing on June 17, 2018. Based on fair value of the underlying ordinary shares, the Group has used Binomial option-pricing model to determine the fair value of the share option as the grant date. Key valuation assumptions include discount rate (post-tax) of 18.5%, risk-free interest rate of 3.99%, volatility of 46%. Accordingly, RMB102,608,000 was recognized as share-based compensation expenses on June 17, 2018 by the Group.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 28 Share-based payments (continued)

### Employee fund

On August 31, 2014, the Board of Directors of the Company approved the establishment of Employee Fund with the purpose of which is to invest in companies within the business ecosystem of the Group. The Company invited certain employees to participate, with the condition that they would only receive the original investment sum with interest should they decide to resign from the Group within 5 years from the investment date (the "**Lockup Period**"). Upon the end of the Lockup Period, the holders would become the equity holders of the Employee Fund. Thereafter when the employees decide to resign after Lockup Period, the employees can demand the Company to buy back the shares at fair value or continue to hold the shares. Accordingly, the Group granted compound financial instruments to its employees and accounted for it as equity-settled share-based payments and cash-settled share-based payments.

The total expenses recognized in the consolidated income statement for the Employee Fund granted to the Group's employees are RMB91,986,000 for the year ended December 31, 2018 (2017: RMB101,261,000).

## 29 Other non-current liabilities

| | As of December 31, | |
|---|---|---|
| | **2018** | 2017 |
| | **RMB'000** | RMB'000 |
| Investment from fund investors (Note (a)) | **2,823,504** | — |
| Others | **21,355** | 35,211 |
| | **2,844,859** | 35,211 |

Note:

(a) It represents the funds raised by the third party investors under the Hubei Fund (Note 12(a)). The Group controls the Hubei Fund as the Group is exposed to and has rights to variable returns from its involvement with the Hubei Fund and has the ability to affect those returns through its power over the Hubei Fund. Hubei Fund has limited operation during the current period. For the amount raised from limited partners, the Group has contractual obligation to settle the liability with the limited partners and therefore is classified as a financial liability measured at amortized cost in the consolidated financial statements.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 30 Trade payables

Trade payables primarily include payables for inventories and royalty fees. As of December 31, 2018 and 2017, the carrying amounts of trade payables were primarily denominated in RMB, US$ and INR.

Trade payables and their aging analysis based on invoice date are as follows:

| | As of December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| Up to 3 months | 44,312,748 | 32,859,302 |
| 3 to 6 months | 1,656,699 | 936,690 |
| 6 months to 1 year | 266,623 | 180,060 |
| 1 to 2 years | 50,350 | 22,525 |
| Over 2 years | 851 | 4,754 |
| | 46,287,271 | 34,003,331 |

## 31 Other payables and accruals

| | As of December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| Amounts collected for third parties | 1,628,230 | 1,056,228 |
| Payroll and welfare payables | 795,593 | 694,887 |
| Deposits payable | 953,132 | 678,472 |
| Employee Fund (Note 28) | 553,108 | 469,930 |
| Accrual expenses | 499,295 | 373,034 |
| Payables for construction cost | 619,935 | 241,881 |
| Payables for investments | 222,382 | 151,712 |
| Loans from related parties | — | 51,336 |
| Other taxes payables | 192,182 | 59,431 |
| Others | 848,913 | 447,068 |
| | 6,312,770 | 4,223,979 |

The carrying amounts of other payables were primarily denominated in RMB and approximate their fair values as of December 31, 2018 and 2017.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 32 Advance from customers

Advance from customers primarily includes advance from customers when the Group receives payments in advance of the delivery of products or performance of services.

## 33 Borrowings

| | As of December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| **Included in non-current liabilities** | | |
| Asset-backed securities (Note (a)) | 2,752,815 | 2,400,105 |
| Fund raised through trusts (Note (b)) | — | 400,000 |
| Secured borrowings (Note (c)) | 1,260,941 | 714,107 |
| Unsecured borrowings (Note (d)) | 3,842,387 | 3,737,100 |
| | 7,856,143 | 7,251,312 |
| **Included in current liabilities** | | |
| Asset-backed securities (Note (a)) | 586,282 | 1,491,147 |
| Fund raised through trusts (Note (b)) | 648,390 | 1,170,250 |
| Pledged borrowings | — | 729,404 |
| Unsecured borrowings (Note (d)) | 1,840,522 | 160,000 |
| | 3,075,194 | 3,550,801 |

Notes:

(a) The Group has securitized certain loan receivables and completed several rounds of issuance of its asset-backed securities ("**ABS**"). As of December 31, 2018, the total ABS amounting to RMB3,339,097,000 (2017: RMB3,891,252,000) bore interest at 5.1%–8.0% per annum in 2018 (2017: 5.3%–8.8%).

(b) The Group has securitized certain loan receivables and raised several rounds of funds through third party trusts. As of December 31, 2018, the fund raised through trusts amounting to RMB648,390,000 (2017: RMB1,570,250,000) bore interest at 6.1%–6.2% per annum in 2018 (2017: 5.2%–9.0%). The Group is committed to unconditionally repurchase the aforementioned securitized loan receivables. The balance will mature in 2019.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 33 Borrowings (continued)

Notes (continued):

(c) As of December 31, 2018, RMB1,260,941,000 (2017: RMB714,107,000) of long-term borrowings were secured by construction in progress and land use rights amounting to approximately RMB4,082,853,000 (2017: RMB3,579,363,000). The interest rate of these borrowings was 4.655%–4.900% per annum (2017: 4.655%–4.900%). These borrowings should be repaid by the Group by the end of September 27, 2032.

(d) As of December 31, 2018, the Group had (i) US$500,000,000 (equivalent to approximately RMB3,431,600,000) unsecured borrowings relating to a three-year bank loan facility agreement entered into on July 26, 2017 with the available commitment US$1,000,000,000 (equivalent to approximately RMB6,863,200,000) including US$500,000,000 (equivalent to approximately RMB3,431,600,000) term loan and US$500,000,000 (equivalent to approximately RMB3,431,600,000) revolving loan, which should be repaid by the Group on July 25, 2020; (ii) RMB815,408,000 (2017: Nil) unsecured borrowings with interest rate 4.568% per annum and RMB55,114,000 (2017: Nil) unsecured borrowings with interest rate 4.568%-8.500% per annum, which should be repaid by the Group in 2019; (iii) RMB470,000,000 (2017: RMB490,000,000) unsecured borrowings with interest rate 4.750% per annum, of which RMB20,000,000 (2017: RMB20,000,000) should be repaid by the Group within the next twelve months and RMB450,000,000 (2017: RMB470,000,000) should be repaid by the Group by March 1, 2022; and (iv) unsecured borrowings of RMB450,000,000 (2017: RMB140,000,000) with interest rate 6.960% per annum (2017: 5.8725%) and RMB500,000,000 (2017: Nil) with interest rate of 6.960% per annum, which should be repaid by the Group in 2019.

For the year ended December 31, 2018, the annual interest rate of the interest-bearing liabilities ranges from 2.22% to 9.00% per annum (2017: from 2.22% to 9.00%).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 34 Deferred income taxes

Deferred income taxes are calculated in full on temporary differences under the liability method using the tax rates at which are expected to be applied at the time of reversal of the temporary differences.

The amount of offsetting deferred income tax assets and liabilities is RMB93,750,000 as of December 31, 2018 (2017: RMB129,813,000). The analysis of deferred income tax assets and liabilities before offsetting is as follows:

| | As of December 31, | |
|---|---|---|
| | **2018** | 2017 |
| | **RMB'000** | RMB'000 |
| **Deferred income tax assets:** | | |
| — to be recovered after 12 months | **625,671** | 221,133 |
| — to be recovered within 12 months | **780,324** | 500,256 |
| | **1,405,995** | 721,389 |
| **Deferred income tax liabilities:** | | |
| — to be settled after 12 months | **(870,082)** | (1,147,770) |
| — to be settled within 12 months | **(1,313)** | (694) |
| | **(871,395)** | (1,148,464) |

The gross movement on the deferred income tax assets is as follows:

| | Year ended December 31, | |
|---|---|---|
| | **2018** | 2017 |
| | **RMB'000** | RMB'000 |
| **At the beginning of the year** | **721,389** | 488,054 |
| Credited to the consolidated income statement | **684,606** | 233,335 |
| **At the end of the year** | **1,405,995** | 721,389 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 34 Deferred income taxes (continued)

The gross movement on the deferred income tax liabilities is as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| At the beginning of the year | (1,148,464) | (500,040) |
| Credited/(debited) to the consolidated income statement | 280,619 | (648,424) |
| Acquisition of a subsidiary | (3,550) | — |
| At the end of the year | (871,395) | (1,148,464) |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 34 Deferred income taxes (continued)

The movement in deferred income tax assets and liabilities during the years without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

Deferred income tax assets:

| | Accrued liabilities and provisions RMB'000 | Provision for impairment of inventories RMB'000 | Depreciation of property and amortization of intangible assets RMB'000 | Tax losses RMB'000 | Fair value changes of financial assets RMB'000 | Provision for impairment of receivables RMB'000 | Unrealized gain on intra-group transactions RMB'000 | Others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|---|---|---|
| At January 1, 2018 | 267,649 | 148,193 | 93,119 | 62,019 | 55,991 | 41,186 | 44,696 | 8,536 | 721,389 |
| (Debited)/credited to consolidated income statement | (36,189) | 237,176 | 558 | 297,180 | 24,350 | 51,775 | 111,744 | (1,988) | 684,606 |
| At December 31, 2018 | 231,460 | 385,369 | 93,677 | 359,199 | 80,341 | 92,961 | 156,440 | 6,548 | 1,405,995 |
| At January 1, 2017 | 276,035 | 66,722 | 93,474 | – | 24,643 | 1,015 | 5,540 | 20,625 | 488,054 |
| (Debited)/credited to consolidated income statement | (8,386) | 81,471 | (355) | 62,019 | 31,348 | 40,171 | 39,156 | (12,089) | 233,335 |
| At December 31, 2017 | 267,649 | 148,193 | 93,119 | 62,019 | 55,991 | 41,186 | 44,696 | 8,536 | 721,389 |

Deferred income tax assets are recognized for deductible temporary differences to the extent that the realization of the related tax benefits through future taxable profits is probable.

As of December 31, 2018, the Group did not recognize deferred income tax assets of RMB520,995,000 (2017: RMB521,499,000), in respect of deductible temporary differences and cumulative tax losses amounting RMB2,293,425,000 (2017: RMB2,330,552,000), that can be carried forward against future taxable income.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 34 Deferred income taxes (continued)

Deferred income tax liabilities:

| | Changes in fair value of financial assets RMB'000 | Business combination RMB'000 | Total RMB'000 |
|---|---|---|---|
| At January 1, 2018 | (1,147,419) | (1,045) | (1,148,464) |
| Credited to consolidated income statement | 279,038 | 1,581 | 280,619 |
| Acquisition of a subsidiary | — | (3,550) | (3,550) |
| At December 31, 2018 | (868,381) | (3,014) | (871,395) |
| At January 1, 2017 | (498,200) | (1,840) | (500,040) |
| (Debited)/credited to consolidated income statement | (649,219) | 795 | (648,424) |
| At December 31, 2017 | (1,147,419) | (1,045) | (1,148,464) |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 35 Convertible redeemable preferred shares

Since the date of incorporation, the Company has completed several rounds of financing by issuing Preferred Shares. For details, please refer to below table:

| | | Purchase Price (US$/Share) | | Number of Shares | | Total Consideration | |
|---|---|---|---|---|---|---|---|
| | Date of Issuance | Before the Share Split on March 14, 2014 (Note (a)) | After the Share Split on March 14, 2014 | Before the Share Split on March 14, 2014 | After the Share Split on March 14, 2014 | US$ | RMB |
| Series A Preferred Shares | September 28, 2010 | 0.1000 | 0.0250 | 100,000,000 | 400,000,000 | 10,000,000 | 67,051,000 |
| Series A Preferred Shares | December 21, 2010 | 0.1000 | 0.0250 | 2,500,000 | 10,000,000 | 250,000 | 1,665,000 |
| Series B1 Preferred Shares | December 21, 2010 | 0.4113 | 0.1028 | 60,775,862 | 243,103,448 | 25,000,000 | 166,493,000 |
| Series B2 Preferred Shares | December 21, 2010 | 0.5818 | 0.1454 | 4,297,283 | 17,189,132 | 2,500,000 | 16,650,000 |
| Series B+ Preferred Shares | April 11, 2011 | 0.5818 | 0.1454 | 4,727,011 | 18,908,044 | 2,750,000 | 17,371,000 |
| Series B++ Preferred Shares | August 24, 2011 | 0.5818 | 0.1454 | 1,031,347 | 4,125,388 | 600,000 | 3,834,000 |
| Series C Preferred Shares | September 30, 2011 | 2.0942 | 0.5236 | 21,010,411 | 84,041,644 | 44,000,000 | 279,616,000 |
| Series C+ Preferred Shares | November 10, 2011 | 2.0942 | 0.5236 | 1,002,765 | 4,011,060 | 2,100,000 | 13,299,000 |
| Series C Preferred Shares | March 29, 2012 | 2.0942 | 0.5236 | 21,010,411 | 84,041,644 | 44,000,000 | 276,901,000 |
| Series D Preferred Shares | June 22, 2012 | 8.1882 | 2.0471 | 13,189,777 | 52,759,108 | 108,000,000 | 680,835,000 |
| Series D Preferred Shares | December 21, 2012 | 8.1882 | 2.0471 | 13,189,777 | 52,759,108 | 108,000,000 | 679,118,000 |
| Series E1 Preferred Shares | August 5, 2013 | 15.0392 | 3.7598 | 5,319,419 | 21,277,676 | 80,000,000 | 494,139,000 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 35 Convertible redeemable preferred shares (continued)

| | Date of Issuance | Purchase Price (US$/Share) Before the Share Split on March 14, 2014 (Note (a)) | After the Share Split on March 14, 2014 | Number of Shares Before the Share Split on March 14, 2014 | After the Share Split on March 14, 2014 | Total Consideration US$ | RMB |
|---|---|---|---|---|---|---|---|
| Series E2 Preferred Shares | August 5, 2013 | 18.7614 | 4.6904 | 1,066,016 | 4,264,064 | 20,000,000 | 123,534,000 |
| Series F1 Preferred Shares | December 23, 2014 | NA | 20.1682 | NA | 37,226,830 | 750,800,000 | 4,597,137,000 |
| Series F2 Preferred Shares | December 23, 2014 | NA | 17.9273 | NA | 8,376,037 | 150,160,000 | 919,430,000 |
| Series F1 Preferred Shares | March 25, 2015 | NA | 20.1682 | NA | 1,147,843 | 23,150,000 | 144,252,000 |
| Series F1 Preferred Shares | July 3, 2015 | NA | 20.1682 | NA | 9,916,601 | 200,000,000 | 1,246,240,000 |
| Series F1 Preferred Shares | August 24, 2017 | NA | 20.1682 | NA | 495,830 | 10,000,000 | 67,573,000 |

Notes:

(a) Pursuant to the shareholders' resolution passed on March 14, 2014, every share of the issued convertible redeemable preferred shares is subdivided into four shares.

(b) Series B Preferred Shares includes Series B1 Preferred Shares, Series B2 Preferred Shares, Series B+ Preferred Shares and Series B++ Preferred Shares; Series C Preferred Shares includes Series C Preferred Shares and Series C+ Preferred Shares; Series E Preferred Shares includes Series E1 Preferred Shares and Series E2 Preferred Shares; Series F Preferred Shares includes Series F1 Preferred Shares and Series F2 Preferred Shares.

(c) Following the Share Subdivision as detailed in Note 25, each of convertible redeemable preferred share was further subdivided into 10 shares. However, the purchase price and number of shares stated above were not adjusted for the effect of the Share Subdivision.

## 35 Convertible redeemable preferred shares (continued)

The key terms of the Preferred Shares are summarized as follows:

### (a) Dividends rights

Each holder of Preferred Shares shall be entitled to receive from the Company on the preferential basis, out of funds legally available therefore, non-cumulative dividends per Preferred Share held by such holder accrued at the rate of eight percent (8%) of the applicable original issue price per annum (as adjusted for any stock dividends, combinations or splits with respect to such shares), when and if declared by the board, prior and in preference to holders of all other current or future class or series of shares of the Company, including the ordinary shares. No dividend, whether in cash, in property or in shares of the capital of the Company, shall be paid on or declared and set aside for any ordinary shares or any other class or series of shares of the Company unless and until all dividends have been paid in full on the Preferred Shares (on an as-converted basis).

### (b) Conversion feature

The Preferred Shares shall be converted into Class B ordinary shares at the option of holders at any time after July 3, 2015, or automatically converted into Class B ordinary shares at the then effective applicable conversion price upon (i) the closing of a QPO, or (ii) with written consent of holders of more than fifty percent (50%) of the issued and outstanding Series A Preferred Shares, or written consent of holders of more than two thirds (2/3) of the issued and outstanding Preferred Shares (other than Series A Preferred Shares), respectively. In the event of the automatic conversion of the Preferred Shares, the person(s) entitled to receive the Class B ordinary shares issuable upon such conversion of Preferred Shares shall not be deemed to have converted such Preferred Shares until immediately prior to the closing of such transaction.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 35 Convertible redeemable preferred shares (continued)

### (b) Conversion feature (continued)

QPO means a firm underwritten public offering of the ordinary shares or other equity securities of the Company (or as the case may be, the shares or other equity securities of the relevant entity resulting from any merger, reorganization or other arrangements made by or to the Company for the purposes of a firm underwritten public offering) on the Hong Kong Stock Exchange, New York Stock Exchange or National Association of Securities Dealers Automated Quotations ("**NASDAQ**") that has been registered under the applicable securities laws with the Group's valuation reaching a certain amount, or in a similar public offering of such shares or other equity securities in another jurisdiction which results in such shares or other equity securities trading publicly on a recognized regional or national securities exchange, provided, however, that such offering satisfies the foregoing valuation requirement and that the regulatory approval of such other jurisdiction and securities exchange is reasonably similar to that of Hong Kong Stock Exchange, New York Stock Exchange or NASDAQ as mutually determined by the majority investors and the Company.

### (c) Redemption feature

At any time commencing on the redemption start date of December 23, 2019, at the option of a holder of the Preferred Shares (other than Series F) or the option of the holders of a majority of the then issued and outstanding Series F Preferred Shares (on an as converted basis), the Company shall redeem all, but not less than all, of the issued and outstanding Preferred Shares held by the requesting holders as elected by such holders out of funds legally available therefore including capital.

The redemption price shall be paid by the Company to the Preferred Shares holders in amount equal to the greater of (i) and (ii) below: (i) one hundred percent (100%) of the issue price on each Preferred Share, plus an eight percent (8%) per annum compound interest of the issue price on each Preferred Share accrued during the period from the issue date of each Preferred Share until the date stated on redemption notice on which the Preferred Shares are to be redeemed, and any declared but unpaid dividends thereon; (ii) the fair market value of such Preferred Share, the valuation of which shall be determined through an independent appraisal performed by an appraiser selected jointly by the board and the supermajority investors, provided that such valuation shall not take into account any liquidity or minority interest discounts.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 35 Convertible redeemable preferred shares (continued)

### (d) Liquidation preferences

In the event of any liquidation, dissolution or winding up of the Company, either voluntary or involuntary, distributions to the members of the Company shall be made in the following manner (after satisfaction of all creditors' claims and claims that may be preferred by law):

Each holder of Preferred Shares shall be entitled to receive for each series of Preferred Shares he or it holds on the preferential basis, prior and in preference to any distribution of any of the assets or surplus funds of the Company to the holders of other series of Preferred Shares and ordinary shares or any other class or series of shares by reason of their ownership of such shares, the amount equal to one hundred percent (100%) of the respective applicable issue price, plus accrued or declared but unpaid dividends for holders of Series E Preferred Shares, Series D Preferred Shares, certain Series C Preferred Shares, certain Series B Preferred Shares and certain Series A Preferred Shares, respectively, or one hundred and ten percent (110%) of the respective applicable issue price, plus accrued or declared but unpaid dividends for holders of the series of Preferred Shares other than those aforementioned. If the assets and funds available for distribution shall be insufficient to permit the payment to such holders of the full preferred preference amount, the liquidation preference amount will be paid to the holders of Preferred Shares in the following order: first to holders of Series F Preferred Shares, second to holders of Series E Preferred Shares, third to holders of Series D Preferred Shares, fourth to Series C Preferred shares, fifth to Series B Preferred shares and lastly to holders of Series A Preferred Shares. After distributing or paying in full the liquidation preference amount to all of the holders of Preferred Shares, the remaining assets of the Company available for distribution to members, if any, shall be distributed to the holders of the Preferred Shares and ordinary shares on a pro rata basis, based on the number of ordinary shares then held by each holder on an as-converted basis.

The Group does not bifurcate any embedded derivatives from the host instruments and designates the entire instruments as financial liabilities at fair value through profit or loss with the changes in the fair value recorded in the consolidated income statement.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 35 Convertible redeemable preferred shares (continued)

The movement of the convertible redeemable preferred shares is set out as below:

| | RMB'000 |
|---|---|
| **At January 1, 2018** | 161,451,203 |
| Changes in fair value | (12,514,279) |
| Currency translation differences | 2,163,584 |
| Conversion into ordinary shares | (151,100,508) |
| **At December 31, 2018** | — |
| **At January 1, 2017** | 115,802,177 |
| Issuance of Series F1 Preferred Shares | 89,214 |
| Changes in fair value | 54,071,603 |
| Currency translation differences | (8,511,791) |
| **At December 31, 2017** | 161,451,203 |

Prior to the completion of IPO on July 9, 2018, the Group has used the discounted cash flow method to determine the underlying share value of the Company and adopted equity allocation model to determine the fair value of the Preferred Shares as of the dates of issuance and at the end of each reporting period.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Expressed in RMB unless otherwise indicated)

## 35 Convertible redeemable preferred shares (continued)

Key valuation assumptions used to determine the fair value of Preferred Shares are as follows:

| | As of December 31, 2017 |
|---|---|
| Discount rate | 17.00% |
| Risk-free interest rate | 2.42%–2.61% |
| DLOM | 10.00% |
| Volatility | 30.76%–33.05% |

Discount rate (post-tax) was estimated by weighted average cost of capital as of each valuation date. The Group estimated the risk-free interest rate based on the yield of US Government Bond with maturity life close to the QPO timing as of valuation date plus country risk spread. The DLOM was estimated based on the option-pricing method. Under option-pricing method, the cost of put option, which can hedge the price change before the private held share can be sold, was considered as a basis to determine the lack of marketability discount. Volatility was estimated based on annualized standard deviation of daily stock price return of comparable companies for a period from the respective valuation date and with similar span as time to expiration. Probability weight under each of the conversion feature, redemption feature and liquidation preferences was based on the Group's best estimates. In addition to the assumptions adopted above, the Company's projections of future performance were also factored into the determination of the fair value of Preferred Shares on each valuation date.

On July 9, 2018, the Company has successfully listed on the Main Board of the Stock Exchange and made an offering of 2,179,585,000 Class B ordinary shares (excluding any Class B ordinary shares issued pursuant to the exercise of the over-allotment option) at a price at HK$17.00 per share. All Preferred Shares were converted into Class B ordinary shares upon completion of the IPO on July 9, 2018. The fair value of each of Preferred Share on the conversion date is the Offer Price in the Global Offering.

Changes in fair value of Preferred Shares were recorded in "fair value changes of convertible redeemable preferred shares". Management considered that fair value changes in the Preferred Shares that are attributable to changes of credit risk of this liability are not significant.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 36 Cash flow information

### (a) Cash generated from operations

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| **Profit/(loss) before income tax** | **13,927,124** | (41,829,352) |
| Adjustments for: | | |
| — Depreciation of property and equipment | **219,523** | 166,515 |
| — Amortization of intangible assets | **528,693** | 194,441 |
| — Gain on disposal of property and equipment | **(10,295)** | (513) |
| — Provision for impairment for trade and other receivables | **33,211** | 16,965 |
| — Impairment provision for loan receivables | **607,180** | 258,470 |
| — Impairment provision for inventories | **3,006,525** | 652,560 |
| — Interest income | **(601,065)** | (242,518) |
| — Interest expense | **384,692** | 215,734 |
| — Dividend income | **(131,804)** | (106,291) |
| — Share of losses of investments accounted for using the equity method | **614,920** | 231,496 |
| — Remeasurement of investments transferring from financial assets measured at fair value through profit or loss to investments accounted for using the equity method | **(126,614)** | — |
| — Net gains on disposals of long-term investments measured at fair value through profit or loss | **(28,176)** | (192,008) |
| — Gains on disposal of an investment accounted for using the equity method | **—** | (91,429) |
| — Fair value changes of convertible redeemable preferred shares | **(12,514,279)** | 54,071,603 |
| — Fair value gains on long-term investments measured at fair value through profit or loss | **(4,430,359)** | (6,371,098) |
| — Share-based compensation | **12,380,668** | 909,155 |
| — Foreign exchanges losses, net | **14,550** | 144,265 |
| — Investment income from short-term investments measured at fair value through profit or loss | **(335,695)** | (162,702) |
| — Investment income from short-term investments measured at amortized cost | **(20,199)** | (54,789) |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 36 Cash flow information (continued)

### (a) Cash generated from operations (continued)

| | Year ended December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| Changes in working capital: | | |
| — Increase in inventories | (16,114,975) | (8,617,146) |
| — Increase in trade receivables | (91,003) | (3,396,954) |
| — Increase in loan receivables | (2,752,183) | (6,856,767) |
| — Increase in prepayments and other receivables | (9,463,591) | (6,624,612) |
| — Decrease/(increase) in restricted cash | 294,753 | (1,788,284) |
| — Increase in trade payables | 12,627,385 | 15,476,486 |
| — Increase in advance from customers | 1,050,583 | 1,554,508 |
| — (Decrease)/increase in warranty provision | (51,600) | 885,170 |
| — Increase in other payables and accruals | 1,118,058 | 2,056,983 |
| — (Decrease)/increase in other non-current liabilities | (13,856) | 27,433 |
| **Cash generated from operations** | 122,171 | 527,321 |

### (b) Proceeds from disposal of property and equipment

In the consolidated statement of cash flows, proceeds from sale of property and equipment comprise:

| | Year ended December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| Net book amount (Note 16) | 17,072 | 1,018 |
| Gain on disposal of property and equipment | 10,295 | 513 |
| **Proceeds from disposal of property and equipment** | 27,367 | 1,531 |

### (c) Non-cash transactions

Other than the share based awards described in Note 28, the reclassification of the investment in associates measured at fair value through profit or loss to investment accounted for using the equity method as described in Note 12(b), the conversion of convertible redeemable preferred shares described in Note 35 and the issuance of Class B ordinary shares as consideration in exchange for certain indirect equity interests in Timi Personal Computing Co., Ltd. described in Note 25, there were no material non-cash transactions for the year ended December 31, 2018 (2017: Nil).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 36 Cash flow information (continued)

### (d) Reconciliation of liabilities generated from financing activities

| | Liabilities from financing activities | | | | |
|---|---|---|---|---|---|
| | Borrowing due within 1 year RMB'000 | Borrowing due after 1 year RMB'000 | Convertible redeemable preferred shares RMB'000 | Interest payable RMB'000 | Total RMB'000 |
| Liabilities from financing activities as of January 1, 2018 | 3,550,801 | 7,251,312 | 161,451,203 | 5,742 | 172,259,058 |
| Cash flows | (5,928,062) | 5,691,840 | — | (243,966) | (480,188) |
| Accrued interest expenses | — | — | — | 334,416 | 334,416 |
| Fair value changes of convertible redeemable preferred shares | — | — | (12,514,279) | — | (12,514,279) |
| Foreign exchange adjustments | (14,290) | 418,950 | 2,163,584 | — | 2,568,244 |
| Conversion of Preferred Shares to ordinary shares | — | — | (151,100,508) | — | (151,100,508) |
| Reclassification from non-current to current | 5,466,745 | (5,466,745) | — | — | — |
| Others | — | (39,214) | — | — | (39,214) |
| Liabilities from financing activities as of December 31, 2018 | 3,075,194 | 7,856,143 | — | 96,192 | 11,027,529 |
| Liabilities from financing activities as of January 1, 2017 | 3,768,500 | 390,000 | 115,802,177 | 3,489 | 119,964,166 |
| Cash flows | (338,406) | 6,982,019 | 67,573 | (146,378) | 6,564,808 |
| Accrued interest expenses | — | — | — | 148,631 | 148,631 |
| Fair value changes of convertible redeemable preferred shares | — | — | 54,071,603 | — | 54,071,603 |
| Foreign exchange adjustments | — | — | (8,511,791) | — | (8,511,791) |
| Reclassification from non-current to current | 120,707 | (120,707) | — | — | — |
| Others | — | — | 21,641 | — | 21,641 |
| Liabilities from financing activities as of December 31, 2017 | 3,550,801 | 7,251,312 | 161,451,203 | 5,742 | 172,259,058 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 37 Contingencies

The Group did not have any material contingent liabilities as of December 31, 2018 and 2017.

## 38 Commitments

### (a) Capital commitments

Capital expenditure contracted for at the end of the years but not yet incurred is as follows:

| | As of December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Property and equipment | 1,825,343 | 1,486,029 |
| Intangible assets | 57,778 | 112,888 |
| Investments | 137,176 | 198,788 |
| | 2,020,297 | 1,797,705 |

### (b) Operating lease commitments

The Group leases offices and servers under non-cancellable operating lease agreements. The lease terms are between 1 to 7 years, and majority of lease agreements are renewable at the end of the lease at market rate.

The Group's future aggregate minimum lease payments under non-cancellable operating leases are as follows:

| | As of December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Not later than 1 year | 560,926 | 258,230 |
| Later than 1 year and not later than 5 years | 385,038 | 280,613 |
| Later than 5 years | 83,276 | — |
| | 1,029,240 | 538,843 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operational decisions. Parties are also considered to be related if they are subject to common control. Members of key management and their close family members of the Group are also considered as related parties.

Save as disclosed in Note 22 and Note 31, the following significant transactions were carried out between the Group and its related parties during the years presented. In the opinion of the directors of the Company, the related party transactions were carried out in the normal course of business and at terms negotiated between the Group and the respective related parties.

### (a) Names and relationships with related parties

The following companies are significant related parties of the Group that had transactions and/or balances with the Group during the year.

| Company | Relationship |
|---|---|
| Beijing Kingsoft Cloud Technology Co., Ltd. | Associate of the Group |
| Beijing Kingsoft Internet Security Software Co., Ltd. (Note (b)) | Associate of Lei Jun |
| Suzhou Industrial Park Shunwei Technology Venture Capital Partnership (Limited Partnership) | Controlled by a director |
| Zhuhai Xishanju Mobile Technology Co., Ltd. | Associate of the Group |
| Qingdao Yeelink Information Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Beijing Fengmi Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Beijing Miiiw Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Nanjing Jiqidao Smart Technology Co., Ltd. | Associate of the Group |
| Shanghai Chuangmi Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Shanghai Chunmi Electronic Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Shanghai Xiaoxun Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Wuxi Roidmi Co., Ltd. (Note (a)) | Associate of the Group |
| Beijing Yuemi Technology Co., Ltd. | Associate of the Group |
| Ximalaya Inc. (Note (a)) | Associate of the Group |
| Beijing Roborock Technology Co., Ltd. | Associate of the Group |
| Shanghai Runmi Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Banya Information Technology (Shanghai) Co., Ltd. (Note (a)) | Associate of the Group |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions (continued)

### (a) Names and relationships with related parties (continued)

| Company | Relationship |
|---|---|
| Sichuan Xin Wang Bank Co., Ltd. (Note 12(b)) | Associate of the Group |
| Dongguan Powerise Fashion Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Turok Steinhardt (Beijing) Optical Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Qiji (Xiamen) Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Tianjin Hualai Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Shenzhen ShowmePlus Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Soocare (Shenzhen) Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Ningxia Raycom Technology Development Co., Ltd. (Note (a)) | Associate of the Group |
| Longcheer Technology (Huizhou) Co., Ltd. | Associate of the Group |
| ChingMi (Beijing) Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Shanghai Longcheer Technology Co., Ltd. | Associate of the Group |
| Longcheer Communication Technology (HK) Co., Ltd. | Associate of the Group |
| Beijing iQIYI Science & Technology Co., Ltd. (Note (12(b)) | Associate of the Group |
| Beijing Particle Information Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Shenzhen Lumi Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Beijing SmartMi Electronic Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Anhui Huami Information Technology Co., Ltd. (Note 12(b)) | Associate of the Group |
| Jiangsu Zimi Electronic Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Ninebot Limited (Note (a)) | Associate of the Group |
| Foshan Yunmi Electrical Technology Co., Ltd. (Note (12(b)) | Associate of the Group |
| Zimi Communication Technology (Jiangsu) Co., Ltd. (Note (a)) | Associate of the Group |
| Shenzhen Pineapple Games Co., Ltd. (Note (a)) | Associate of the Group |
| FiMi United Technology Limited (Note (a)) | Associate of the Group |
| Shanghai Pineapple Entertainment Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Eryihao Acoustics Science & Technology (Shenzhen) Co., Ltd. (Note (a)) | Associate of the Group |
| 1 More Acoustics Science & Technology (Shenzhen) Co., Ltd. (Note (a)) | Associate of the Group |
| Viomi Technology Co., Ltd. (Note 12(b)) | Associate of the Group |
| Nanchang Blackshark Technology Co., Ltd. | Associate of the Group |
| Seasun Entertainment Co., Ltd. | Associate of the Group |
| Forewin Suzhou Electronics Co., Ltd. (Note (a)) | Associate of the Group |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions (continued)

### (a) Names and relationships with related parties (continued)

| Company | Relationship |
|---|---|
| Luokeshidai Technology (Shenzhen) Co., Ltd. (Note (a)) | Associate of the Group |
| Guolong Information Technology (Shanghai) Co., Ltd. | Associate of the Group |
| Liesheng Technology (Dongguan) Co., Ltd. (Note (a)) | Associate of the Group |
| Feihui Smart Lighting (Shanghai) Co., Ltd. | Associate of the Group |
| Miaobo Software Technology (Shanghai) Co., Ltd. | Associate of the Group |
| Tianjin Smate Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Beijing iHealth Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Rice Sugar Culture Creative Co., Ltd. (Note (a)) | Associate of the Group |
| XiaoHou Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Inso Technology Co., Ltd. (Note (a)) | Associate of the Group |
| QingHeXiaoBei (Wuxi) Inc. | Associate of the Group |
| LeXiu Technology (Hangzhou) Co., Ltd. (Note (a)) | Associate of the Group |
| Chunmi Technology (Wuhu) Co., Ltd. (Note (a)) | Associate of the Group |
| Beijing Xiaomi Insurance Co., Ltd. | Associate of the Group |
| Shunwei Ventures II (Hong Kong) Limited | Controlled by a director |
| Beijing MADV Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Beijing ClearGrass Technology Co., Ltd. (Note (a)) | Associate of the Group |

Notes:

(a) The Group's investments were made in the form of ordinary shares with preferential rights or convertible redeemable preferred shares which are accounted as financial assets measured at fair value through profit or loss.

(b) Since March 13, 2018, the Group has ceased to be a related party with Beijing Kingsoft Internet Security Software Co., Ltd., subsidiaries of Cheetah Mobile Inc. as Lei Jun resigned as the Chairman and a member of the Board of Cheetah Mobile Inc.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions (continued)

### (b) Significant transactions with related parties

| | Year ended December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| **(i) Sales of goods and services** | | |
| Associates of the Group | 1,153,491 | 704,476 |
| Associates of Lei Jun | 25,376 | 61,456 |
| | 1,178,867 | 765,932 |
| **(ii) Purchases of goods and services** | | |
| Associates of the Group | 18,634,514 | 13,254,277 |
| Associates of Lei Jun | 14,768 | 686 |
| | 18,649,282 | 13,254,963 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions (continued)

### (c) Year end balances with related parties

| | As of December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| **(i) Trade receivables from related parties** | | |
| Associates of the Group | 361,792 | 162,901 |
| Associates of Lei Jun | 2,816 | 25,715 |
| | 364,608 | 188,616 |
| **(ii) Trade payables to related parties** | | |
| Associates of the Group | 4,004,778 | 3,204,190 |
| Associates of Lei Jun | 1,916 | 4,572 |
| | 4,006,694 | 3,208,762 |
| **(iii) Other receivables from related parties** | | |
| Associates of the Group | 243,126 | 177,831 |
| Controlled by a director | — | 4,000 |
| | 243,126 | 181,831 |
| **(iv) Other payables to related parties** | | |
| Associates of the Group | 770,032 | 416,348 |
| Controlled by a director | 76,966 | — |
| Associates of Lei Jun | 7,652 | 8,202 |
| | 854,650 | 424,550 |
| **(v) Prepayments** | | |
| Associates of the Group | 88,289 | 67,336 |

All the balances with related parties above were unsecured and repayable within one year.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions (continued)

### (d) Loans to related parties

| | Year ended December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| **Loans to associates:** | | |
| At the beginning of the year | 62,143 | 74,329 |
| Loans advanced | 50,000 | 1,500 |
| Loans repaid | (103,116) | (14,000) |
| Interest charged | 1,921 | 3,481 |
| Interest received | (2,210) | (1,845) |
| Currency translation differences | (759) | (1,322) |
| At the end of the year | 7,979 | 62,143 |

### (e) Loans from related parties

| | Year ended December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| **Loans from associates:** | | |
| At the beginning of the year | 51,336 | 50,873 |
| Loans repaid | (50,958) | — |
| Interest charged | 146 | 463 |
| Interest paid | (855) | — |
| Currency translation differences | 331 | — |
| At the end of the year | — | 51,336 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions (continued)

### (f) Key management compensation

| | Year ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | RMB'000 | RMB'000 |
| Salaries | 15,124 | 6,113 |
| Discretionary bonuses | 1,200 | 9,550 |
| Share-based compensation | 10,464,196 | 186,095 |
| Employer's contribution to pension schedule | 989 | 1,067 |
| | 10,481,509 | 202,825 |

## 40 Events after the reporting period

The Company repurchased 6,140,000, 9,849,600 and 3,982,600 Class B ordinary shares of the Company on January 17, 2019, January 18, 2019 and January 22, 2019, representing approximately 0.026%, 0.041% and 0.017% of the issued total share capital of the Company as at the respective transaction days. The total considerations were approximately HK$59,942,000, HK$100,000,000 and HK$39,989,000, respectively.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 41 Financial position and reserve movement of the Company

### (a) Financial position of the Company

| | As of December 31, 2018 RMB'000 | 2017 RMB'000 |
|---|---|---|
| **Assets** | | |
| **Non-current assets** | | |
| Property and equipment | 35 | 33 |
| Investment in subsidiaries | 13,434,702 | 5,815,295 |
| Other assets | 77 | 73 |
| | 13,434,814 | 5,815,401 |
| **Current assets** | | |
| Prepayments and other receivables | 30,217,183 | 7,550,122 |
| Cash and cash equivalents | 5,707 | 2,131 |
| | 30,222,890 | 7,552,253 |
| **Total assets** | 43,657,704 | 13,367,654 |
| **Equity and liabilities** | | |
| **Equity attributable to owners of the Company** | | |
| Share capital | 377 | 150 |
| Reserves | 39,159,983 | (149,322,405) |
| **Total equity** | 39,160,360 | (149,322,255) |
| **Liabilities** | | |
| **Non-current liabilities** | | |
| Convertible redeemable preferred shares | — | 161,451,203 |
| | — | 161,451,203 |
| **Current liabilities** | | |
| Other payables and accruals | 4,497,344 | 1,238,706 |
| | 4,497,344 | 1,238,706 |
| **Total liabilities** | 4,497,344 | 162,689,909 |
| **Total equity and liabilities** | 43,657,704 | 13,367,654 |

The balance sheet of the Company was approved by the Board of Directors on March 19, 2019 and was signed on its behalf:

**Lei Jun**
*Director*

**Lin Bin**
*Director*

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 41 Financial position and reserve movement of the Company (continued)

### (b) Reserve movement of the Company

| | Share premium RMB'000 | Share-based compensation reserve RMB'000 | Currency translation differences RMB'000 | Capital reserve RMB'000 | Others RMB'000 | Subtotal RMB'000 | Accumulated losses RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|---|---|
| **At January 1, 2018** | 742,760 | 3,816,153 | (3,495,173) | 25,950 | 9,392 | 1,099,082 | (150,421,487) | (149,322,405) |
| Issuance of ordinary shares | 9,827,146 | — | — | — | — | 9,827,146 | — | 9,827,146 |
| Issuance of ordinary shares relating to initial public offering, net of underwriting commissions and other issuance costs | 23,248,593 | — | — | — | — | 23,248,593 | — | 23,248,593 |
| Release of ordinary shares from Share Scheme Trusts | 933,592 | (841,640) | — | — | — | 91,952 | — | 91,952 |
| Conversion of Preferred Shares to ordinary shares | 151,100,334 | — | — | — | — | 151,100,334 | — | 151,100,334 |
| Employees share-based compensation scheme: — value of employee services (Note 28) | — | 2,461,525 | — | — | — | 2,461,525 | — | 2,461,525 |
| Acquisition of additional equity interests in non wholly owned subsidiaries | 230,899 | — | — | — | — | 230,899 | — | 230,899 |
| Currency translation differences (Note (a)) | — | — | (1,098,818) | — | — | (1,098,818) | — | (1,098,818) |
| Share premium set off the accumulated losses and other reserves | (142,232,042) | — | 5,579,472 | — | — | (136,652,570) | 136,652,570 | — |
| Profit for the year | — | — | — | — | — | — | 2,620,757 | 2,620,757 |
| **At December 31, 2018** | 43,851,282 | 5,436,038 | 985,481 | 25,950 | 9,392 | 50,308,143 | (11,148,160) | 39,159,983 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 41 Financial position and reserve movement of the Company (continued)

### (b) Reserve movement of the Company (continued)

| | Share premium RMB'000 | Share-based compensation reserve RMB'000 | Currency translation differences RMB'000 | Capital reserve RMB'000 | Others RMB'000 | Subtotal RMB'000 | Accumulated losses RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|---|---|
| **At January 1, 2017** | 742,760 | 3,008,259 | (11,549,446) | 13,662 | 16,466 | (7,768,299) | (96,219,976) | (103,988,275) |
| Employees share-based compensation scheme: | | | | | | | | |
| – value of employee services (Note 28) | – | 807,894 | – | – | – | 807,894 | – | 807,894 |
| Share of other comprehensive loss of investments accounted for using the equity method | – | – | – | – | (7,074) | (7,074) | – | (7,074) |
| Share of other reserves of investments accounted for using the equity method | – | – | – | 12,288 | – | 12,288 | – | 12,288 |
| Currency translation differences (Note (a)) | – | – | 8,054,273 | – | – | 8,054,273 | – | 8,054,273 |
| Loss for the year | – | – | – | – | – | – | (54,201,511) | (54,201,511) |
| **At December 31, 2017** | 742,760 | 3,816,153 | (3,495,173) | 25,950 | 9,392 | 1,099,082 | (150,421,487) | (149,322,405) |

Note:

(a) Foreign Currency translation reserve represents the difference arising from the translation of the financial statements of the Company as its functional currency in US$, different from its presentation currency as RMB.

# INDEPENDENT AUDITOR'S REPORT

pwc 羅兵咸永道

To the Shareholders of Xiaomi Corporation
(incorporated in the Cayman Islands with limited liability)

## Opinion

### What we have audited

The consolidated financial statements of Xiaomi Corporation (the "**Company**") and its subsidiaries (the "**Group**") set out on pages 183 to 325, which comprise:

- the consolidated balance sheet as of December 31, 2019;
- the consolidated income statement for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

### Our opinion

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as of December 31, 2019, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("**IFRSs**") and have been properly prepared in compliance with the disclosure requirements of the Hong Kong Companies Ordinance.

## Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing ("**ISAs**"). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

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# INDEPENDENT AUDITOR'S REPORT

### Independence

We are independent of the Group in accordance with the International Code of Ethics for Professional Accountants (including International Independence Standards) issued by the International Ethics Standards Board for Accountants ("**IESBA Code**"), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code.

## Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter identified in our audit is related to the classification and fair value determination for unlisted securities classified as "long-term investments measured at fair value through profit or loss".

| Key Audit Matter | How our audit addressed the Key Audit Matter |
|---|---|
| **The classification and fair value determination for unlisted securities classified as "long-term investments measured at fair value through profit or loss"**<br><br>Refer to Note 3.3 and Note 19 to the consolidated financial statements.<br><br>During the year ended December 31, 2019, the Group recognized fair value changes on the following investments in profits or losses: (i) equity investments in unlisted companies other than those accounted for using equity method, and (ii) convertible redeemable preferred shares or ordinary shares with preferential rights investments in unlisted companies (collectively the "**Unlisted Securities**"), amounting to RMB2,494,191,000 and RMB13,406,909,000, respectively. The total amount of Unlisted Securities as of December 31, 2019 was RMB15,901,100,000, accounting for 9% of the Group's total assets. | We understood and evaluated the key controls over the capturing, measurement and recording of the Unlisted Securities investments.<br><br>For the classification and initial recognition of the Unlisted Securities, we have performed the following procedures:<br><br>(1) We checked relevant legal documents such as shareholder agreements, share purchase agreements and articles of association of the investees on a sample basis to understand the commercial rationale for these Unlisted Securities investments;<br><br>(2) We evaluated management's analysis on contract terms and assessed the reasonableness of management's accounting treatments on a sample basis. |

# INDEPENDENT AUDITOR'S REPORT

| Key Audit Matter | How our audit addressed the Key Audit Matter |
|---|---|
| The classification and initial recognition of the Unlisted Securities require management to analyze certain complex contract terms and make judgments to determine the classifications of the above financial assets, based on the Group's business models of managing these financial assets and the contractual terms of the cash flows. The Group identified its various rights and evaluated the financial impacts based on key terms from relevant legal documents.<br><br>Management engaged an external valuer to assist to determine the fair value of these Unlisted Securities. The fair value determination of such Unlisted Securities required management to make judgments and estimates, including the appropriateness of using various unobservable inputs.<br><br>We focused on this area due to the significance of the balances of these investments and their related fair value gain or loss for the year, as well as management judgments, assumptions and estimations involved in the initial recognition and fair value determination of the Unlisted Securities. | For the assessment of fair value determination of the Unlisted Securities, we involved our internal valuation specialists to perform the following procedures:<br><br>(1) We assessed the objectivity, independence and competence of the external valuer engaged by the Group;<br><br>(2) We interviewed management and understood the underlying assumptions and inputs used in fair value determination of Unlisted Securities;<br><br>(3) We assessed the reasonableness of assumptions and inputs used in fair value determination of Unlisted Securities, including expected volatility, risk-free interest rate, discounted for lack of marketability;<br><br>(4) We recalculated the fair values of Unlisted Securities on a sample basis; and<br><br>(5) We tested the accuracy of the fair value changes on investments measured at fair value through profit or loss for the year on a sample basis.<br><br>We found the judgments, assumptions and estimations made by management in relation to the initial recognition and fair value determination of the Unlisted Securities to be supportable based on the available evidences. |

# INDEPENDENT AUDITOR'S REPORT

## Other Information

The directors of the Company are responsible for the other information. The other information comprises all of the information included in the annual report other than the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

## Responsibilities of Directors and the Audit Committee for the Consolidated Financial Statements

The directors of the Company are responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with IFRSs and the disclosure requirements of the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

The Audit Committee is responsible for overseeing the Group's financial reporting process.

# INDEPENDENT AUDITOR'S REPORT

## Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. We report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.

- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

# INDEPENDENT AUDITOR'S REPORT

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Audit Committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Yuen Kwok Sun.

**PricewaterhouseCoopers**
Certified Public Accountants

Hong Kong, March 31, 2020

# CONSOLIDATED INCOME STATEMENT

For the year ended December 31, 2019

(Expressed in Renminbi ("RMB"))

| | Note | Year ended December 31, 2019 RMB'000 | 2018 RMB'000 |
|---|---|---|---|
| **Revenue** | 6 | 205,838,682 | 174,915,425 |
| Cost of sales | 8 | (177,284,649) | (152,723,486) |
| **Gross profit** | | 28,554,033 | 22,191,939 |
| Selling and marketing expenses | 8 | (10,378,073) | (7,993,072) |
| Administrative expenses | 8 | (3,103,901) | (12,099,078) |
| Research and development expenses | 8 | (7,492,554) | (5,776,826) |
| Fair value changes on investments measured at fair value through profit or loss | 19(iv) | 3,813,012 | 4,430,359 |
| Share of losses of investments accounted for using the equity method | 11(b) | (671,822) | (614,920) |
| Other income | 7 | 1,265,921 | 844,789 |
| Other (losses)/gains, net | | (226,399) | 213,281 |
| **Operating profit** | | 11,760,217 | 1,196,472 |
| Finance income, net | 10 | 402,429 | 216,373 |
| Fair value changes of convertible redeemable preferred shares | 35 | — | 12,514,279 |
| **Profit before income tax** | | 12,162,646 | 13,927,124 |
| Income tax expenses | 12 | (2,059,696) | (449,377) |
| **Profit for the year** | | 10,102,950 | 13,477,747 |
| **Attributable to:** | | | |
| — Owners of the Company | | 10,044,164 | 13,553,886 |
| — Non-controlling interests | | 58,786 | (76,139) |
| | | 10,102,950 | 13,477,747 |
| **Earnings per share (expressed in RMB per share):** | 13 | | |
| Basic | | 0.423 | 0.843 |
| Diluted | | 0.410 | 0.044 |

*The notes on pages 191 to 325 are an integral part of these consolidated financial statements.*

# CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended December 31, 2019

(Expressed in RMB)

| | Note | Year ended December 31, 2019 RMB'000 | 2018 RMB'000 |
|---|---|---|---|
| **Profit for the year** | | **10,102,950** | 13,477,747 |
| **Other comprehensive income/(loss):** | | | |
| *Items that may be reclassified subsequently to profit or loss* | | | |
| Share of other comprehensive income of investments accounted for using the equity method | 11(b) | 9,279 | 191,449 |
| Currency translation differences | | (77,430) | (648,746) |
| *Item that will not be reclassified subsequently to profit or loss* | | | |
| Currency translation differences | | 508,584 | (1,098,818) |
| **Other comprehensive income/(loss) for the year, net of tax** | | **440,433** | (1,556,115) |
| **Total comprehensive income for the year** | | **10,543,383** | 11,921,632 |
| **Attributable to:** | | | |
| — Owners of the Company | | 10,472,914 | 11,989,243 |
| — Non-controlling interests | | 70,469 | (67,611) |
| | | 10,543,383 | 11,921,632 |

*The notes on pages 191 to 325 are an integral part of these consolidated financial statements.*

# CONSOLIDATED BALANCE SHEET

As of December 31, 2019

(Expressed in RMB)

| | Note | As of December 31, 2019 RMB'000 | 2018 RMB'000 |
|---|---|---|---|
| **Assets** | | | |
| **Non-current assets** | | | |
| Land use rights | | — | 3,402,968 |
| Property and equipment | 14 | 6,992,331 | 5,068,053 |
| Intangible assets | 15 | 1,672,002 | 2,061,192 |
| Investments accounted for using the equity method | 11(b) | 9,300,507 | 8,639,238 |
| Long-term investments measured at fair value through profit or loss | 19 | 20,679,363 | 18,636,208 |
| Deferred income tax assets | 34 | 1,283,415 | 1,312,245 |
| Other non-current assets | 17 | 6,162,503 | 95,485 |
| | | 46,090,121 | 39,215,389 |
| **Current assets** | | | |
| Inventories | 23 | 32,585,438 | 29,480,685 |
| Trade receivables | 21 | 6,948,567 | 5,598,443 |
| Loan receivables | 20 | 12,723,503 | 10,293,645 |
| Prepayments and other receivables | 22 | 19,837,018 | 20,914,946 |
| Short-term investments measured at fair value through profit or loss | 19 | 16,463,390 | 6,648,526 |
| Short-term bank deposits | 24(c) | 21,523,043 | 1,365,991 |
| Restricted cash | 24(b) | 1,538,266 | 1,480,178 |
| Cash and cash equivalents | 24(a) | 25,919,861 | 30,230,147 |
| | | 137,539,086 | 106,012,561 |
| **Total assets** | | 183,629,207 | 145,227,950 |
| **Equity and liabilities** | | | |
| **Equity attributable to owners of the Company** | | | |
| Share capital | 25 | 388 | 377 |
| Reserves | | 81,330,186 | 71,322,608 |
| | | 81,330,574 | 71,322,985 |
| **Non-controlling interests** | | 327,102 | (72,856) |
| **Total equity** | | 81,657,676 | 71,250,129 |

# CONSOLIDATED BALANCE SHEET

As of December 31, 2019

(Expressed in RMB)

| | Note | As of December 31, 2019 RMB'000 | 2018 RMB'000 |
|---|---|---|---|
| **Liabilities** | | | |
| **Non-current liabilities** | | | |
| Borrowings | 33 | 4,786,856 | 7,856,143 |
| Deferred income tax liabilities | 34 | 579,902 | 777,645 |
| Warranty provision | | 667,857 | 559,016 |
| Other non-current liabilities | 29 | 3,756,211 | 2,844,859 |
| | | 9,790,826 | 12,037,663 |
| **Current liabilities** | | | |
| Trade payables | 30 | 59,527,940 | 46,287,271 |
| Other payables and accruals | 31 | 9,101,343 | 6,312,770 |
| Advance from customers | 32 | 8,237,119 | 4,479,522 |
| Borrowings | 33 | 12,836,555 | 3,075,194 |
| Income tax liabilities | | 479,350 | 661,816 |
| Warranty provision | | 1,998,398 | 1,123,585 |
| | | 92,180,705 | 61,940,158 |
| **Total liabilities** | | 101,971,531 | 73,977,821 |
| **Total equity and liabilities** | | 183,629,207 | 145,227,950 |

*The notes on pages 191 to 325 are an integral part of these consolidated financial statements.*

The consolidated financial statements on pages 183 to 325 were approved by the Board of Directors on March 31, 2020 and were signed on its behalf:

**Lei Jun** **Lin Bin**

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended December 31, 2019

(Expressed in RMB)

| | Note | Share capital RMB'000 | Treasury shares RMB'000 | Share premium RMB'000 | Other reserves (Note 26) RMB'000 | Retained earnings RMB'000 | Sub-total RMB'000 | Non-controlling interests RMB'000 | Total equity RMB'000 |
|---|---|---|---|---|---|---|---|---|---|
| | | Attributable to owners of the Company | | | | | | | |
| **Balance at January 1, 2019** | | 377 | — | 43,851,282 | 6,447,415 | 21,023,911 | 71,322,985 | (72,856) | 71,250,129 |
| **Comprehensive income** | | | | | | | | | |
| Profit for the year | | — | — | — | — | 10,044,164 | 10,044,164 | 58,786 | 10,102,950 |
| **Other comprehensive income** | | | | | | | | | |
| *Items that may be reclassified subsequently to profit or loss* | | | | | | | | | |
| Share of other comprehensive income of investments accounted for using the equity method | 11(b) | — | — | — | 9,279 | — | 9,279 | — | 9,279 |
| Currency translation differences | 26 | — | — | — | (89,113) | — | (89,113) | 11,683 | (77,430) |
| *Item that will not be reclassified subsequently to profit or loss* | | | | | | | | | |
| Currency translation differences | 26 | — | — | — | 508,584 | — | 508,584 | — | 508,584 |
| **Total comprehensive income** | | — | — | — | 428,750 | 10,044,164 | 10,472,914 | 70,469 | 10,543,383 |
| **Transactions with owners in their capacity as owners** | | | | | | | | | |
| Purchase of own shares | 25 | — | (2,932,111) | — | — | — | (2,932,111) | — | (2,932,111) |
| Cancellation of shares | 25 | 1 | 1,879,289 | (1,882,527) | — | — | (3,237) | — | (3,237) |
| Release of ordinary shares from Share Scheme Trusts | 25 | 1 | — | 167,447 | (139,015) | — | 28,433 | — | 28,433 |
| Share of other reserves of investments accounted for using the equity method | 11(b) | — | — | — | 229,740 | — | 229,740 | — | 229,740 |
| Employees share-based compensation scheme: | | | | | | | | | |
| — value of employee services | 28 | — | — | — | 2,127,878 | — | 2,127,878 | 89 | 2,127,967 |
| — exercise of share options and restricted stock units | 28 | 9 | — | 1,442,634 | (1,184,767) | — | 257,876 | — | 257,876 |
| Capital injection from non-controlling interests | | — | — | — | — | — | — | 155,496 | 155,496 |
| Acquisition of additional equity interests in non-wholly owned subsidiaries | 11(a) | — | — | — | (173,904) | — | (173,904) | 173,904 | — |
| Appropriation to statutory reserves | 26 | — | — | — | 295,047 | (295,047) | — | — | — |
| Appropriation to general reserves | 26 | — | — | — | 2 | (2) | — | — | — |
| **Total transactions with owners in their capacity as owners** | | 11 | (1,052,822) | (272,446) | 1,154,981 | (295,049) | (465,325) | 329,489 | (135,836) |
| **Balance at December 31, 2019** | | 388 | (1,052,822) | 43,578,836 | 8,031,146 | 30,773,026 | 81,330,574 | 327,102 | 81,657,676 |

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended December 31, 2019

(Expressed in RMB)

| | | Attributable to owners of the Company | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Note | Share capital RMB'000 | Share premium RMB'000 | Other reserves (Note 26) RMB'000 | Accumulated losses/retained earnings RMB'000 | Sub-total RMB'000 | Non-controlling interests RMB'000 | Total equity RMB'000 |
| **Balance at January 1, 2018** | | 150 | 742,760 | 947,420 | (128,962,691) | (127,272,361) | 61,670 | (127,210,691) |
| **Comprehensive income** | | | | | | | | |
| Profit for the year | | – | – | – | 13,553,886 | 13,553,886 | (76,139) | 13,477,747 |
| **Other comprehensive income** | | | | | | | | |
| *Items that may be reclassified subsequently to profit or loss* | | | | | | | | |
| Share of other comprehensive income of investments accounted for using the equity method | 11(b) | – | – | 191,449 | – | 191,449 | – | 191,449 |
| Currency translation differences | 26 | – | – | (657,274) | – | (657,274) | 8,528 | (648,746) |
| *Item that will not be reclassified subsequently to profit or loss* | | | | | | | | |
| Currency translation differences | 26 | – | – | (1,098,818) | – | (1,098,818) | – | (1,098,818) |
| **Total comprehensive income** | | – | – | (1,564,643) | 13,553,886 | 11,989,243 | (67,611) | 11,921,632 |
| **Transactions with owners in their capacity as owners** | | | | | | | | |
| Issuance of ordinary shares | 25 | 11 | 9,827,146 | – | – | 9,827,157 | – | 9,827,157 |
| Issuance of ordinary shares relating to initial public offering, net of underwriting commissions and other issuance costs | 25 | 27 | 23,248,593 | – | – | 23,248,620 | – | 23,248,620 |
| Release of ordinary shares from Share Scheme Trust | 25 | 15 | 933,592 | (841,640) | – | 91,967 | – | 91,967 |
| Conversion of convertible redeemable preferred shares to ordinary shares | 35 | 174 | 151,100,334 | – | – | 151,100,508 | – | 151,100,508 |
| Share of other reserves of investments accounted for using the equity method | 11(b) | – | – | 62,657 | – | 62,657 | – | 62,657 |
| Employees share-based compensation scheme: | | | | | | | | |
| – value of employee services | 28 | – | – | 2,358,720 | – | 2,358,720 | 102,805 | 2,461,525 |
| Acquisition of additional equity interests in non-wholly owned subsidiaries | | – | 230,899 | (152,071) | (162,046) | (83,218) | (171,220) | (254,438) |
| Appropriation to statutory reserves | 26 | – | – | 57,808 | (57,808) | – | – | – |
| Share premium set off the accumulated losses and other reserves | 25 | – | (142,232,042) | 5,579,472 | 136,652,570 | – | – | – |
| Others | | – | – | (308) | – | (308) | 1,500 | 1,192 |
| **Total transactions with owners in their capacity as owners** | | 227 | 43,108,522 | 7,064,638 | 136,432,716 | 186,606,103 | (66,915) | 186,539,188 |
| **Balance at December 31, 2018** | | 377 | 43,851,282 | 6,447,415 | 21,023,911 | 71,322,985 | (72,856) | 71,250,129 |

*The notes on pages 191 to 325 are an integral part of these consolidated financial statements.*

# CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended December 31, 2019

(Expressed in RMB)

| | Note | Year ended December 31, 2019 RMB'000 | 2018 RMB'000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Cash generated from operations | 36(a) | 25,952,239 | 122,171 |
| Income tax paid | | (2,141,885) | (1,536,742) |
| Net cash generated from/(used in) operating activities | | 23,810,354 | (1,414,571) |
| **Cash flows from investing activities** | | | |
| Capital expenditures | | (3,405,163) | (3,785,259) |
| Proceeds from disposal of property and equipment | 36(b) | 67,735 | 27,367 |
| Placement of short-term bank deposits | | (25,728,849) | (2,060,799) |
| Withdrawal of short-term bank deposits | | 5,525,882 | 903,504 |
| Placement of long-term bank deposits | | (590,157) | — |
| Purchase of short-term investments measured at fair value through profit or loss | | (134,409,027) | (140,955,400) |
| Receipt from maturity of short-term investments measured at fair value through profit or loss | | 124,632,553 | 139,154,171 |
| Purchase of short-term investments measured at amortized cost | | — | (3,500,000) |
| Receipt from maturity of short-term investments measured at amortized cost | | — | 4,300,000 |
| Interest income received | | 864,226 | 489,816 |
| Investment income received | | 386,461 | 335,695 |
| Purchase of long-term investments measured at fair value through profit or loss | | (3,987,225) | (1,999,752) |
| Proceeds from disposal of long-term investments measured at fair value through profit or loss | | 4,846,175 | 304,999 |
| Purchase of investments accounted for using the equity method | | (200,000) | (793,595) |
| Proceeds from disposal of investments accounted for using the equity method | | 80,048 | — |
| Disposal of a subsidiary | | — | (25,655) |
| Acquisition of a subsidiary, net of cash acquired | | — | (34,936) |
| Dividends received | | 347,205 | 131,804 |
| Net cash used in investing activities | | (31,570,136) | (7,508,040) |

# CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended December 31, 2019

(Expressed in RMB)

| | Note | Year ended December 31, 2019 RMB'000 | 2018 RMB'000 |
|---|---|---|---|
| **Cash flows from financing activities** | | | |
| Proceeds from borrowings | | 17,036,724 | 10,269,415 |
| Repayment of borrowings | | (10,417,425) | (10,505,637) |
| Finance expenses paid | | (218,994) | (243,966) |
| Placement of restricted cash | | — | (4,152,345) |
| Withdrawal of restricted cash | | 75,773 | 5,059,245 |
| Payment for acquisition of non-controlling interests in a non-wholly owned subsidiary | | (187,000) | (165,000) |
| Proceeds from fund investors | | — | 2,781,000 |
| Net proceeds from issuance of ordinary shares relating to the initial public offering | | — | 23,248,620 |
| Net proceeds from exercise of share options | | 186,838 | — |
| Payments for shares repurchase | | (2,932,111) | — |
| Payment of lease liabilities | | (578,063) | — |
| Capital contribution from non-controlling interests | | 155,496 | — |
| Proceeds from release of ordinary shares from Share Scheme Trust | | — | 91,967 |
| Others | | — | 190,873 |
| Net cash generated from financing activities | | 3,121,238 | 26,574,172 |
| **Net (decrease)/increase in cash and cash equivalents** | | (4,638,544) | 17,651,561 |
| Cash and cash equivalents at the beginning of the year | 24(a) | 30,230,147 | 11,563,282 |
| Effects of exchange rate changes on cash and cash equivalents | | 328,258 | 1,015,304 |
| **Cash and cash equivalents at the end of the year** | 24(a) | 25,919,861 | 30,230,147 |

*The notes on pages 191 to 325 are an integral part of these consolidated financial statements.*

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 1 General information

Xiaomi Corporation (formerly known as Top Elite Limited) (the "**Company**"), was incorporated in the Cayman Islands on January 5, 2010 as an exempted company with limited liability under the Companies Law, Cap. 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands. The address of the Company's registered office is at the offices of Maples Corporate Services Limited, PO Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands.

The Company is an investment holding company. The Company and its subsidiaries, including controlled structured entities (together, the "**Group**") are principally engaged in development and sales of smartphones, internet of things ("**IoT**") and lifestyle products, provision of internet services and investments holding in the People's Republic of China and other countries or regions.

Lei Jun is the ultimate controlling shareholder of the Company as of the date of approval of these consolidated financial statements.

The regulations in mainland China restrict foreign ownership of companies that provide internet services, e-commerce and value-added telecommunications services, etc., which include certain activities and services operated by the Group. In order to enable certain foreign companies to make investments into these businesses of the Group, the Company controls certain subsidiaries through contractual arrangements. On August 25, 2010, a wholly owned subsidiary of the Company, Xiaomi Communications Co., Ltd. ("**Xiaomi Communications**", a wholly foreign-owned enterprise) had entered into a series of contractual arrangements (the "**Contractual Arrangements**") with Xiaomi Inc. and its equity holders, which enable Xiaomi Communications and the Group to:

- govern the financial and operating policies of Xiaomi Inc.;
- exercise equity holders' voting rights of Xiaomi Inc.;
- receive substantially all of the economic interest returns generated by Xiaomi Inc. in consideration for the business support, technical and consulting services provided by Xiaomi Communications;
- obtain an irrevocable and exclusive right to purchase all or part of the equity interests in Xiaomi Inc. from the respective equity holders at a minimum purchase price when it is permitted under laws and regulations in mainland China. Xiaomi Communications may exercise such options at any time until it has acquired all equity interests of Xiaomi Inc.; and

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 1 General information (continued)

- obtain a pledge over the entire equity interests of Xiaomi Inc. from its respective equity holders as collateral security for all of Xiaomi Inc.'s payments due to Xiaomi Communications and to secure performance of Xiaomi Inc.'s obligation under the Contractual Arrangements.

As a result of the Contractual Arrangements, the Group has rights to exercise power over Xiaomi Inc. and its subsidiaries, receives variable returns from its involvement in Xiaomi Inc. and its subsidiaries, has the ability to affect those returns through its power over Xiaomi Inc. and its subsidiaries and is considered to control Xiaomi Inc. and its subsidiaries. Consequently, the Company regards Xiaomi Inc. and its subsidiaries as controlled structured entities and consolidated the assets, liabilities and results of operations of Xiaomi Inc. and its subsidiaries in the consolidated financial information of the Group.

Nevertheless, the Contractual Arrangements may not be as effective as direct legal ownership in providing the Group with direct control over Xiaomi Inc. and its subsidiaries. Uncertainties presented by the legal system in mainland China could impede the Group's beneficiary rights of the results, assets and liabilities of Xiaomi Inc. and its subsidiaries. The directors of the Company, based on the advice of its legal counsel, consider that the Contractual Arrangements among Xiaomi Communications, Xiaomi Inc. and its equity holders are in compliance with the relevant laws and regulations in mainland China and are legally binding and enforceable.

Other Contractual Arrangements were also executed for other operating companies in mainland China established by the Group similar to Xiaomi Inc. subsequently. All of these operating companies are treated as controlled structured entities of the Company and their financial statements have also been consolidated by the Company. See details in Note 11(a).

## 2 Summary of significant accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied throughout all the years presented, unless otherwise stated.

### 2.1 Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with all applicable International Financial Reporting Standards ("**IFRSs**") issued by International Accounting Standards Board ("**IASB**") and disclosure requirements of the Hong Kong Companies Ordinance.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.1 Basis of preparation (continued)

The consolidated financial statements of the Group have been prepared under the historical cost convention, as modified by the revaluation of financial assets and financial liabilities which are carried at fair value.

The preparation of consolidated financial statements in conformity with IFRSs requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

**(a) New and amended standards adopted by the Group**

The following new and amended standards, and annual improvements are mandatory for the first time for the Group's financial year beginning on January 1, 2019 and are applicable for the Group:

- IFRS 16 Leases ("**IFRS 16**")
- IFRIC 23 Uncertainty over income tax treatments
- Amendments to IAS 19 Employee benefits on plan amendment, curtailment or settlement
- Amendments to IFRS Annual Improvements to IFRSs Standards 2015–2017 Cycle
- Amendments to IAS 28 Long-term interests in associates and joint ventures
- Amendment to IFRS 9 Prepayment features with negative compensation

The adoption of these interpretation and amendments to standards has had no significant impact on the results and the financial position of the Group other than IFRS 16, details of which are set out in Note 2.2.

**(b) New standards and interpretations not yet adopted**

Certain new accounting standards and interpretations have been published that are not mandatory for the year ended December 31, 2019 and have not been early adopted by the Group. These standards are not expected to have a material impact on the Group in the current or future reporting periods and on foreseeable future transactions.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.2 Changes in accounting policies

This note explains the impact of the adoption of IFRS 16 on the Group's consolidated financial statements.

As indicated in Note 2.1, the Group has adopted IFRS 16 from January 1, 2019. The Group has applied IFRS 16 using the simplified transition approach and has not restated comparatives for the 2018 reporting period as permitted under the specific transition provisions in the standard. The reclassifications and the adjustments arising from the new leasing rules are therefore recognized in the opening balance sheet on January 1, 2019. The new accounting policies are disclosed in Note 2.33.

On adoption of IFRS 16, the Group recognized lease liabilities in relation to leases which had previously been classified as 'operating leases' under the principles of IAS 17 Leases. These liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate as of January 1, 2019. The weighted average lessee's incremental borrowing rate applied to the lease liabilities on January 1, 2019 was 5.16% per annum.

All right-of-use assets were measured at the amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognized in the consolidated balance sheet immediately before the adoption of the IFRS 16. As a result of the adoption of IFRS 16, as of January 1, 2019, the Group recognized a right-of-use asset of RMB4,281,939,000 in other non-current assets, and lease liabilities of RMB285,402,000 and RMB573,431,000 in other payables and accruals and other non-current liabilities, respectively. The impact on transition also included a decrease of RMB52,987,000 in prepayments and other receivables, a decrease of RMB3,389,731,000 in land use rights and a decrease of RMB19,612,000 in other payables and accruals as a result of the adjustment of prepaid or accrued lease payments. On adoption of IFRS 16, the Group reclassified the land use rights to right-of-use assets, which represent the prepaid operating lease payments.

In applying IFRS 16 for the first time, the Group has used the following practical expedients permitted by the standard:

- the use of a single discount rate to a portfolio of leases with reasonably similar characteristics;
- account for operating leases with a remaining lease term of less than 12 months as of January 1, 2019 in the same way as short-term leases; and
- the exclusion of initial direct costs for the measurement of the right-of-use asset at the date of initial application.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.2 Changes in accounting policies (continued)

The reconciliation between the operating lease commitments disclosed as of December 31, 2018 and the lease liability recognized as of January 1, 2019 is as follows:

| | RMB'000 |
|---|---|
| Operating lease commitments disclosed as of December 31, 2018 | 1,029,240 |
| Discounted using the Group's incremental borrowing rate of 5.16% | 979,755 |
| Less: short-term leases recognized on a straight-line basis as expense | (258,968) |
| Add: adjustments as a result of a different treatment of extension and termination options and others | 138,046 |
| Lease liabilities recognized as of January 1, 2019 | 858,833 |

In addition, upon adoption of IFRS 16, principal elements of lease payments and related interest portion have been classified within financing activities in the consolidated statement of cash flows.

### 2.3 Subsidiaries

#### 2.3.1 Consolidation

A subsidiary is an entity (including a structured entity) over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases.

Intra-group transactions, balances and unrealized gains on transactions between group companies are eliminated. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the transferred asset. When necessary, amounts reported by subsidiaries have been adjusted to conform with the Group's accounting policies.

(a) **Subsidiaries controlled through Contractual Arrangements**

There are entities controlled by the Group under Contractual Arrangements. The Group does not have legal ownership in equity of these structured entities or their subsidiaries. Nevertheless, under Contractual Arrangements entered into with the registered owners of these structured entities, the Company and its other legally owned subsidiaries control these companies by way of controlling the voting rights, governing their financial and operating policies, appointing or removing the majority of the members of their controlling authorities, and casting the majority of votes at meetings of such authorities. Accordingly, the Group has rights to exercise power over these structured entities, receives variable returns from its involvement in these structured entities, and has the ability to affect those returns through its power over these structured entities. As a result, they are presented as controlled structured entities of the Group, and their assets, liabilities and results are consolidated in the Group's consolidated financial statements.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.3 Subsidiaries (continued)

#### 2.3.1 Consolidation (continued)

**(b) Business combination**

The Group applies the acquisition method to account for business combinations except for business combination under common control. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date.

The Group recognizes any non-controlling interest in the acquiree on an acquisition-by-acquisition basis either at fair value or at the non-controlling interest's proportionate share of the acquiree's net identifiable assets.

Acquisition-related costs are expensed as incurred.

If the business combination is achieved in stages, the acquisition date carrying value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date; any gains or losses arising from such remeasurement are recognized in profit or loss.

Any contingent consideration to be transferred by the Group is recognized at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration that is deemed to be an asset or liability is recognized in accordance with IFRS 9 in profit or loss. Contingent consideration that is classified as equity is not remeasured, and its subsequent settlement is accounted for within equity.

The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired is recorded as goodwill. If those amounts are less than the fair value of the net assets of the business acquired in the case of a bargain purchase, the difference is recognized directly in the profit or loss.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

# 2 Summary of significant accounting policies (continued)

## 2.3 Subsidiaries (continued)

### 2.3.1 Consolidation (continued)

**(b) Business combination (continued)**

An acquisition of a business which is a business combination under common control is accounted for in a manner similar to a uniting of interests whereby the assets and liabilities acquired are accounted for at carryover predecessor values to the other party to the business combination within all periods presented as if the operations of the Group and the business acquired have always been combined. The difference between the consideration paid by the Group and the net assets or liabilities of the business acquired is adjusted against equity.

**(c) Changes in ownership interests in subsidiaries without change of control**

Transactions with non-controlling interests that do not result in a loss of control are accounted for as equity transactions — that is, as transactions with the owners of the subsidiary in their capacity as owners. The difference between fair value of any consideration paid and the relevant share of the carrying amount of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

**(d) Disposal of subsidiaries**

When the Group ceases to have control, any retained interest in the entity is re-measured to its fair value at the date when control is lost, with the change in carrying amount recognized in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognized in other comprehensive income in respect of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities. It means the amounts previously recognized in other comprehensive income ("**OCI**") are reclassified to profit or loss, or transferred to another category of equity as specified/permitted by applicable IFRSs.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.3 Subsidiaries (continued)

#### 2.3.2 Separate financial statements

Investments in subsidiaries (including controlled structured entities) are accounted for at cost less impairment. Cost includes direct attributable costs of investment. The results of subsidiaries are accounted for by the Company on the basis of dividend received and receivable.

Impairment testing of the investments in subsidiaries is required upon receiving a dividend from these investments if the dividend exceeds the total comprehensive income of the subsidiary in the period the dividend is declared or if the carrying amount of the investment in the separate financial statements exceeds the carrying amount in the consolidated financial information of the investee's net assets including goodwill.

### 2.4 Associates

An associate is an entity over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights.

#### (a) Investments in associates in the form of ordinary shares

Investments in associates in the form of ordinary shares are accounted for using the equity method of accounting in accordance with IAS 28 "Investments in Associates and Joint Ventures". Under the equity method, the investment is initially recognized at cost, and the carrying amount is increased or decreased to recognize the investor's share of the profit or loss of the investee after the date of acquisition. The Group's investments in these associates include goodwill identified on acquisition, net of any accumulated impairment loss. Upon the acquisition of the ownership interest in an associate, any difference between the cost of the associate and the Group's share of the net fair value of the associate's identifiable assets and liabilities is accounted for as goodwill.

If the ownership interest in an associate in the form of ordinary shares is reduced but significant influence is retained, only a proportionate share of the amounts previously recognized in other comprehensive income is reclassified to consolidated income statement where appropriate.

The Group's share of the associates' post-acquisition profit or loss is recognized in the consolidated income statement, and its share of post-acquisition movements in other comprehensive income is recognized in other comprehensive income. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognize further losses, unless it has incurred legal or constructive obligations or made payments on behalf of the associate.

## 2 Summary of significant accounting policies (continued)

### 2.4 Associates (continued)

#### (a) Investments in associates in the form of ordinary shares (continued)

The Group determines at each reporting date whether there is any objective evidence that the investments in the associate are impaired. If this is the case, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and includes the amount in "other (losses)/gains, net" in the consolidated income statement.

Profits and losses resulting from upstream and downstream transactions between the Group and its associate are recognized in the Group's financial statements only to the extent of unrelated investor's interests in the associates. Unrealized losses are eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

Gain or losses on dilution of equity interest in associates are recognized in the consolidated income statement.

#### (b) Investments in associates in the form of ordinary shares with preferential rights or convertible redeemable preferred shares

Investments in associates in the form of ordinary shares with preferential rights or convertible redeemable preferred shares are accounted as financial assets measured at fair value through profit or loss (Note 2.12).

### 2.5 Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker ("**CODM**"). The CODM, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Chief Executive Officer that makes strategic decisions.

### 2.6 Foreign currency translation

#### (a) Functional and presentation currency

Items included in the financial information of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "**functional currency**"). The functional currency of the Company is United States dollar ("**US$**"). The Company's primary subsidiaries were incorporated in mainland China and these subsidiaries considered RMB as their functional currency. As the major operations of the Group are within mainland China, the Group determined to present its consolidated financial statements in RMB (unless otherwise stated).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.6 Foreign currency translation (continued)

**(b) Transactions and balances**

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where items are re-measured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the consolidated income statement. Foreign exchange gains and losses are presented in the consolidated income statement within "other (losses)/gains, net".

Translation differences on non-monetary financial assets and liabilities are recognized in profit or loss as part of the fair value changes.

**(c) Group companies**

The results and financial position of all the Group entities (none of which has the currency of a hyper-inflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions); and
- all resulting currency translation differences are recognized in other comprehensive income.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate. Currency translation differences arising are recognized in other comprehensive income.

**(d) Disposal of foreign operation and partial disposal**

On the disposal of a foreign operation (that is, a disposal of the Group's entire interest in a foreign operation, or a disposal involving loss of control over a subsidiary that includes a foreign operation, a disposal involving loss of joint control over a joint venture that includes a foreign operation, or a disposal involving loss of significant influence over an associate that includes a foreign operation), all of the currency translation differences accumulated in equity in respect of that operation attributable to the owners of the Company are reclassified to profit or loss.

## 2 Summary of significant accounting policies (continued)

### 2.6 Foreign currency translation (continued)

**(d) Disposal of foreign operation and partial disposal (continued)**

In the case of a partial disposal that does not result in the Group losing control over a subsidiary that includes a foreign operation, the proportionate share of accumulated currency translation differences are re-attributed to non-controlling interests and are not recognized in profit or loss. For all other partial disposals (that is, reductions in the Group's ownership interest in associates or joint ventures that do not result in the Group losing significant influence or joint control), the proportionate share of the accumulated exchange difference is reclassified to profit or loss.

### 2.7 Property and equipment

Property and equipment are stated at historical cost less accumulated depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are charged to profit or loss during the financial period in which they are incurred.

Depreciation on property and equipment is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

| | |
|---|---|
| — Leasehold improvements | Estimated useful lives or remaining lease terms, whichever is shorter |
| — Electronic equipment | 3 years |
| — Office equipment | 3–5 years |
| — Buildings | 40 years |

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

Construction in progress mainly represents office buildings under construction, which is stated at actual construction cost less accumulated impairment losses. Construction in progress is transferred to appropriate categories of property and equipment upon the completion of their respective construction and depreciated over their respective estimated useful lives.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2.11).

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognized within "other (losses)/gains, net" in the consolidated income statement.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.8 Land use rights

Land use rights represent prepayments for the land use rights in mainland China and are stated at cost initially and expensed on a straight-line basis over the periods of the leases.

### 2.9 Investment properties

Investment properties, principally freehold office buildings, are held for long-term rental yields and are not occupied by the Group. Investment properties are initially measured at cost, including related transaction costs and where applicable borrowing costs. Subsequently, investment properties are stated at cost less accumulated depreciation and accumulated impairment losses (if any). Depreciation is recognized so as to write off the cost of investment properties to their residual values over their estimated useful lives of 40 years by using the straight-line method.

### 2.10 Intangible assets

#### (a) Goodwill

Goodwill arises from the acquisition of subsidiaries represents the excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identified net assets acquired.

For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the cash-generating units ("**CGUs**"), or groups of CGUs, that is expected to benefit from the synergies of the combination. Each unit or group of units to which the goodwill is allocated represents the lowest level within the entity at which the goodwill is monitored for internal management purposes. Goodwill is monitored at the operating segment level.

Goodwill impairment reviews are undertaken annually or more frequently if events or changes in circumstances indicate a potential impairment. The carrying value of the CGU containing the goodwill is compared to the recoverable amount, which is the higher of value in use and the fair value less costs of disposal. Any impairment is recognized immediately as an expense and is not subsequently reversed.

#### (b) License

License includes third-party payment license and other licenses. Third-party payment license represents the license issued by the People's Republic of China government authorities that enable the Group to operate third-party payment business. Other licenses mainly include the licenses to use certain intellectual properties purchased from third parties. These acquired licenses are shown at historical cost. License that have an indefinite useful life are tested annually for impairment and carried at cost less accumulated impairment losses. Others are amortized over their estimated useful lives of 1 to 10 years using straight-line method.

## 2 Summary of significant accounting policies (continued)

### 2.10 Intangible assets (continued)

(c) **Trademarks, patents and domain name**

Separately acquired trademarks, patents and domain name are shown at historical cost. Trademarks, patents and domain name acquired in a business combination are recognized at fair value at the acquisition date. Trademarks, patents and domain name have a finite useful life and are carried at cost less accumulated amortization. Amortization is calculated using the straight-line method to allocate the cost of trademarks, patents and domain name over their estimated useful lives of 1 to 16 years.

(d) **Other intangible assets**

Other intangible assets mainly include computer software. They are initially recognized and measured at costs incurred to acquire and bring them to use. Other intangible assets are amortized on a straight-line basis over their estimated useful lives, and recorded in amortization within operating expenses in the consolidated income statement.

(e) **Research and development expenditures**

Research expenditure is recognized as an expense as incurred. Costs incurred on development projects (relating to the design and testing of new or improved products) are capitalized as intangible assets when recognition criteria are fulfilled. These criteria include:

- it is technically feasible to complete the software product so that it will be available for use;
- management intends to complete the software product and use or sell it;
- there is an ability to use or sell the software product;
- it can be demonstrated how the software product will generate probable future economic benefits;
- adequate technical, financial and other resources to complete the development and to use or sell the software product are available; and
- the expenditure attributable to the software product during its development can be reliably measured.

Other development expenditures that do not meet these criteria are recognized as an expense as incurred.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.11 Impairment of non-financial assets

Intangible assets that have an indefinite useful life are not subject to amortization and are tested annually for impairment. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

### 2.12 Financial assets

#### 2.12.1 Classification

The Group classifies its financial assets in the following measurement categories:

- those to be measured subsequently at fair value (either through other comprehensive income, or through profit or loss), and

- those to be measured at amortized cost.

The classification depends on the Group's business model for managing the financial assets and the contractual terms of the cash flows.

For assets measured at fair value, gains and losses will either be recorded in profit or loss or other comprehensive income. For investments in debt instruments, this will depend on the business model in which the investment is held. For investments in equity instruments that are not held for trading, this will depend on whether the Group has made an irrevocable election at the time of initial recognition to account for the equity investment at fair value through other comprehensive income.

See Note 18 for details of each type of financial asset.

The Group reclassifies debt investments when and only when its business model for managing those assets changes.

#### 2.12.2 Measurement

At initial recognition, the Group measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at fair value through profit or loss are recorded in profit or loss.

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.12 Financial assets (continued)

#### 2.12.2 Measurement (continued)

***Debt instruments***

Subsequent measurement of debt instruments depends on the Group's business model for managing the asset and the cash flow characteristics of the asset. There are three measurement categories into which the Group classifies its debt instruments:

- Amortized cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortized cost. A gain or loss on a debt investment that is subsequently measured at amortized cost and is not part of a hedging relationship is recognized in profit or loss when the asset is derecognized or impaired. Interest income from these financial assets is included in finance income using the effective interest method.

- Fair value through other comprehensive income ("**FVOCI**"): Assets that are held for collection of contractual cash flows and for selling the financial assets, where the assets' cash flows represent solely payments of principal and interest, are measured at FVOCI. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest income and foreign exchange gains and losses which are recognized in profit or loss. When the financial asset is derecognized, the cumulative gain or loss previously recognized in OCI is reclassified from equity to profit or loss and recognized in other (losses)/gains, net. Interest income from these financial assets is included in finance income using the effective interest method. Foreign exchange gains and losses are presented in other (losses)/gains, net.

- Fair value through profit or loss ("**FVPL**"): Assets that do not meet the criteria for amortized cost or FVOCI are measured at FVPL. A gain or loss on a debt investment that is subsequently measured at FVPL and is not part of a hedging relationship is recognized in profit or loss and presented net in the consolidated income statement within other (losses)/gains, net in the period in which it arises.

***Equity instruments***

The Group subsequently measures all equity investments at fair value. Where the Group's management has elected to present fair value gains and losses on equity investments in OCI, there is no subsequent reclassification of fair value gains and losses to profit or loss following the derecognition of the investment. Dividends from such investments continue to be recognized in profit or loss as other income when the Group's right to receive payments is established.

Changes in the fair value of financial assets at FVPL are recognized in the consolidated income statement. Impairment losses (and reversal of impairment losses) on equity investments measured at FVOCI are not reported separately from other changes in fair value.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.12 Financial assets (continued)

#### 2.12.3 Impairment

The Group has types of financial assets subject to IFRS 9's new expected credit loss model:

- loan receivables from fintech business;
- trade receivables for sales of goods or provision of services; and
- other receivables

The Group assesses on a forward looking basis the expected credit losses associated with its debt instruments carried at amortized cost including loan receivables, and with the exposure arising from financial guarantee contracts. The impairment methodology applied depends on whether there has been a significant increase in credit risk. Note 3.1(b) details how the Group determines whether there has been a significant increase in credit risk.

For trade receivables, the Group applies the simplified approach permitted by IFRS 9, which requires expected lifetime losses to be recognized from initial recognition of the receivables.

Impairment on other receivables is measured as either 12-month expected credit losses or lifetime expected credit loss, depending on whether there has been a significant increase in credit risk since initial recognition. If a significant increase in credit risk of a receivable has occurred since initial recognition, then impairment is measured as lifetime expected credit losses.

#### 2.12.4 Derecognition

*Financial assets*

The Group derecognizes a financial asset, if the part being considered for derecognition meets one of the following conditions: (i) the contractual rights to receive the cash flows from the financial asset expire; or (ii) the contractual rights to receive the cash flows of the financial asset have been transferred, the Group transfers substantially all the risks and rewards of ownership of the financial asset; or (iii) the Group retains the contractual rights to receive the cash flows of the financial asset, but assumes a contractual obligation to pay the cash flows to the eventual recipient in an agreement that meets all the conditions of de-recognition of transfer of cash flows ("**pass through**" requirements) and transfers substantially all the risks and rewards of ownership of the financial asset.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.12 Financial assets (continued)

#### 2.12.4 Derecognition (continued)

*Financial assets (continued)*

Where a transfer of a financial asset in its entirety meets the criteria for derecognition, the difference between the two amounts below is recognized in profit or loss:

- the carrying amount of the financial asset transferred; and

- the sum of the consideration received from the transfer and any cumulative gain or loss that has been recognized directly in equity.

If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group continues to recognize the asset to the extent of its continuing involvement and recognizes an associated liability.

*Asset-backed securities*

As part of its operations, the Group securitizes financial assets, generally through the sale of these assets to special purpose vehicles which issue securities to investors. Further details on prerequisites for derecognition of financial assets are set out above. When the securitization of financial assets that qualify for derecognition, the relevant financial assets are derecognized in their entirety and a new financial asset or liabilities is recognized regarding the interest in the unconsolidated securitization vehicles that the Group acquired. When the securitization of financial assets that do not qualify for derecognition, the relevant financial assets are not derecognized, and the consideration paid by third parties are recorded as a financial liability; when the securitization of financial assets that partially qualify for derecognition, the book value of the transferred asset should be recognized between the derecognized portion and the retained portion based on their respective relative fair values, and the difference between the book value of the derecognized portion and the total consideration received from the derecognized portion shall be recorded in profit or loss.

*Other financial liabilities*

A financial liability is derecognized when the obligation under the liability is discharged, canceled, or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and a recognition of a new liability, and the difference between the respective carrying amounts is recognized in profit or loss.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.13 Financial guarantee contracts

Financial guarantee contracts are recognized as a financial liability at the time the guarantee is issued. The liability is initially measured at fair value and subsequently at the higher of:

- the amount determined in accordance with the expected credit loss model under IFRS 9 and
- the amount initially recognized less, where appropriate, the cumulative amount of income recognized in accordance with the principles of IFRS 15.

The fair value of financial guarantees is determined based on the present value of the difference in cash flows between the contractual payments required under the debt instrument and the payments that would be required without the guarantee, or the estimated amount that would be payable to a third party for assuming the obligations.

Where guarantees in relation to loans or other payables of associates are provided for no compensation, the fair values are accounted for as contributions and recognized as part of the cost of the investment.

### 2.14 Inventories

Inventories are stated at the lower of cost and net realizable value. Cost is determined using the weighted average method. The cost of finished goods and work in progress comprises raw materials, assembly cost and other direct costs. It excludes borrowing costs. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs to completion, applicable variable selling expense and related tax.

### 2.15 Trade and other receivables

Trade receivables are amounts due from customers for goods sold or services performed in the ordinary course of business. Majority of other receivables are amounts due from outsourcing partners for raw material delivered in the ordinary course of business and value-added tax and other tax recoverable. They are generally due for settlement within one year and therefore all classified as current.

Trade and other receivables are recognized initially at the amount of consideration that is unconditional unless they contain significant financing components, when they are recognized at fair value. The Group holds the trade and other receivables with the objective of collecting the contractual cash flows and therefore measures them subsequently at amortized cost using the effective interest method. See Note 2.12.3 for a description of the Group's impairment policies for trade and other receivables.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.16 Loan receivables

Loan receivables held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are recognized initially at fair value plus transaction costs that are attributable to the acquisition of the assets and subsequently measured at amortized cost using the effective interest method, less credit loss allowance. Amortized cost is calculated by taking into account any discount or premium on acquisition and includes fees or costs that are an integral part of the effective interest rate. The effective interest rate amortization is included in the profit or loss. The loss allowance is recognized in profit or loss. See Note 2.12.3 for a description of the Group's impairment policy for loan receivables.

### 2.17 Cash and cash equivalents

In the consolidated statement of cash flows, cash and cash equivalents includes cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less.

### 2.18 Share capital

Ordinary shares are classified as equity. Convertible redeemable preferred shares are classified as liabilities (see Note 2.20).

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction from the proceeds.

### 2.19 Trade payables

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Trade payables are classified as current liabilities if payment is due within one year (or in the normal operating cycle of the business if longer). If not, they are presented as non-current liabilities.

Trade payables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.20 Convertible redeemable preferred shares

Convertible redeemable preferred shares ("**Preferred Shares**") issued by the Company are redeemable at the option of the holders at any time commencing on the redemption start date of December 23, 2019. This instrument can be converted into Class B ordinary shares of the Company at the option of a holder after July 3, 2015, or automatically converted into ordinary shares upon occurrence of (i) the closing of a Qualified Public Offering ("**QPO**"), or (ii) with written consent of holders of more than fifty percent (50%) of the issued and outstanding Series A Preferred Shares, or written consent of holders of more than two thirds (2/3) of the issued and outstanding Preferred Shares (other than Series A Preferred Shares).

The Group designated the Preferred Shares as financial liabilities at fair value through profit or loss. They are initially recognized at fair value. Any directly attributable transaction costs are recognized as finance costs in the consolidated income statement.

Subsequent to initial recognition, the Preferred Shares are carried at fair value with changes in fair value recognized in the consolidated income statement.

The Preferred Shares are classified as non-current liabilities if the Preferred Shares holders cannot demand the Company to redeem the Preferred Shares for at least 12 months after the end of the reporting period.

### 2.21 Borrowings

Borrowings are recognized initially at fair value, net of transaction costs incurred. Borrowings are subsequently carried at amortized cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the consolidated income statement over the period of the borrowings using the effective interest method.

Fees paid on the establishment of loan facilities are recognized as transaction costs of the loan to the extent that it is probable that some or all of the facility will be drawn down. In this case, the fee is deferred until the draw-down occurs. To the extent there is no evidence that it is probable that some or all of the facility will be drawn down, the fee is capitalized as a pre-payment for liquidity services and amortized over the period of the facility to which it relates.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the end of the reporting period.

## 2 Summary of significant accounting policies (continued)

### 2.22 Borrowing costs

General and specific borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalization.

All other borrowing costs are recognized in profit or loss in the period in which they are incurred.

### 2.23 Dividend distribution

Dividend distribution to the Company's shareholders is recognized as a liability in the Group's financial statements in the period in which the dividends are approved by the Company's shareholders or directors, where appropriate.

### 2.24 Current and deferred income tax

The income tax expense for the period comprises current and deferred tax. Income tax is recognized in the consolidated income statement, except to the extent that it relates to items recognized in other comprehensive income or directly in equity. In this case, the income tax is also recognized in other comprehensive income or directly in equity, respectively.

#### (a) Current income tax

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the Company and its subsidiaries operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.24 Current and deferred income tax (continued)

(b) **Deferred income tax**

*Inside basis differences*

Deferred income tax is recognized, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax liabilities are not recognized if they arise from the initial recognition of goodwill, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred income tax assets are recognized only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

*Outside basis differences*

Deferred income tax liabilities are provided on taxable temporary differences arising from investments in subsidiaries, associates and joint arrangements, except for deferred income tax liability where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future. Generally the Group is unable to control the reversal of the temporary difference for associates. Only when there is an agreement in place that gives the Group the ability to control the reversal of the temporary difference in the foreseeable future, deferred tax liability in relation to taxable temporary differences arising from the associate's undistributed profits is not recognized.

Deferred income tax assets are recognized on deductible temporary differences arising from investments in subsidiaries and associates only to the extent that it is probable the temporary difference will reverse in the future and there is sufficient taxable profit available against which the temporary difference can be utilized.

(c) **Offsetting**

Deferred income tax assets and liabilities are offset where there is a legally enforceable right to offset current income tax assets against current income tax liabilities and where the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.25 Employee benefits

(a) **Pension obligations**

The Group operates a mandatory provident fund scheme ("**MPF Scheme**") for the eligible employees in Hong Kong. The MPF Scheme is a defined contribution scheme, the assets of which are held in separate trustee — administered funds. The Group's contributions to MPF Scheme are expensed as incurred.

The Group's subsidiaries operating in mainland China have to make contribution to staff retirement scheme managed by local government authorities in accordance with the relevant rules and regulations. Contributions to these schemes are charged to the consolidated income statement as and when incurred and not reduced by contributions forfeited by those who leave the plans prior to vesting fully in the contributions. The Group has no legal or constructive obligations to pay further contributions.

(b) **Employee leave entitlements**

Employee entitlements to annual leave are recognized when they accrue to employees. A provision is made for the estimated liability for annual leave as a result of services rendered by employees up to the balance sheet date. Employee entitlements to sick leave and maternity leave are not recognized until the time of leave.

(c) **Bonus plans**

The expected cost of bonuses is recognized as a liability when the Group has a present legal or constructive obligation for payment of bonus as a result of services rendered by employees and a reliable estimate of the obligation can be made. Liabilities for bonus plans are expected to be settled within 1 year and are measured at the amounts expected to be paid when they are settled.

### 2.26 Share-based payment

(a) **Equity-settled share-based payment transactions**

The Group operates share incentive plan, under which it receives services from employees as consideration for equity instruments (restricted shares units ("**RSUs**") and options) of the Company. The fair value of the services received in exchange for the grant of the equity instruments (RSUs and options) is recognized as an expense on the consolidated income statement with a corresponding increase in equity.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.26 Share-based payment (continued)

**(a) Equity-settled share-based payment transactions (continued)**

In terms of the RSUs and options awarded to employees, the total amount to be expensed is determined by reference to the fair value of equity instruments (RSUs and options) granted:

- including any market performance conditions;
- excluding the impact of any service and non-market performance vesting conditions; and
- including the impact of any non-vesting conditions.

Service and non-marketing performance conditions are included in calculation of the number of RSUs and options that are expected to vest. The total amount expensed is recognized over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied.

At the end of each reporting period, the Group revises its estimates of the number of RSUs and options that are expected to vest based on the non-marketing performance and service conditions. It recognizes the impact of the revision to original estimates, if any, in the consolidated income statement, with a corresponding adjustment to equity.

In some circumstances, employees may provide services in advance of the grant date and therefore the grant date fair value is estimated for the purposes of recognizing the expense during the period between service commencement period and grant date.

When the options are exercised, the Company issues new ordinary shares. The proceeds received net of any directly attributable transaction costs are credited to share capital and share premium.

**(b) Cash-settled share-based payment transactions**

The cost of cash-settled transactions is measured initially at fair value at the grant date. This fair value is with recognition of a corresponding liability. The liability is re-measured at each reporting date up to and at the date of settlement, with any changes in fair value recognized in profit or loss for the year.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.27 Provisions

Provisions are recognized when the Group has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognized for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognized even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

**(a) Warranty provision**

The Group records warranty liabilities at the time of sale for the estimated costs that will be incurred under its basic limited warranty. The specific warranty terms and conditions vary depending upon the product and the country in which it was sold, but generally includes technical support, repair parts and labor associated with warranty repair and service actions. The period ranges from one to six years. The Group revaluates its estimates on an annual basis to assess the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary.

### 2.28 Revenue recognition

The Group principally derives revenue from sales of products and provision of internet services.

Revenue is measured at the fair value of the consideration received or receivable, and represents amounts receivable for goods sold or services performed, stated net of discounts, returns and value-added taxes. The Group recognizes revenue when the specific criteria have been met for each of the Group's activities, as described below.

**(a) Sales of products**

Revenue from the sales of products (mainly including smartphones, IoT and lifestyle products) directly to customers, is recognized when control of the goods has been transferred, being when the products are accepted by the customers. The customers have full discretion over the products, and there is no unfulfilled obligation that could affect the customers' acceptance of the products.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.28 Revenue recognition (continued)

**(a) Sales of products (continued)**

Customers in mainland China have an unconditional right to return the products purchased online within 7 days. The Group bases its estimates of sales return on historical results, taking into consideration the type of customers, the type of transactions and the specifics of each arrangement.

**(b) Internet services**

Internet services mainly comprise advertising services and internet value-added services.

***(i) Advertising services***

Advertising revenues comprise mainly display-based and performance-based advertisements.

Revenue from display-based advertisements to the users of smartphones and other devices is recognized on a straight-line basis over the contracted period with customers in which the advertisements are displayed.

Revenue from performance-based advertisements is recognized based on actual performance measurement. The Group recognizes the revenue from the delivery of (i) per-click when the users click on the content, (ii) per-impression when the advertising contents are displayed to users, or (iii) per-download when the third parties' apps are downloaded by users.

***(ii) Internet value-added services***

The Group recognizes the internet value-added services revenue (including online game and fintech business) on a gross or net basis depending on whether the Group is acting as a principal or an agent in the transaction. For online game, the Group also defers the related revenue, over the estimated user relationship periods, given there is an explicit or implicit obligation of the Group to maintain the relevant applications and allow users to have access to them.

Fintech business

The Group's fintech revenues are primarily consist of financial interest income and intermediary services income.

The Group generates financial interest income from provision of loans services through its own online internet finance platform. Financial interest income is recognized over the terms of loan receivables using the effective interest method.

## 2 Summary of significant accounting policies (continued)

### 2.28 Revenue recognition (continued)

**(b) Internet services (continued)**

***(ii) Internet value-added services (continued)***

Fintech business (continued)

The Group also provides intermediary services to the borrowers and third party funding parties (as the lenders). The Group are determined as neither the legal lender nor the legal borrower in the loan origination and repayment process. Therefore, the Group does not record loans receivable and payable arising from the loans between lenders and borrowers. The Group acts as an agent to facilitate such loans. The Group considers the loan facilitation and post-lending management services as distinct performance obligations because both the borrowers and lenders can benefit from the loan facilitation services and post-lending management services on their own, and those services are clearly stated in the contract and are separately identifiable, they are not integrated or interrelated with each other, and do not significantly affect each other. For intermediary services with a financial guarantee obligation, the Group first allocates the total transaction price to the financial guarantee liability, then the remaining consideration is allocated to loan facilitation and post-lending management services on the basis of the relative standalone selling prices, determined by using the cost plus margin approach; for intermediary services with no financial guarantee obligation, the Group allocates the total consideration to loan facilitation and post-lending management services on the basis of the relative standalone selling prices, determined by using the cost plus margin approach. Revenues from loan facilitation services are recognized at point-in-time upon the successful matching between the borrowers and the lenders. Revenues from post-lending management services are recognized ratably over the terms of the underlying loans as the performance obligation is satisfied over time.

Determining whether revenue of the Group should be reported gross or net is based on a continuing assessment of various factors. When determining whether the Group is acting as the principal or agent in offering goods or services to the customer, the Group needs to first identify who controls the specified goods or services before they are transferred to the customer. The Group is a principal if the Group obtains control through any of the following: (i) a good or another asset from the other party that the Group then transfers to the customer; (ii) a right to a service to be performed by the other party, which gives the Group the ability to direct that party to provide the service to the customer on the Group's behalf; (iii) a good or service from the other party that the Group then combines with other goods or services in providing the specified good or service to the customer. If control is unclear, when the Group is primarily obligated in a transaction, is subject to inventory risk, has latitude in establishing prices and selecting suppliers, or has several but not all of these indicators, the Group records revenues on a gross basis. Otherwise, the Group records the net amount earned as commissions from products sold or services provided.

The Group does not expect to have any contracts where the period between the transfer of the promised goods or services to the customer and payment by the customer exceeds one year. As a consequence, the Group does not adjust any of the transaction prices for the time value of money.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.29 Interest income

Interest income from financial assets at FVPL is included in investment income as part of other income.

Interest income on financial assets at amortized cost calculated using the effective interest method is recognized in the consolidated income statement as part of other income.

Interest income is presented as finance income where it is earned from financial assets that are held for cash management purposes.

Interest income is calculated by applying the effective interest rate to the gross carrying amount of a financial asset except for financial assets that subsequently become credit-impaired. For credit-impaired financial assets the effective interest rate is applied to the net carrying amount of the financial asset (after deduction of the loss allowance).

### 2.30 Earnings per share

#### (a) Basic earnings per share

Basic earnings per share is calculated by dividing:

- the profit attributable to owners of the Company, excluding any costs of servicing equity other than ordinary shares.

- by the weighted average number of ordinary shares outstanding during the financial year, adjusted for bonus elements in ordinary shares issued during the year and excluding treasury shares.

#### (b) Diluted earnings per share

Diluted earnings per share adjusts the figures used in the determination of basic earnings per share to take into account:

- the after income tax effect of interest and other financing costs associated with dilutive potential ordinary shares, and

- the weighted average number of additional ordinary shares that would have been outstanding assuming the conversion of all dilutive potential ordinary shares.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 2 Summary of significant accounting policies (continued)

### 2.31 Dividend income

Dividends are received from financial assets measured at FVPL and at FVOCI. Dividends are recognized as other income in profit or loss when the right to receive payment is established. This applies even if they are paid out of pre-acquisition profits, unless the dividend clearly represents a recovery of part of the cost of an investment. In this case, the dividend is recognized in OCI if it relates to an investment measured at FVOCI. However, the investment may need to be tested for impairment as a consequence.

### 2.32 Government grants

Grants from government are recognized at their fair value where there is a reasonable assurance that the grants will be received and the Group will comply with all attached conditions.

Government grants relating to costs are deferred and recognized in the consolidated income statement over the period necessary to match them with the costs that they are intended to compensate. Government grants relating to the property and equipment, and other non-current assets are included in the liabilities and are credited to consolidated income statement on a straight-line basis over the expected lives of the related assets.

### 2.33 Leases

As explained in Note 2.2 above, the Group has changed its accounting policy for leases where the Group is the lessee. The new policy is described below and the impact of the change in Note 2.2.

Until December 31, 2018, leases of plant and equipment and office where the Group, as lessee, had substantially all the risks and rewards of ownership were classified as finance leases. Finance leases were capitalized at the lease's inception at the fair value of the leased property or, if lower, the present value of the minimum lease payments. The corresponding rental obligations, net of finance charges, were included in other short-term and long-term payables. Each lease payment was allocated between the repayment of lease liability and finance cost. The finance cost was charged to the profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The property and equipment acquired under finance leases was depreciated over the asset's useful life or over the shorter of the asset's useful life and the lease term if there was no reasonable certainty that the Group will obtain ownership at the end of the lease term. Leases in which a significant portion of the risks and rewards of ownership were retained by the lessor were classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) were charged to the consolidated income statement on a straight-line basis over the period of the lease.

From January 1, 2019, leases are recognized as a right-of-use asset and a corresponding liability at the date at which the leased asset is available for use by the Group.

## 2 Summary of significant accounting policies (continued)

### 2.33 Leases (continued)

Contracts may contain both lease and non-lease components. The Group allocates the consideration in the contract to the lease and non-lease components based on their relative stand-alone prices.

Assets and liabilities arising from a lease are initially measured on a present value basis. Lease liabilities include the net present value of the following lease payments:

- fixed payments (including in-substance fixed payments), less any lease incentives receivable
- variable lease payment that are based on an index or a rate, initially measured using the index or rate as at the commencement date
- amounts expected to be payable by the Group under residual value guarantees
- the exercise price of a purchase option if the Group is reasonably certain to exercise that option, and
- payments of penalties for terminating the lease, if the lease term reflects the Group exercising that option

Lease payments to be made under reasonably certain extension options are also included in the measurement of the liability.

The lease payments are discounted using the interest rate implicit in the lease. If that rate cannot be readily determined, which is generally the case for leases in the Group, the lessee's incremental borrowing rate is used, being the rate that the individual lessee would have to pay to borrow the funds necessary to obtain an asset of similar value to the right-of-use asset in a similar economic environment with similar terms, security and conditions.

To determine the incremental borrowing rate, the Group:

- where possible, uses recent third-party financing received by the individual lessee as a starting point, adjusted to reflect changes in financing conditions since third party financing was received
- uses a build-up approach that starts with a risk-free interest rate adjusted for credit risk for leases held by the Group, which does not have recent third party financing, and
- makes adjustments specific to the lease, e.g. term, country, currency and security.

## 2 Summary of significant accounting policies (continued)

### 2.33 Leases (continued)

Lease payments are allocated between principal and finance cost. The finance cost is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

Right-of-use assets are measured at cost comprising the following:

- the amount of the initial measurement of lease liability
- any lease payments made at or before the commencement date less any lease incentives received
- any initial direct costs, and
- restoration costs.

Right-of-use assets are generally depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis. If the Group is reasonably certain to exercise a purchase option, the right-of-use asset is depreciated over the underlying asset's useful life. The Group has chosen not to revalue its right-of-use assets.

Payments associated with short-term leases of cloud servers are recognized on a straight-line basis as an expense in profit or loss. Short-term leases are leases with a lease term of 12 months or less.

Lease income from operating leases where the Group is a lessor is recognized in income on a straight-line basis over the lease term (Note 17). Initial direct costs incurred in obtaining an operating lease are added to the carrying amount of the underlying asset and recognized as expense over the lease term on the same basis as lease income. The respective leased assets are included in the balance sheet based on their nature. The Group did not need to make any adjustments to the accounting for assets held as lessor as a result of adopting the new leasing standard.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management

### 3.1 Financial risk factors

The Group's activities expose it to a variety of financial risks: market risk (including foreign exchange risk, interest rate risk and price risk), credit risk and liquidity risk. The Group's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Group's financial performance. Risk management is carried out by the senior management of the Group.

(a) Market risk

*(i) Foreign exchange risk*

The transactions of the Company are denominated and settled in its functional currency, US$. The Group's subsidiaries operate in mainland China and overseas, and they are exposed to foreign exchange risk arising from various currency exposures, primarily with respect to US$ and RMB. Therefore, foreign exchange risk primarily arose from recognized assets and liabilities in the Group's subsidiaries in mainland China when receiving or to receive foreign currencies from, or paying or to pay foreign currencies to overseas business partners, and recognized assets and liabilities in the Group's overseas subsidiaries when receiving or to receive foreign currencies from, or paying or to pay foreign currencies to business partners in mainland China.

For the Group's subsidiaries whose functional currency is RMB, if RMB had strengthened/weakened by 5% against US$ with all other variables held constant, the profit before income tax for the year ended December 31, 2019 would have been approximately RMB28,060,000 lower/higher (2018: RMB148,939,000 higher/lower), as a result of net foreign exchange losses (2018: net foreign exchange gains) on translation of net monetary assets (2018: net monetary liabilities) denominated in US$.

For the Company and the Group's subsidiaries whose functional currency is US$, if RMB had strengthened/weakened by 5% against US$ with all other variables held constant, the profit before income tax for the year ended December 31, 2019 would have been approximately RMB326,278,000 (2018: RMB213,622,000) lower/higher, as a result of net foreign exchange losses on translation of net monetary liabilities denominated in RMB.

# 3 Financial risk management (continued)

## 3.1 Financial risk factors (continued)

### (a) Market risk (continued)

#### *(ii) Interest rate risk*

The Group's interest rate risk primarily arose from borrowings with floating and fixed rates (details of which has been disclosed in Note 33), loan receivables, long-term bank deposits, short-term bank deposits and cash and cash equivalents. Those carried at floating rates expose the Group to cash flow interest rate risk whereas those carried at fixed rates expose the Group to fair value interest rate risk.

If the interest rate of borrowings with floating rate had been 50 basis points higher/lower, the profit before income tax for the year ended December 31, 2019 would have been approximately RMB29,537,000 (2018: RMB17,158,000) lower/higher. This analysis does not include the effect of interest capitalized.

If the interest rate of short-term bank deposits had been 50 basis points higher/lower, the profit before income tax for the year ended December 31, 2019 would have been RMB107,615,000 (2018: RMB6,830,000) higher/lower.

If the interest rate of cash and cash equivalents had been 50 basis points higher/lower, the profit before income tax for the year ended December 31, 2019 would have been RMB129,599,000 (2018: RMB151,151,000) higher/lower.

The Group regularly monitors its interest rate risk to ensure there is no undue exposure to significant interest rate movements.

#### *(iii) Price risk*

The Group is exposed to price risk in respect of the long-term investments and short-term investments measured at fair value through profit or loss held by the Group. The Group is not exposed to commodity price risk. To manage its price risk arising from the investments, the Group diversifies its portfolio. Each investment is managed by senior management on a case by case basis. The sensitivity analysis is performed by management, see Note 3.3 for detail.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

#### (b) Credit risk

The Group is exposed to credit risk in relation to its cash and cash equivalents, long-term bank deposits, short-term bank deposits, restricted cash, short-term investments, loan receivables, trade receivables, other receivables, and financial guarantee contracts. The carrying amounts of each class of the above financial assets represent the Group's maximum exposure to credit risk in relation to financial assets.

To manage risk arising from cash and cash equivalents, long-term bank deposits, short-term bank deposits, restricted cash, short-term investments, the Group only transacts with state-owned or reputable financial institutions in mainland China and reputable international financial institutions outside of mainland China. There has been no recent history of default in relation to these financial institutions.

To manage risk arising from trade receivables, the Group has policies in place to ensure that credit terms are made to counterparties with an appropriate credit history and the management performs ongoing credit evaluations of its counterparties. The credit period granted to the customers is usually no more than 180 days and the credit quality of these customers is assessed, which takes into account their financial position, past experience and other factors.

For other receivables, management makes periodic collective assessments as well as individual assessment on the recoverability of other receivables based on historical settlement records and past experiences. In view of the history of cooperation with debtors and the sound collection history of receivables due from them, management believes that the credit risk inherent in the Group's outstanding other receivable balances due from them is not significant.

For the financial guarantee contracts, the Group has taken measures to manage credit risk, including credit examination, fraud examination and risk monitoring alert. The maximum credit risk from financial guarantee contracts is RMB8,142,058,000 as of December 31, 2019 (2018: RMB4,391,098,000), the majority of which are not credit-impaired on initial recognition and no significant increase in credit risk subsequently. The Group has recognized loss allowance for such losses at each of the reporting date.

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

#### (b) Credit risk (continued)

To manage risk arising from loan receivables, the Group performs standardized credit management procedures. For pre-approval investigation, the Group uses its platform and systems using big data technology to optimize the review process, including credit analysis, assessment of collectability of borrowers, possibility of misconduct and fraudulent activities. In terms of credit examining management, the Group has established specific policies and procedures to assess loans offering. For subsequent monitoring, the Group has implemented credit examination on each borrower every three months. For unqualified borrowers, credit facilities granted previously could be terminated immediately. Once the loan was issued, all borrowers would be assessed by fraud examination model to prevent fraudulent behaviors. In post-loan supervision, the Group has established risk monitoring alert system through periodical monitoring, system alert, and corresponding solutions to identify impaired loans. The estimation of credit exposure for risk management purposes is complex and requires the use of models, as the exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties. The Group measures credit risk using Probability of Default ("**PD**"), Exposure at Default ("**EAD**") and Loss Given Default ("**LGD**"). This is similar to the approach used for the purposes of measuring Expected Credit Loss ("**ECL**") under IFRS 9.

***(b1) Expected credit loss model for loan receivables, as summarized below:***

- The loan receivables that are not credit-impaired on initial recognition are classified in 'Stage 1' and have their credit risk continuously monitored by the Group. The expected credit loss is measured on a 12-month basis.

- If a significant increase in credit risk (as defined below) since initial recognition is identified, the financial instrument is moved to 'Stage 2' but is not yet deemed to be credit-impaired. The expected credit loss is measured on lifetime basis.

- If the financial instrument is credit-impaired (as defined below), the financial instrument is then moved to 'Stage 3'. The expected credit loss is measured on lifetime basis.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

#### (b) Credit risk (continued)

***(b1) Expected credit loss model for loan receivables, as summarized below (continued):***

- In Stages 1 and 2, interest income is calculated on the gross carrying amount (without deducting the loss allowance). If a financial asset subsequently becomes credit-impaired (Stage 3), the Group is required to calculate the interest income by applying the effective interest method in subsequent reporting periods to the amortized cost of the financial asset (the gross carrying amount net of loss allowance) rather than the gross carrying amount.

The impairment of loan receivables was provided based on the 'three-stages' model by referring to the changes in credit quality since initial recognition.

The key judgments and assumptions adopted by the Group in addressing the requirements of the standard are discussed below:

(1) Significant increase in credit risk (SICR)

The Group considers loan receivables to have experienced a significant increase in credit risk when backstop criteria has been met. A backstop is applied and the loan receivables considered to have experienced a significant increase in credit risk if the borrower is more than 1 day past due on its contractual payments.

(2) Definition of default and credit-impaired assets

The Group defines a financial instrument as in default, when the borrower is more than 90 days past due on its contractual payments. This has been applied to all loan receivables held by the Group.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

#### (b) Credit risk (continued)

***(b1) Expected credit loss model for loan receivables, as summarized below (continued):***

(3) Measuring ECL — Explanation of inputs, assumptions and estimation techniques

The expected credit loss is measured on either a 12-month ("**12M**") or Lifetime basis depending on whether a significant increase in credit risk has occurred since initial recognition or whether an asset is considered to be credit-impaired. Expected credit losses are the discounted product of the PD, EAD and LGD.

The ECL is determined by projecting the PD, LGD and EAD for each future month and for each portfolio. These three components are multiplied together and adjusted for the likelihood of survival (i.e. the exposure has not prepaid or defaulted in an earlier month). This effectively calculates an ECL for each future month, which is then discounted back to the reporting date and summarized. The discount rate used in the ECL calculation is the original effective interest rate or an approximation thereof.

(4) Forward-looking information incorporated in the ECL models

The calculation of ECL incorporate forward-looking information. The Group has performed historical analysis and identified the per capita disposable income of urban residents as the key economic variables impacting credit risk and expected credit losses.

As with any economic forecasts, the projections and likelihoods of occurrence are subject to a high degree of inherent uncertainty and therefore the actual outcomes may be significantly different to those projected. The Group considers these forecasts to represent its best estimate of the possible outcomes and has analyzed the non-linearities and asymmetries within the Group's different portfolios to establish that the chosen scenarios are appropriately representative of the range of possible scenarios.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

(b) Credit risk (continued)

*(b1) Expected credit loss model for loan receivables, as summarized below (continued):*

(5) Grouping of instruments for losses measured on a collective basis

For expected credit loss provisions modeled on a collective basis, a grouping of exposures is performed on the basis of shared risk characteristics, such that risk exposures within a group are homogeneous.

*(b2) Credit loss allowance*

The credit loss allowance recognized in the year is impacted by a variety of factors, as described below:

- Transfers between Stage 1 and Stages 2 or 3 due to loan receivables experiencing significant increases (or decreases) of credit risk in the year, and the subsequent "step up" (or "**step down**") between 12-month and Lifetime ECL;

- Additional allowances for new financial instruments recognized, as well as releases for loan receivables derecognized in the year;

- Loan receivables derecognized and write-offs of allowances related to assets that were written off during the year.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

(b) Credit risk (continued)

*(b2) Credit loss allowance (continued)*

The following tables explain the changes in the credit loss allowance for loan receivables between the beginning and the end of the year due to these factors:

| | Stage 1 RMB'000 | Stage 2 RMB'000 | Stage 3 RMB'000 | Total RMB'000 |
|---|---|---|---|---|
| Loss allowance as of January 1, 2019 | 101,621 | 89,271 | 510,973 | 701,865 |
| *Transfers:* | | | | |
| Transfer from Stage 1 to Stage 2 | (208) | 13,785 | — | 13,577 |
| Transfer from Stage 1 to Stage 3 | (2,114) | — | 175,902 | 173,788 |
| Transfer from Stage 2 to Stage 3 | — | (68,890) | 146,511 | 77,621 |
| Change in PDs/LGDs/EADs | 17 | 11 | 35,593 | 35,621 |
| Loan receivables derecognized during the year | (98,076) | (21,373) | (183,746) | (303,195) |
| New loan receivables originated | 196,849 | 387,281 | 642,015 | 1,226,145 |
| Write-offs | — | — | (255,685) | (255,685) |
| Loss allowance as of December 31, 2019 | 198,089 | 400,085 | 1,071,563 | 1,669,737 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

(b) Credit risk (continued)

*(b2) Credit loss allowance (continued)*

| | Stage 1 RMB'000 | Stage 2 RMB'000 | Stage 3 RMB'000 | Total RMB'000 |
|---|---|---|---|---|
| **Loss allowance as of January 1, 2018** | 122,584 | 50,757 | 100,327 | 273,668 |
| *Transfers:* | | | | |
| Transfer from Stage 1 to Stage 2 | (74) | 2,630 | — | 2,556 |
| Transfer from Stage 1 to Stage 3 | (2,502) | — | 168,584 | 166,082 |
| Transfer from Stage 2 to Stage 1 | — | (13) | — | (13) |
| Transfer from Stage 2 to Stage 3 | — | (38,453) | 84,121 | 45,668 |
| Transfer from Stage 3 to Stage 1 | — | — | (9) | (9) |
| Transfer from Stage 3 to Stage 2 | — | 1 | (2) | (1) |
| Change in PDs/LGDs/EADs | (17) | 4 | 2,711 | 2,698 |
| Loan receivables derecognized during the year | (108,910) | (15,333) | (25,239) | (149,482) |
| New loan receivables originated | 90,540 | 89,678 | 316,746 | 496,964 |
| Write-offs | — | — | (136,266) | (136,266) |
| **Loss allowance as of December 31, 2018** | 101,621 | 89,271 | 510,973 | 701,865 |

Significant changes in the gross carrying amount of loan receivables that contributed to changes in the loss allowance were as follows:

The high volume of new loan receivables originated during the year ended December 31, 2019, aligned with the Group's organic growth objective, increased the gross carrying amount of the loan receivables by 126% (2018: 128%) with a corresponding RMB196,849,000 (2018: RMB90,540,000) increase in loss allowance measured on a 12-month basis.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

(b) Credit risk (continued)

*(b2) Credit loss allowance (continued)*

The gross carrying amount of the loan receivables explains their significance to the changes in the loss allowance as discussed above:

| | Stage 1 RMB'000 | Stage 2 RMB'000 | Stage 3 RMB'000 | Total RMB'000 |
|---|---|---|---|---|
| **Gross carrying amount as of January 1, 2019** | 10,227,478 | 207,640 | 560,392 | 10,995,510 |
| *Transfers:* | | | | |
| Transfer from Stage 1 to Stage 2 | (18,538) | 18,538 | — | — |
| Transfer from Stage 1 to Stage 3 | (188,121) | — | 188,121 | — |
| Transfer from Stage 2 to Stage 3 | — | (154,171) | 154,171 | — |
| Loan receivables derecognized during the year other than write-offs | (10,000,977) | (53,444) | (199,724) | (10,254,145) |
| New loan receivables originated | 12,713,842 | 514,412 | 679,306 | 13,907,560 |
| Write-offs | — | — | (255,685) | (255,685) |
| **Gross carrying amount as of December 31, 2019** | 12,733,684 | 532,975 | 1,126,581 | 14,393,240 |
| **Gross carrying amount as of January 1, 2018** | 8,172,340 | 133,327 | 112,494 | 8,418,161 |
| *Transfers:* | | | | |
| Transfer from Stage 1 to Stage 2 | (5,381) | 5,381 | — | — |
| Transfer from Stage 1 to Stage 3 | (183,244) | — | 183,244 | — |
| Transfer from Stage 2 to Stage 1 | 25 | (25) | — | — |
| Transfer from Stage 2 to Stage 3 | — | (91,436) | 91,436 | — |
| Transfer from Stage 3 to Stage 1 | 10 | — | (10) | — |
| Transfer from Stage 3 to Stage 2 | — | 3 | (3) | — |
| Loan receivables derecognized during the year other than write-offs | (7,976,884) | (41,810) | (28,232) | (8,046,926) |
| New loan receivables originated | 10,220,612 | 202,200 | 353,886 | 10,776,698 |
| Write-offs | — | — | (152,423) | (152,423) |
| **Gross carrying amount as of December 31, 2018** | 10,227,478 | 207,640 | 560,392 | 10,995,510 |

There is no originated credit-impaired loan receivables of the Group during the year.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

(b) Credit risk (continued)

*(b3) Write-off policy*

The Group writes off loan receivables, in whole or in part, when it has exhausted all practical recovery efforts and has concluded there is no reasonable expectation of recovery. Indicators that there is no reasonable expectation of recovery include ceasing enforcement activity.

The Group may write-off loan receivables that are still subject to enforcement activity. The outstanding contractual amounts of loan receivables written off during the year ended December 31, 2019 was RMB255,685,000(2018: RMB152,423,000). The Group still seeks to recover amounts it is legally owed in full, but which have been written off due to no reasonable expectation of full recovery.

*(b4) Modification*

The Group rarely modifies the terms of loans provided to customers due to commercial renegotiations, or for distressed loans, with a view to maximizing recovery. The Group considers the impact from such modification is not significant.

(c) Liquidity risk

The Group aims to maintain sufficient cash and cash equivalents. Due to the dynamic nature of the underlying business, the policy of the Group is to regularly monitor the Group's liquidity risk and to maintain adequate cash and cash equivalents or adjust financing arrangements to meet the Group's liquidity requirements. There are loan covenants terms for certain borrowings. As of December 31, 2019, there is no non-compliance with such loan covenants (2018: Nil).

The table below analyzes the Group's non-derivative financial liabilities and off-balance sheet guarantee liabilities into relevant maturity grouping based on the remaining year at each balance sheet date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.1 Financial risk factors (continued)

#### (c) Liquidity risk (continued)

| | Less than 1 year RMB'000 | Between 1 year and 2 years RMB'000 | Between 2 years and 5 years RMB'000 | Over 5 years RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|
| Group | | | | | |
| At December 31, 2019 | | | | | |
| Borrowings | 12,836,555 | 3,176,000 | 1,074,448 | 536,408 | 17,623,411 |
| Trade payables | 59,527,940 | — | — | — | 59,527,940 |
| Other payables | 6,175,923 | 166,065 | 355,915 | 392,040 | 7,089,943 |
| Lease liabilities | 414,687 | 204,959 | 275,879 | 108,590 | 1,004,115 |
| Investment from fund investors | — | — | — | 3,074,210 | 3,074,210 |
| Off-balance sheet guarantee liabilities | 7,893,941 | — | — | — | 7,893,941 |
| At December 31, 2018 | | | | | |
| Borrowings | 3,075,194 | 6,145,202 | 450,308 | 1,260,633 | 10,931,337 |
| Trade payables | 46,287,271 | — | — | — | 46,287,271 |
| Other payables | 5,312,834 | 206,488 | 201,689 | 217,965 | 5,938,976 |
| Investment from fund investors | — | — | — | 2,823,504 | 2,823,504 |
| Off-balance sheet guarantee liabilities | 4,325,961 | — | — | — | 4,325,961 |

### 3.2 Capital management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to enhance shareholders' value in the long-term.

The Group monitors capital (including share capital, share premium and Preferred Shares on an as-if-converted basis) by regularly reviewing the capital structure. As a part of this review, the Group considers the cost of capital and the risks associated with the issued share capital. The Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or repurchase the Company's shares. In the opinion of the directors of the Company, the Group has operating profits and a low level of indebtedness. As a result, capital risk is not significant for the Group and measurement of capital management is not a tool currently used in the internal management reporting procedures of the Group.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.3 Fair value estimation

The table below analyzes the Group's financial instruments carried at fair value as of each balance sheet date, by level of the inputs to valuation techniques used to measure fair value. Such inputs are categorized into three levels within a fair value hierarchy as follows:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1);
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2); and
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (level 3).

The following table presents the Group's financial assets that are measured at fair value at December 31, 2019:

| | Level 1<br>RMB'000 | Level 2<br>RMB'000 | Level 3<br>RMB'000 | Total<br>RMB'000 |
|---|---|---|---|---|
| **Assets** | | | | |
| Long-term investments measured at fair value through profit or loss (Note 19) | 3,651,090 | — | 17,028,273 | 20,679,363 |
| Short-term investments measured at fair value through profit or loss (Note 19) | — | — | 16,463,390 | 16,463,390 |
| | 3,651,090 | — | 33,491,663 | 37,142,753 |

# 3 Financial risk management (continued)

## 3.3 Fair value estimation (continued)

The following table presents the Group's financial assets that are measured at fair value at December 31, 2018:

| | Level 1 RMB'000 | Level 2 RMB'000 | Level 3 RMB'000 | Total RMB'000 |
|---|---|---|---|---|
| **Assets** | | | | |
| Long-term investments measured at fair value through profit or loss (Note 19) | 5,215,898 | — | 13,420,310 | 18,636,208 |
| Short-term investments measured at fair value through profit or loss (Note 19) | — | — | 6,648,526 | 6,648,526 |
| | 5,215,898 | — | 20,068,836 | 25,284,734 |

(a) **Financial instruments in level 1**

The fair value of financial instruments traded in active markets is based on quoted market prices at each of the reporting dates. A market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service, or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. The quoted market price used for financial assets held by the Group is the current bid price. These instruments are included in level 1.

(b) **Financial instruments in level 2**

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. These valuation techniques maximize the use of observable market data where it is available and rely as little as possible on entity specific estimates. If all significant inputs required to fair value of an instrument are observable, the instrument is included in level 2.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.3 Fair value estimation (continued)

#### (c) Financial instruments in level 3

If one or more of the significant inputs is not based on observable market data, the instrument is included in level 3.

Specific valuation techniques used to value financial instruments include:

- Quoted market prices or dealer quotes for similar instruments;

- Discounted cash flow model and unobservable inputs mainly including assumptions of expected future cash flows and discount rate; and

- A combination of observable and unobservable inputs, including risk-free rate, expected volatility, discount rate for lack of marketability, market multiples, etc.

Level 3 instruments of the Group's assets and liabilities include long-term investments measured at fair value through profit or loss, short-term investments measured at fair value through profit or loss and Preferred Shares.

The changes in level 3 instruments of Preferred Shares for the year ended December 31, 2018 are presented in the Note 35.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.3 Fair value estimation (continued)

#### (c) Financial instruments in level 3 (continued)

The following table presents the changes in level 3 instruments of long-term investments measured at fair value through profit or loss for the years ended December 31, 2019 and 2018:

| | Year ended December 31, 2019 RMB'000 | 2018 RMB'000 |
|---|---|---|
| At the beginning of the year | 13,420,310 | 13,092,429 |
| Addition | 3,486,670 | 1,727,614 |
| Disposal | (396,683) | (146,908) |
| Changes in fair value | 2,287,879 | 6,566,513 |
| Transfer to long-term investments accounted for using the equity method | (958,701) | (6,523,539) |
| Transfer to level 1 financial instruments | (967,179) | (1,467,599) |
| Exchange gains | 155,977 | 171,800 |
| At the end of the year | 17,028,273 | 13,420,310 |
| Net unrealized gains for the year | 1,772,043 | 4,047,551 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.3 Fair value estimation (continued)

#### (c) Financial instruments in level 3 (continued)

The following table presents the changes in level 3 instruments of short-term investments measured at fair value through profit or loss for the years ended December 31, 2019 and 2018:

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| At the beginning of the year | 6,648,526 | 4,488,076 |
| Addition | 134,409,027 | 140,955,400 |
| Disposal | (125,019,014) | (139,154,171) |
| Changes in fair value | 424,851 | 359,221 |
| At the end of the year | 16,463,390 | 6,648,526 |
| Net unrealized gains for the year | 38,390 | 23,526 |

The Group has a team that manages the valuation of level 3 instruments for financial reporting purposes. The team manages the valuation exercise of the investments on a case by case basis. At least once every year, the team would use valuation techniques to determine the fair value of the Group's level 3 instruments. External valuation experts will be involved when necessary.

The valuation of the level 3 instruments mainly included long-term investments measured at fair value through profit or loss in unlisted companies and certain listed companies for which sale is restricted for a specified period (Note 19), and short-term investments measured at fair value through profit or loss (Note 19). As these instruments are not traded in an active market, their fair values have been determined by using various applicable valuation techniques, including market approach etc.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.3 Fair value estimation (continued)

#### (c) Financial instruments in level 3 (continued)

The following table summarizes the quantitative information about the significant unobservable inputs used in recurring level 3 fair value measurements.

| Description | Fair values | | Significant unobservable inputs | Range of inputs | | Relationship of unobservable inputs to fair values |
|---|---|---|---|---|---|---|
| | As of December 31, | | | As of December 31, | | |
| | 2019 | 2018 | | 2019 | 2018 | |
| | RMB'000 | RMB'000 | | | | |
| Long-term investments measured at fair value through profit or loss | 17,028,273 | 13,420,310 | Expected volatility | 26%–59% | 32%–62% | The higher the expected volatility, the lower the fair value |
| | | | Discount for lack of marketability ("DLOM") | 5%–25% | 5%–25% | The higher the DLOM, the lower the fair value |
| | | | Risk-free rate | 2%–3% | 2%–4% | The higher the risk-free rate, the higher the fair value |
| Short-term investments measured at fair value through profit or loss | 16,463,390 | 6,648,526 | Expected rate of return | 2%–5% | 2%–5% | The higher the expected rate of return, the higher the fair value |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 3 Financial risk management (continued)

### 3.3 Fair value estimation (continued)

If the fair values of the long-term investments and short-term investments measured at fair value through profit or loss held by the Group had been 10% higher/lower, the profit before income tax for the year ended December 31, 2019 would have been approximately RMB3,714,275,000 (2018: RMB2,528,473,000) higher/lower.

There were no material transfers between level 1, 2 and 3 of fair value hierarchy classifications during the year ended December 31, 2019, except that certain financial assets were transferred out of level 3 of fair value hierarchy to level 1 classifications due to the conversion to ordinary shares as the result of the initial public offering of the investee companies.

The carrying amounts of the Group's financial assets that are not measured at fair value, including cash and cash equivalents, restricted cash, short-term bank deposits, short-term investments measured at amortized cost, trade receivables, loan receivables and other receivables, and the Group's financial liabilities that are not measured at fair value, including borrowing, trade payables and other payables, approximate their fair values due to short maturities or the interest rates are close to the market interest rates.

## 4 Critical accounting estimates and judgments

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are addressed below.

### (a) Fair value of financial assets

Fair value of financial assets, in the absence of an active market, is estimated by using appropriate valuation techniques. Such valuations were based on certain assumptions about credit risk, volatility and liquidity risks associated with the instruments, which are subject to uncertainty and might materially differ from the actual results. Further details are included in Note 3.3.

## 4 Critical accounting estimates and judgments (continued)

### (b) Impairment of loan receivables

The Group follows the guidance of IFRS 9 to determine when a loan receivable is impaired. This determination requires significant judgment and estimation. In making this judgment and estimation, the Group evaluates, among other factors, the duration of receivables and the financial health collection history of individual debtors and expected future change of credit risks, including the consideration of factors such as general economy measure, changes in macroeconomic indicators etc. Further details are included in Note 3.1 to the consolidated financial statements.

### (c) Current and deferred income taxes

The Group is subject to income taxes in different jurisdictions. Significant judgment is required in determining the worldwide provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain. The Group recognizes liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current and deferred income tax assets and liabilities in the period in which such determination is made.

For temporary differences which give rise to deferred tax assets, the Group assesses the likelihood that the deferred income tax assets could be recovered. Deferred tax assets are recognized based on the Group's estimates and assumptions that they will be recovered from taxable income arising from continuing operations in the foreseeable future.

### (d) Inventory provision

Inventories are stated at the lower of cost and net realizable value. Management makes provision for inventories based on historical experience and estimation of future market condition and sales. Management will adjust the provision where actual net realizable value is higher or lower than previously estimated. This requires significant judgment and estimation.

### (e) Recoverability of non-financial assets and investments accounted for using the equity method

The recoverable amount of non-financial assets and investments accounted for using the equity method is the greater of its fair value less costs of disposal and value-in-use. In assessing value-in-use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset, which requires significant judgment relating to level of revenue and amount of operating costs.

## 4 Critical accounting estimates and judgments (continued)

### (e) Recoverability of non-financial assets and investments accounted for using the equity method (continued)

The Group uses all readily available information in determining an amount that is a reasonable estimation of the recoverable amount, including estimates based on reasonable and supportable assumptions and projections of revenue and operating costs. Changes in these estimates could have a significant impact on the carrying value of the assets and could result in further impairment charge or reversal of impairment in future periods.

### (f) Warranty provision

Warranty provision is based on the estimated cost of product warranties when revenue is recognized. Factors that affect the Group's warranty liability include the number of products sold under warranty, historical and anticipated rates of warranty claims on those products, and cost per claim to satisfy the warranty obligation. The estimation basis is reviewed on an on-going basis and revised where appropriate.

### (g) Revenue

Application of various accounting principles related to the measurement and recognition of revenue requires the Group to make judgments and estimates. Specifically, significant judgments include determining whether the Group is acting as the principal in a transaction. The Group is a principal in a transaction if the Group obtains control of the products sold or services provided before they are transferred to customers. If control is unclear, when the Group is primarily obligated in a transaction, is subject to inventory risk, has latitude in establishing prices and selecting suppliers, or has several but not all of these indicators, the Group records revenues on a gross basis. Otherwise, the Group records the net amount earned as commissions from products sold or services provided.

## 5 Segment information

The Group's business activities, for which discrete financial statements are available, are regularly reviewed and evaluated by the CODM. The CODM, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Chief Executive Officer that makes strategic decisions. As a result of this evaluation, the Group determined that it has operating segments as follows:

- Smartphones
- IoT and lifestyle products
- Internet services
- Others

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 5 Segment information (continued)

The CODM assesses the performance of the operating segments mainly based on segment revenue and gross profit of each operating segment. The selling and marketing expenses, administrative expenses and research and development expenses are not included in the measure of the segments' performance which is used by CODM as a basis for the purpose of resource allocation and assessment of segment performance. Fair value changes on investments measured at fair value through profit or loss, share of losses of investments accounted for using the equity method, other income, other (losses)/gains, net, finance income, net, fair value changes of convertible redeemable preferred shares and income tax expenses are also not allocated to individual operating segments.

The revenues from external customers reported to CODM are measured as segment revenue, which is the revenue derived from the customers in each segment. Revenues from smartphones segment are derived from the sale of smartphones. Revenues from the IoT and lifestyle products segment primarily comprise revenues from sales of (i) the Group's other in-house products, including smart TVs, laptops, AI speakers and smart routers, and (ii) the Group's ecosystem products, including certain IoT and other smart hardware products, as well as certain lifestyle products. Revenues from internet services segment are derived from advertising services and internet value-added services. Others segment primarily comprises revenue from the Group's hardware repair services for products and sale of materials.

The Group's cost of sales for smartphones segment and IoT and lifestyle products segment primarily consist of (i) procurement cost of raw materials and components for the Group's in-house products, (ii) assembly cost charged by the Group's outsourcing partners for the Group's in-house products, (iii) royalty fees for certain technologies embedded in the Group's in-house products, (iv) costs, in the forms of production costs and profit-sharing, paid to the Group's partners for procuring ecosystem products, (v) warranty expenses, and (vi) provision for impairment of inventories. The Group's cost of sales for internet services segment primarily consist of (i) content fees to game developers, and (ii) bandwidth, server custody and cloud service related costs. Cost of sales for others segment primarily consists of hardware repair costs and costs from sale of materials. Other information, together with the segment information, provided to the CODM, is measured in a manner consistent with that applied in the consolidated financial statements. There were no separate segment assets and segment liabilities information provided to the CODM, as CODM does not use this information to allocate resources or to evaluate the performance of the operating segments.

There were no material inter-segment sales during the years ended December 31, 2019 and 2018. The revenues from external customers reported to the CODM are measured in a manner consistent with that applied in the consolidated income statement.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 5 Segment information (continued)

The segment results for the years ended December 31, 2019 and 2018 are as follows:

| | Year ended December 31, 2019 | | | | |
|---|---|---|---|---|---|
| | Smartphones RMB'000 | IoT and lifestyle products RMB'000 | Internet services RMB'000 | Others RMB'000 | Total RMB'000 |
| Segment revenues | 122,094,897 | 62,087,998 | 19,841,569 | 1,814,218 | 205,838,682 |
| Cost of sales | (113,335,546) | (55,134,299) | (6,998,096) | (1,816,708) | (177,284,649) |
| Gross profit/(loss) | 8,759,351 | 6,953,699 | 12,843,473 | (2,490) | 28,554,033 |

| | Year ended December 31, 2018 | | | | |
|---|---|---|---|---|---|
| | Smartphones RMB'000 | IoT and lifestyle products RMB'000 | Internet services RMB'000 | Others RMB'000 | Total RMB'000 |
| Segment revenues | 113,800,386 | 43,816,885 | 15,955,558 | 1,342,596 | 174,915,425 |
| Cost of sales | (106,757,127) | (39,306,134) | (5,683,856) | (976,369) | (152,723,486) |
| Gross profit | 7,043,259 | 4,510,751 | 10,271,702 | 366,227 | 22,191,939 |

The reconciliation of gross profit to profit before income tax is shown in the consolidated income statement.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 5 Segment information (continued)

The Company is domiciled in the Cayman Islands while the Group mainly operates its businesses in mainland China. For the years ended December 31, 2019 and 2018, the geographical information on the total revenues is as follows:

| | Year ended December 31, | | | |
|---|---|---|---|---|
| | 2019 | | 2018 | |
| | RMB'000 | % | RMB'000 | % |
| Mainland China | 114,608,633 | 55.7 | 104,944,803 | 60.0 |
| Rest of the world (Note(a)) | 91,230,049 | 44.3 | 69,970,622 | 40.0 |
| | 205,838,682 | | 174,915,425 | |

Note:

(a) Revenues outside mainland China are mainly from India, Indonesia and Western Europe.

The major customers which contributed more than 10% of the total revenue of the Group for the years ended December 31, 2019 and 2018 are listed as below:

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | % | % |
| Customer A | 12.1 | 10.9 |

All the revenues derived from other single external customer were less than 10% of the Group's total revenues for the years ended December 31, 2019 and 2018.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 6 Revenue

| | Year ended December 31, | |
|---|---|---|
| | 2019 RMB'000 | 2018 RMB'000 |
| Smartphones | 122,094,897 | 113,800,386 |
| IoT and lifestyle products | 62,087,998 | 43,816,885 |
| Internet services | 19,841,569 | 15,955,558 |
| Others | 1,814,218 | 1,342,596 |
| | 205,838,682 | 174,915,425 |

## 7 Other income

| | Year ended December 31, | |
|---|---|---|
| | 2019 RMB'000 | 2018 RMB'000 |
| Government grants | 400,405 | 274,584 |
| Value-added tax and other tax refunds | 55,282 | 82,507 |
| Dividend income | 347,205 | 131,804 |
| Investment income from short-term investments measured at fair value through profit or loss | 386,461 | 335,695 |
| Investment income from short-term investments measured at amortized cost | — | 20,199 |
| Others | 76,568 | — |
| | 1,265,921 | 844,789 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 8 Expenses by nature

| | Year ended December 31, | |
|---|---|---|
| | 2019 RMB'000 | 2018 RMB'000 |
| Cost of inventories sold | 157,935,754 | 138,237,733 |
| Provision for impairment of inventories (Note 23) | 3,859,675 | 3,006,525 |
| Royalty fees | 5,042,116 | 4,263,421 |
| Employee benefit expenses (Note 9) | 8,304,928 | 17,114,892 |
| Depreciation of property and equipment, right-of-use assets and investment properties (Note 14, 16, 17) | 895,273 | 219,523 |
| Amortization of intangible assets (Note 15) | 485,786 | 528,693 |
| Promotion and advertising expenses | 3,355,201 | 2,486,350 |
| Content fees to game developers and video providers | 1,754,622 | 1,629,144 |
| Credit loss allowance for loan receivables | 1,015,619 | 607,180 |
| Consultancy and professional service fees | 730,312 | 903,076 |
| Cloud service, bandwidth and server custody fees | 1,724,145 | 1,725,218 |
| Office rental expenses | — | 529,497 |
| Warranty expenses | 2,641,794 | 1,068,252 |
| Auditor's remuneration | 79,126 | 51,803 |

During the year, the Group incurred expenses for the purpose of research and development of approximately RMB7,492,554,000 (2018: RMB5,776,826,000), which comprised employee benefits expenses of RMB4,526,246,000 (2018: RMB4,043,476,000). No significant development expenses had been capitalized during the year (2018: Nil).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 9 Employee benefit expenses

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Wages, salaries and bonuses | 4,699,234 | 3,565,209 |
| Share-based compensation expenses (Note (a) and Note 28) | 2,201,722 | 12,380,668 |
| Contributions to pension plans | 551,073 | 481,686 |
| Other social security costs, housing benefits and other employee benefits | 852,899 | 687,329 |
| | 8,304,928 | 17,114,892 |

Note:

(a) Share-based compensation expenses contain the expenses for share-based awards granted to the Group's employees and the expenses for Xiaomi Development Fund ("**Employee Fund**").

### (a) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group include one director (Chew Shou Zi) during the year ended December 31, 2019 (2018: Lei Jun). All of these individuals including that one director have not received any emolument from the Group as an inducement to join the Group or compensation for loss of office during the years ended December 31, 2019 and 2018. The emoluments payable to the five highest paid individuals during the years ended December 31, 2019 and 2018 are as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Wages, salaries and bonuses | 6,762 | 9,398 |
| Share-based compensation expenses | 262,073 | 10,208,783 |
| Contributions to pension plans | 154 | 71 |
| Other social security costs, housing benefits and other employee benefits | 229 | 70 |
| | 269,218 | 10,218,322 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 9 Employee benefit expenses (continued)

### (a) Five highest paid individuals (continued)

The emoluments fell within the following bands:

| | Number of individuals Year ended December 31, 2019 | 2018 |
|---|---|---|
| Hong Kong dollar ("**HK$**") 10,000,001 to HK$30,000,000 | — | — |
| HK$30,000,001 to HK$100,000,000 | 5 | 4 |
| HK$100,000,001 to HK$150,000,000 | — | — |
| HK$150,000,001 to HK$15,000,000,000 | — | 1 |

### (b) Benefits and interests of directors

| Name of Director | Fees HK$'000 | Salary HK$'000 | Discretionary bonuses HK$'000 | Allowances and benefits in kind HK$'000 | Employer's contribution to a retirement benefit scheme HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|
| Executive Directors | | | | | | |
| LEI, Jun | — | — | — | — | — | — |
| LIN, Bin | — | — | — | — | — | — |
| CHEW, Shou Zi (i) | — | — | — | — | — | — |
| Non-executive Directors | | | | | | |
| KOH, Tuck Lye (ii) | — | — | — | — | — | — |
| LIU, Qin | — | — | — | — | — | — |
| Independent non-executive Directors | | | | | | |
| CHEN, Dongsheng | 500 | — | — | — | — | 500 |
| LEE, Ka Kit (iii) | 311 | — | — | — | — | 311 |
| WONG, Shun Tak (v) | 823 | — | — | — | — | 823 |
| TONG, Wai Cheung Timothy (iv) (vi) | 511 | — | — | — | — | 511 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 9 Employee benefit expenses (continued)

### (b) Benefits and interests of directors (continued)

Notes:

(i) Mr. Chew Shou Zi was appointed as an executive director of the Company with effect from October 25, 2019.

(ii) Mr. Koh Tuck Lye has resigned as a non- executive director of the Company with effect from October 25, 2019.

(iii) Dr. Lee Ka Kit has resigned as an independent non-executive director of the Company with effect from August 23, 2019.

(iv) Prof. Tong Wai Cheung Timothy was appointed as an independent non-executive director of the Company with effect from August 23, 2019.

(v) HK$323,000 was paid to Mr. Wong Shun Tak during the year ended December 31, 2019 in connection with his service as director or other service in respect of management of the affairs of the Company's subsidiary undertakings.

(vi) HK$323,000 was paid to Prof. Tong Wai Cheung Timothy during the year ended December 31, 2019 in connection with his service as director or other service in respect of management of the affairs of the Company's subsidiary undertakings.

During the year ended December 31, 2019, no share based awards were granted to directors. Certain share based awards were granted to Lei Jun during the year ended December 31, 2018 (Note 28).

### (c) Directors' termination benefits

No director's termination benefit subsisted as of December 31, 2019 and 2018 or at any time during all the years presented.

### (d) Consideration provided to third parties for making available directors' services

No consideration provided to third parties for making available directors' services subsisted as of December 31, 2019 and 2018 or at any time during all the years presented.

### (e) Information about loans, quasi-loans and other dealings in favor of directors, controlled bodies corporate by and connected entities with such directors

No loans, quasi-loans and other dealings in favor of directors, controlled bodies corporate by and connected entities with such directors subsisted as of December 31, 2019 and 2018 or at any time during all the years presented.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 9 Employee benefit expenses (continued)

### (f) Directors' material interests in transactions, arrangements or contracts

No significant transactions, arrangements and contracts in relation to the Group's business to which the Company was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted as of December 31, 2019 and 2018 or at any time during all the years presented.

## 10 Finance income, net

| | Year ended December 31, | |
|---|---|---|
| | **2019** | 2018 |
| | **RMB'000** | RMB'000 |
| **Finance income:** | | |
| Interest income from bank deposits | **930,889** | 601,065 |

Interest income mainly represents interest income from bank deposits, including bank balance and term deposits.

| | Year ended December 31, | |
|---|---|---|
| | **2019** | 2018 |
| | **RMB'000** | RMB'000 |
| **Finance costs:** | | |
| Interest expense from liabilities to fund investors (Note 29) | **250,706** | 42,504 |
| Interest expense from borrowings (Note 33) and lease liabilities (Note 16) | **407,141** | 415,465 |
| Less: amount capitalized | **(129,387)** | (73,277) |
| | **528,460** | 384,692 |

Finance costs have been capitalized on qualifying assets at average interest rates of 5.78% per annum for the year ended December 31, 2019 (2018: 5.35%).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 11(a) Major subsidiaries and controlled structured entities

As of December 31, 2019 and 2018, the Company had the following major subsidiaries (including controlled structured entities):

| Name | Place of incorporation/ establishment and kind of legal entity | Date of incorporation/ establishment | Particulars of issued/ paid-in capital | Effective interest held As of December 31, 2019 | 2018 | As of the date of this report | Principal activities |
|---|---|---|---|---|---|---|---|
| **Subsidiaries** | | | | | | | |
| **Directly held:** | | | | | | | |
| Xiaomi H.K. Limited | Hong Kong, limited liability company | April 7, 2010 | HK$10,000 | 100% | 100% | 100% | Wholesale and retail of smartphones and ecosystem partners' products |
| Fast Pace Limited | British Virgin Islands, limited liability company | January 8, 2013 | US$2 | 100% | 100% | 100% | Investment holding and investment activities |
| Xiaomi Ventures Limited | British Virgin Islands, limited liability company | March 21, 2013 | US$1 | 100% | 100% | 100% | Investment holding and investment activities |
| Xiaomi Singapore Pte. Ltd. | Singapore, limited liability company | December 23, 2013 | Singapore Dollar ("**SGD**")1 and US$149,000,000 | 100% | 100% | 100% | Sales of smart hardware |
| Xiaomi Finance Inc. | Cayman Islands, limited liability company | February 15, 2018 | US$1 | 100% | 100% | 100% | Investment holding and investment activities |
| Xiaomi Best Time International Ltd. | Hong Kong, limited liability company | December 20, 2018 | US$500,000,000 | 100% | 100% | 100% | Intra-group capital supervision, collection, remittance, credit guarantee and interest rate risk management |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 11(a) Major subsidiaries and controlled structured entities (continued)

As of December 31, 2019 and 2018, the Company had the following major subsidiaries (including controlled structured entities) (continued):

| Name | Place of incorporation/ establishment and kind of legal entity | Date of incorporation/ establishment | Particulars of issued/ paid-in capital | Effective interest held As of December 31, 2019 | 2018 | As of the date of this report | Principal activities |
|---|---|---|---|---|---|---|---|
| **Subsidiaries** | | | | | | | |
| **Indirectly held:** | | | | | | | |
| Xiaomi Communications Co., Ltd. | Mainland China, limited liability company | August 25, 2010 | US$130,000,000 | 100% | 100% | 100% | Sales of smartphones, sales of ecosystem partners' products and provision of customer services |
| Beijing Xiaomi Electronics Co., Ltd. | Mainland China, limited liability company | January 9, 2012 | US$27,000,000 | 100% | 100% | 100% | Sales of smart hardware |
| Taiwan Xiaomi Communications Co., Ltd. | Taiwan, limited liability company | April 25, 2000 | New Taiwan Dollar("**NTD**") 5,000,000 | 100% | 100% | 100% | Sales of smart hardware |
| Chongqing Xiaomi Microcredit Co., Ltd. | Mainland China, limited liability company | June 12, 2015 | US$450,000,000 | 100% | 100% | 100% | Internet finance and consumer loan services |
| Beijing Xiaomi Mobile Software Co., Ltd. | Mainland China, limited liability company | May 8, 2012 | RMB288,000,000 | 100% | 100% | 100% | Software and hardware development and provision of software related services |
| Zhuhai Xiaomi Communications Co., Ltd. | Mainland China, limited liability company | January 25, 2013 | RMB2,000,000 | 100% | 100% | 100% | Procurement and sales of smartphones, ecosystem partners' products and spare parts, procurement of raw materials |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 11(a) Major subsidiaries and controlled structured entities (continued)

As of December 31, 2019 and 2018, the Company had the following major subsidiaries (including controlled structured entities) (continued):

| | | | | Effective interest held | | | |
|---|---|---|---|---|---|---|---|
| Name | Place of incorporation/ establishment and kind of legal entity | Date of incorporation/ establishment | Particulars of issued/ paid-in capital | As of December 31, 2019 | 2018 | As of the date of this report | Principal activities |
| **Subsidiaries Indirectly held (continued):** | | | | | | | |
| Guangdong Xiaomi Inc. | Mainland China, limited liability company | September 21, 2015 | RMB1,000,000,000 | 100% | 100% | 100% | Provision of software and technology service |
| Guangzhou Xiaomi Communications Co., Ltd. | Mainland China, limited liability company | September 22, 2016 | RMB951,000,000 | 100% | 100% | 100% | Sales of smart hardware |
| Timi Personal Computing Co., Ltd. | Mainland China, limited liability company | July 28, 2015 | RMB2,000,000 | 100% | 100% | 100% | Sales of smart hardware |
| Xiaomi Technology India Private Limited | India, limited liability company | October 7, 2014 | Indian Rupees ("**INR**")207,450 | 100% | 100% | 100% | Sales of smartphones and ecosystem partners' products |
| Guangzhou Xiaomi Information Service Co., Ltd. | Mainland China, limited liability company | December 29, 2016 | RMB1,000,000 | 100% | 100% | 100% | Provision of advertising and promotion services |
| Xiaomi Home Commercial Co., Ltd. | Mainland China, limited liability company | June 27, 2017 | RMB100,000,000 | 100% | 100% | 100% | Operation of retail stores |
| Red Better Limited | British Virgin Islands, limited liability company | October 8, 2013 | – | 100% | 100% | 100% | Investment activities |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 11(a) Major subsidiaries and controlled structured entities (continued)

As of December 31, 2019 and 2018, the Company had the following major subsidiaries (including controlled structured entities) (continued):

| Name | Place of incorporation/ establishment and kind of legal entity | Date of incorporation/ establishment | Particulars of issued/ paid-in capital | Effective interest held As of December 31, 2019 | Effective interest held As of December 31, 2018 | Effective interest held As of the date of this report | Principal activities |
|---|---|---|---|---|---|---|---|
| **Subsidiaries Indirectly held (continued):** | | | | | | | |
| Green Better Limited | British Virgin Islands, limited liability company | December 9, 2013 | US$1 | 100% | 100% | 100% | Investment activities |
| People Better Limited | British Virgin Islands, limited liability company | April 22, 2014 | US$1,000,001 | 100% | 100% | 100% | Investment activities |
| Xiaomi Home Technology Co., Ltd. | Mainland China, limited liability company | January 20, 2017 | RMB80,000,000 | 100% | 100% | 100% | Operation of retail stores |
| Beijing Zilin Real Estate Co., Ltd. | Mainland China, limited liability company | November 29, 2018 | RMB1,000,000,000 | 95% | 95% | 95% | Property management |
| Xiaomi Commercial Factoring (Tianjin) Co., Ltd. | Mainland China, limited liability company | March 21, 2018 | US$380,000,000 | 100% | 100% | 100% | Commercial factoring business |
| Beijing Xiaomi Software Co., Ltd. | Mainland China, limited liability company | December 19, 2011 | RMB18,859,500 | 100% | 100% | 100% | Research and development of computer software and information technology |
| PT. Xiaomi Technology Indonesia | Indonesia, limited liability company | April 23, 2018 | Indonesian Rupiah ("**IDR**") 13,000,000,000 | 100% | 100% | 100% | Sales of smartphones and ecosystem partners' products |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 11(a) Major subsidiaries and controlled structured entities (continued)

As of December 31, 2019 and 2018, the Company had the following major subsidiaries (including controlled structured entities) (continued):

| Name | Place of incorporation/ establishment and kind of legal entity | Date of incorporation/ establishment | Particulars of issued/ paid-in capital | Effective interest held: As of December 31, 2019 | Effective interest held: As of December 31, 2018 | Effective interest held: As of the date of this report | Principal activities |
|---|---|---|---|---|---|---|---|
| **Subsidiaries Indirectly held (continued):** | | | | | | | |
| Xiaomi Technology (Wuhan) Co., Ltd. | Mainland China, limited liability company | September 1, 2017 | RMB210,000,000 | 100% | 100% | 100% | Software development |
| Airstar Bank Limited | Hong Kong, limited liability company | July 13, 2018 | HK$1,500,000,000 | 90% | 90% | 90% | Virtual banking |
| Xiaomi Information Technology Wuhan Ltd. | Mainland China, limited liability company | August 3, 2018 | RMB123,770,000 | 100% | 100% | 100% | Information technology advisory services |
| Beijing Pinecone Electronics Co., Ltd. (Note (b)) | Mainland China, limited liability company | October 16, 2014 | RMB250,000,000 | 100% | 72% | 100% | Development and sales of electronic products |
| Chengdu Beida Asset Management Co., Ltd. | Mainland China, limited liability company | August 17, 2017 | RMB20,000,000 | 100% | 100% | 100% | Asset management, project investment, investment consulting |
| Beijing Xiaomi Intelligent Technology Co., Ltd. | Mainland China, limited liability company | May 15, 2018 | RMB40,000,000 | 100% | 100% | 100% | Technology development, technology diffusion, technology transfer, technology consulting |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 11(a) Major subsidiaries and controlled structured entities (continued)

As of December 31, 2019 and 2018, the Company had the following major subsidiaries (including controlled structured entities) (continued):

| | | | | Effective interest held | | | |
|---|---|---|---|---|---|---|---|
| Name | Place of incorporation/ establishment and kind of legal entity | Date of incorporation/ establishment | Particulars of issued/ paid-in capital | As of December 31, 2019 | As of December 31, 2018 | As of the date of this report | Principal activities |
| **Controlled structured entities (Note (a)):** | | | | | | | |
| Xiaomi Inc. | Mainland China, limited liability company | March 3, 2010 | RMB1,850,000,000 | 100% | 100% | 100% | E-commerce business |
| Tianjin Jinxing Venture Investment Co., Ltd. | Mainland China, limited liability company | December 26, 2013 | RMB2,476,557,552 | 100% | 100% | 100% | Investment activities |
| Sichuan Silver Mi Technology Co., Ltd. | Mainland China, limited liability company | October 26, 2005 | RMB2,000,000,000 | 100% | 100% | 100% | Research and development of computer software and market research |
| Jiefu Ruitong Inc. | Mainland China, limited liability company | January 11, 2011 | RMB100,000,000 | 100% | 100% | 100% | Provision of electronic payment services |
| Beijing Duokan Technology Co., Ltd. | Mainland China, limited liability company | February 10, 2010 | RMB10,000,000 | 100% | 100% | 100% | Sales of e-book |
| Beijing Wali Internet Technologies Co., Ltd. | Mainland China, limited liability company | June 1, 2009 | RMB2,100,000 | 100% | 100% | 100% | Provision of internet services |
| Tianjin Gold Mi Investment Partners (Limited Partnership) | Mainland China, limited partnership | July 16, 2014 | RMB2,408,957,772 | 100% | 100% | 100% | Investment activities |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 11(a) Major subsidiaries and controlled structured entities (continued)

As of December 31, 2019 and 2018, the Company had the following major subsidiaries (including controlled structured entities) (continued):

| Name | Place of incorporation/ establishment and kind of legal entity | Date of incorporation/ establishment | Particulars of issued/ paid-in capital | Effective interest held: As of December 31, 2019 | Effective interest held: As of December 31, 2018 | Effective interest held: As of the date of this report | Principal activities |
|---|---|---|---|---|---|---|---|
| **Controlled structured entities (Note (a)):** | | | | | | | |
| Hubei Xiaomi Yangtze River Industry Investment Fund Partners (Limited Partnership) | Mainland China, limited partnership | December 7, 2017 | RMB3,384,000,000 | 18% | 18% | 18% | Investment activities |
| Youpin Information Technology Co., Ltd. | Mainland China, limited liability company | April 4, 2018 | RMB50,000,000 | 100% | 100% | 100% | E-commerce business |

Notes:

(a) The Company does not have directly or indirectly legal ownership in equity of these structured entities or their subsidiaries. Nevertheless, under certain Contractual Arrangements entered into with the registered owners of these structured entities, the Company and its other legally owned subsidiaries control these companies by way of controlling the voting rights, governing their financial and operating policies, appointing or removing the majority of the members of their controlling authorities, and casting the majority of votes at meetings of such authorities. Accordingly, the Group has rights to exercise power over these structured entities, receives variable returns from its involvement in these structured entities, and has the ability to affect those returns through its power over these structured entities. As a result, they are presented as structured entities of the Company.

(b) In 2019, the Group entered into a share repurchase agreement with minority shareholders of Pinecone Cayman Limited ("**Pinecone Cayman**") to obtain certain indirect equity interest in it, as a result, the Group's shareholding interest in Beijing Pinecone Electronics Co., Ltd. which was indirectly owned by Pinecone Cayman changed from 72% to 100%.

(c) The Company considered that the non-wholly owned subsidiaries with non-controlling interests are not significant to the Group, therefore, no summarized financial information of these non-wholly owned subsidiaries is presented separately.

(d) The English names of the subsidiaries are direct translation or transliteration of their Chinese registered names.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 11(b) Investments accounted for using the equity method

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Investments in associate accounted for using the equity method | | |
| — Listed entities | 5,499,386 | 6,198,681 |
| — Unlisted entities | 3,801,121 | 2,440,557 |
| | 9,300,507 | 8,639,238 |

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| **At the beginning of the year** | 8,639,238 | 1,710,819 |
| Additions (Note (a),(b)) | 1,197,944 | 7,289,333 |
| Disposal | (93,596) | (100) |
| Share of losses | (671,822) | (614,920) |
| Share of other comprehensive income | 9,279 | 191,449 |
| Share of changes of other reserves | 229,740 | 62,657 |
| Dividends from associates | (10,276) | — |
| **At the end of the year** | 9,300,507 | 8,639,238 |

Notes:

(a) In April 2019, Ninebot Limited ("**Ninebot**"), an investment engaging in the operation of developing and selling IoT-enabled smart mobility products mainly in mainland China, for which the Group accounted as long-term investments measured at fair value through profit or loss, was accepted by the Shanghai Stock Exchange for its listing application on the Sci-Tech Innovation Board (STAR Market). The conversion of the preference shares in Ninebot owned by the Group into ordinary shares was completed on April 17, 2019, following which the Group reclassified the investment in associate measured at fair value through profit or loss to an investment accounted for using the equity method.

(b) In June 2019, Shanghai Sunmi Technology Co., Ltd. ("**Sunmi**"), an investment engaging in the provision of a full range of intelligent hardware solutions based on Android's operating system for commercial applications in mainland China, for which the Group accounted as long-term investments measured at fair value through profit or loss, underwent the overall change from a limited liability company to a joint stock company. The conversion of the preference shares in Sunmi owned by the Group into ordinary shares was completed on June 28, 2019, following which the Group reclassified the investment in associate measured at fair value through profit or loss to an investment accounted for using the equity method.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 11(b) Investments accounted for using the equity method (continued)

Management has assessed the level of influence that the Group exercises on certain associates and determined that it has significant influence through the board representation, even though the respective shareholding of some investments is below 20%. Accordingly, these investments have been classified as associates.

Set out below are the material associates of the Group as of December 31, 2019 and 2018. The associates as listed below are ordinary shares investment, which held directly by the Group. Mainland China is their principal place of business. The proportion of ownership interest is the same as the proportion of voting rights held.

| Name of entity | Place of incorporation | % of Ownership interest | Principal activities | Quoted fair value As of December 31, 2019 RMB'000 | Quoted fair value As of December 31, 2018 RMB'000 | Carrying amount As of December 31, 2019 RMB'000 | Carrying amount As of December 31, 2018 RMB'000 |
|---|---|---|---|---|---|---|---|
| Sichuan Xin Wang Bank Co., Ltd. ("**XW Bank**") | Mainland China | 29.5 | Provision of internet banking service | NA | NA | 1,269,913 | 936,908 |
| iQIYI, Inc. ("**iQIYI**") | Cayman Islands | 6.7 | Provision of internet video streaming services | 7,192,441 | 4,984,330 | 3,769,444 | 4,377,472 |

The associates of the Group have been accounted by using the equity method based on the financial information of the associates prepared under the accounting policies consistent with the Group.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 11(b)Investments accounted for using the equity method (continued)

Set out below are the summarized financial information of material associates.

| | XW Bank | | iQIYI | |
|---|---|---|---|---|
| | As of December 31, | | As of December 31, | |
| | 2019 | 2018 | 2019 | 2018 |
| | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| **Summarized consolidated balance sheets** | | | | |
| Current assets | 10,427,012 | 28,137,561 | 20,272,838 | 19,853,443 |
| Non-current assets | 33,726,206 | 8,021,166 | 34,721,946 | 35,736,050 |
| Current liabilities | 21,007,556 | 28,454,306 | 20,173,166 | 19,812,356 |
| Non-current liabilities | 18,840,873 | 4,528,463 | 17,455,010 | 9,499,228 |
| Redeemable non-controlling interests | — | — | 101,542 | — |
| Non-controlling interests | — | — | 42,376 | 118,632 |
| Equity attributable to owners of the Company | 4,304,789 | 3,175,958 | 17,222,690 | 26,159,277 |
| **Reconciliation to carrying amounts:** | | | | |
| Group's share of net assets attributable to owners of the associates | 1,269,913 | 936,908 | 1,160,011 | 1,768,039 |
| Adjustment | | | | |
| — Goodwill | — | — | 2,609,433 | 2,609,433 |
| Carrying amount | 1,269,913 | 936,908 | 3,769,444 | 4,377,472 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 11(b) Investments accounted for using the equity method (continued)

| | XW Bank | | iQIYI | |
|---|---|---|---|---|
| | Year ended December 31, | | Year ended December 31, | |
| | 2019 | 2018 | 2019 | 2018 |
| | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| **Summarized consolidated income statements and consolidated statements of comprehensive income** | | | | |
| Revenues | 2,680,662 | 1,160,403 | 28,993,658 | 24,989,116 |
| Profit/(loss) from operations | 1,302,822 | 461,099 | (9,728,508) | (8,420,635) |
| Profit/(loss) before tax | 1,302,121 | 460,343 | (10,695,558) | (9,096,829) |
| Net profit/(loss) | 1,133,181 | 371,470 | (10,747,410) | (9,175,630) |
| Other comprehensive (loss)/income | — | (711) | 226,772 | 1,786,820 |
| Total comprehensive income/(loss) | 1,133,181 | 370,759 | (10,520,638) | (7,388,810) |

In addition to the interests in associates disclosed above, the Group also has interests in a number of individually immaterial associates that are accounted for using the equity method.

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Aggregate carrying amount of individually immaterial associates | 4,261,150 | 3,324,858 |
| Aggregate amounts of the Group's share of: | | |
| Net loss | (271,592) | (108,184) |
| Other comprehensive (loss)/income | (5,996) | 45,587 |
| Total comprehensive loss | (277,588) | (62,597) |

There are no contingent liabilities relating to the Group's interests in the associates.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12 Income tax expenses

The income tax expenses of the Group during the years ended December 31, 2019 and 2018 are analyzed as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Current income tax | 2,228,609 | 1,414,602 |
| Deferred income tax (Note 34) | (168,913) | (965,225) |
| Income tax expenses | 2,059,696 | 449,377 |

The tax on the Group's profit before income tax differs from the theoretical amount that would arise using the statutory tax rate of 25% in mainland China, being the tax rate applicable to the majority of consolidated entities as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Profit before income tax | 12,162,646 | 13,927,124 |
| Tax calculated at statutory income tax rate of 25% in mainland China (Note (a)) | 3,040,662 | 3,481,781 |
| Tax effects of: | | |
| — Effect of different tax rates in other jurisdictions (Note (b),(c),(d)) | (617,082) | (2,037,227) |
| — Preferential income tax rates applicable to subsidiaries (Note (e)) | (1,055,387) | (1,017,178) |
| — Tax losses and temporary differences for which no deferred income tax assets was recognized | 347,222 | 115,452 |
| — Expenses not deductible for income tax purposes | 721,596 | 588,839 |
| — Utilization of previously unrecognized deductible tax losses and temporary differences | (25,515) | (89,626) |
| — Recognition of previously unrecognized deductible tax losses and temporary differences | (285,756) | — |
| — Super Deduction for research and development expenses (Note (f)) | (301,835) | (166,794) |
| — Income not subject to tax | (117,241) | (157,306) |
| — Tax refund (Note (e)) | — | (270,757) |
| — Reversal of deferred income tax assets | 350,959 | — |
| — Others | 2,073 | 2,193 |
| Income tax expenses | 2,059,696 | 449,377 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12 Income tax expenses (continued)

Notes:

(a) Enterprise income tax in mainland China ("**EIT**")

The income tax provision of the Group in respect of its operations in mainland China was calculated at tax rate of 25% on the assessable profits for the periods presented, based on the existing legislation, interpretations and practices in respect thereof.

(b) Cayman Islands and British Virgin Islands income tax

The Company is incorporated in the Cayman Islands as an exempted company with limited liability under the Companies Law of the Cayman Islands and accordingly, is exempted from Cayman Islands income tax. As such, the operating results reported by the Company, including the fair value gain of Preferred Shares (Note 35) and the share-based payments (Note 28), are not subject to any income tax.

The Group entities established under the International Business Companies Acts of British Virgin Islands ("**BVI**") are exempt from BVI income taxes.

(c) Hong Kong income tax

Entities incorporated in Hong Kong are subject to Hong Kong profits tax of which the tax rate was 16.5% up to April 1, 2018 when the two-tiered profits tax regime took effect, under which the tax rate is 8.25% for assessable profits in the first HK$2 million and 16.5% for any assessable profits in excess.

(d) India income tax

The income tax provision for India entities were calculated at corporate income tax rates of 35% before April 1, 2019, after then 25% on the assessable profits, based on the existing legislation, interpretations and practices in respect thereof.

(e) Preferential EIT rate

Certain subsidiaries are entitled to preferential tax rates ranging from 10% to 15%. Main subsidiaries with preferential EIT rates are as follows:

Beijing Xiaomi Mobile Software Co., Ltd. ("**Xiaomi Mobile**") was qualified as a "Key Software Enterprise" in the third quarter of 2018, hence it enjoys a preferential income tax rate of 10% retroactively from January 1, 2017. Accordingly, Xiaomi Mobile was entitled to tax refund for the income tax paid in 2017 and such tax refund was received by Xiaomi Mobile from local tax bureau in December 2018. Xiaomi Mobile enjoys the preferential EIT rate of 10% for the years ended December 31, 2019 and 2018.

Beijing Xiaomi Digital Technology Co., Ltd. was qualified as a "High and New Technology Enterprise" in November 2018, hence it enjoys a preferential income tax rate of 15% for three years from 2018 to 2020.

(f) Super Deduction for research and development expense

According to the relevant laws and regulations promulgated by the State Council of the People's Republic of China that was effective from 2008 onwards, enterprises engaging in research and development activities were entitled to claim 150% of their research and development expenses so incurred as tax deductible expenses when determining their assessable profits for that year ("**Super Deduction**"). The State Taxation Administration of The People's Republic of China announced in September 2018 that enterprises engaging in research and development activities would entitle to claim 175% of their research and development expenses as Super Deduction from January 1, 2018 to December 31, 2020. The Group has made its best estimate for the Super Deduction to be claimed for the Group's entities in ascertaining their assessable profits during the year.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 12 Income tax expenses (continued)

Notes (continued):

(g) Withholding tax in mainland China ("**WHT**")

According to the New Corporate Income Tax Law ("**New EIT Law**"), distribution of profits earned by companies in mainland China since January 1, 2008 to foreign investors is subject to withholding tax of 5% or 10%, depending on the country of incorporation of the foreign investors, upon the distribution of profits to overseas-incorporated immediate holding companies.

The Group does not have any plan in the foreseeable future to require its subsidiaries in mainland China to distribute their retained earnings and intends to retain them to operate and expand its business in mainland China. Accordingly, no deferred income tax liability related to WHT on undistributed earnings was accrued as of the end of each reporting period.

## 13 Earnings per share

On June 17, 2018, pursuant to the shareholders' resolution, each existing issued and unissued share of US$0.000025 each in the share capital of the Company were subdivided into 10 shares of US$0.0000025 each ("**Share Subdivision**"). Following the Share Subdivision, the weighted average number of ordinary shares for the purpose of basic and diluted earnings per share for the year ended December 31, 2018 has been retrospectively adjusted.

### (a) Basic

Basic earnings per share for the years ended December 31, 2019 and 2018 are calculated by dividing the profit or loss attributable to the Company's owners by the weighted average number of ordinary shares in issue during the year.

| | Year ended December 31, 2019 RMB'000 | 2018 RMB'000 |
|---|---|---|
| Net profit attributable to the owners of the Company | **10,044,164** | 13,553,886 |
| Weighted average number of ordinary shares in issue (thousand shares) | **23,746,463** | 16,069,770 |
| Basic earnings per share (expressed in RMB per share) | **0.423** | 0.843 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 13 Earnings per share (continued)

### (b) Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares.

| | Year ended December 31, | |
|---|---|---|
| | **2019** | 2018 |
| | **RMB'000** | RMB'000 |
| Net profit attributable to the owners of the Company | **10,044,164** | 13,553,886 |
| Less: fair value gain of Preferred Shares | **—** | (12,514,279) |
| Net profit used to determine diluted earnings per share | **10,044,164** | 1,039,607 |
| Weighted average number of ordinary shares in issue (thousand shares) | **23,746,463** | 16,069,770 |
| Adjustments for Preferred Shares (thousand shares) | **—** | 5,468,315 |
| Adjustments for RSUs and share options granted to employees (thousand shares) | **762,301** | 2,024,845 |
| Weighted average number of ordinary shares for calculation of diluted earnings per share (thousand shares) | **24,508,764** | 23,562,930 |
| Diluted earnings per share (expressed in RMB per share) | **0.410** | 0.044 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 14 Property and equipment

| | Electronic equipment RMB'000 | Office equipment RMB'000 | Buildings RMB'000 | Leasehold improvements RMB'000 | Construction in progress RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|
| **At January 1, 2019** | | | | | | |
| Cost | 642,723 | 33,932 | — | 564,076 | 4,543,071 | 5,783,802 |
| Accumulated depreciation | (379,599) | (15,627) | — | (320,523) | — | (715,749) |
| **Net book amount** | 263,124 | 18,305 | — | 243,553 | 4,543,071 | 5,068,053 |
| **Year ended December 31, 2019** | | | | | | |
| Opening net book amount | 263,124 | 18,305 | — | 243,553 | 4,543,071 | 5,068,053 |
| Currency translation differences | 288 | 50 | — | (2,950) | 1 | (2,611) |
| Additions | 372,180 | 2,274 | — | 247,015 | 2,511,206 | 3,132,675 |
| Transfer from construction in progress to buildings | — | — | 2,974,650 | — | (2,974,650) | — |
| Disposal | (50,990) | (10,836) | — | (28,579) | (31,690) | (122,095) |
| Transfer to investment properties (Note 17) | — | — | (707,268) | — | (52,512) | (759,780) |
| Depreciation charge (Note 8) | (126,176) | (2,420) | (17,636) | (177,679) | — | (323,911) |
| **Closing net book amount** | 458,426 | 7,373 | 2,249,746 | 281,360 | 3,995,426 | 6,992,331 |
| **At December 31, 2019** | | | | | | |
| Cost | 887,568 | 22,789 | 2,267,382 | 775,970 | 3,995,426 | 7,949,135 |
| Accumulated depreciation | (429,142) | (15,416) | (17,636) | (494,610) | — | (956,804) |
| **Net book amount** | 458,426 | 7,373 | 2,249,746 | 281,360 | 3,995,426 | 6,992,331 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 14 Property and equipment (continued)

| | Electronic equipment RMB'000 | Office equipment RMB'000 | Buildings RMB'000 | Leasehold improvements RMB'000 | Construction in progress RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|
| **At January 1, 2018** | | | | | | |
| Cost | 422,515 | 14,317 | — | 331,083 | 1,473,761 | 2,241,676 |
| Accumulated depreciation | (297,588) | (11,870) | — | (201,346) | — | (510,804) |
| **Net book amount** | 124,927 | 2,447 | — | 129,737 | 1,473,761 | 1,730,872 |
| **Year ended December 31, 2018** | | | | | | |
| Opening net book amount | 124,927 | 2,447 | — | 129,737 | 1,473,761 | 1,730,872 |
| Currency translation differences | (330) | (13) | — | (1,010) | 13 | (1,340) |
| Additions | 242,843 | 19,612 | — | 243,364 | 3,119,183 | 3,625,002 |
| Disposals/transfer | (17,071) | (1) | — | — | (49,886) | (66,958) |
| Depreciation charge (Note 8) | (87,245) | (3,740) | — | (128,538) | — | (219,523) |
| **Closing net book amount** | 263,124 | 18,305 | — | 243,553 | 4,543,071 | 5,068,053 |
| **At December 31, 2018** | | | | | | |
| Cost | 642,723 | 33,932 | — | 564,076 | 4,543,071 | 5,783,802 |
| Accumulated depreciation | (379,599) | (15,627) | — | (320,523) | — | (715,749) |
| **Net book amount** | 263,124 | 18,305 | — | 243,553 | 4,543,071 | 5,068,053 |

Construction in progress as of December 31, 2019 and 2018 mainly comprises new office buildings being constructed in mainland China.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 14 Property and equipment (continued)

Depreciation expenses have been charged to the consolidated income statement as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Administrative expenses | 109,466 | 61,216 |
| Selling and marketing expenses | 124,624 | 98,941 |
| Research and development expenses | 75,223 | 59,366 |
| Cost of sales | 14,598 | — |
| | 323,911 | 219,523 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 15 Intangible assets

| | Goodwill (Note (a)) RMB'000 | License RMB'000 | Trademarks, patents and domain name RMB'000 | Others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|
| **At January 1, 2019** | | | | | |
| Cost | 282,090 | 1,408,219 | 1,084,466 | 224,578 | 2,999,353 |
| Accumulated amortization | — | (395,806) | (416,547) | (125,808) | (938,161) |
| **Net book amount** | 282,090 | 1,012,413 | 667,919 | 98,770 | 2,061,192 |
| **Year ended December 31, 2019** | | | | | |
| Opening net book amount | 282,090 | 1,012,413 | 667,919 | 98,770 | 2,061,192 |
| Currency translation differences | — | (29) | (1,200) | 402 | (827) |
| Additions | — | 18,820 | 6,461 | 116,231 | 141,512 |
| Disposals | (33,923) | — | (9,889) | (277) | (44,089) |
| Amortization charge (Note 8) | — | (331,803) | (112,481) | (41,502) | (485,786) |
| **Closing net book amount** | 248,167 | 699,401 | 550,810 | 173,624 | 1,672,002 |
| **At December 31, 2019** | | | | | |
| Cost | 248,167 | 1,426,992 | 1,080,599 | 340,711 | 3,096,469 |
| Accumulated amortization | — | (727,591) | (529,789) | (167,087) | (1,424,467) |
| **Net book amount** | 248,167 | 699,401 | 550,810 | 173,624 | 1,672,002 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 15 Intangible assets (continued)

| | Goodwill (Note (a)) RMB'000 | License RMB'000 | Trademarks, patents and domain name RMB'000 | Others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|
| **At January 1, 2018** | | | | | |
| Cost | 248,167 | 1,343,686 | 1,003,239 | 107,792 | 2,702,884 |
| Accumulated amortization | — | (63,735) | (280,034) | (84,763) | (428,532) |
| **Net book amount** | 248,167 | 1,279,951 | 723,205 | 23,029 | 2,274,352 |
| **Year ended December 31, 2018** | | | | | |
| Opening net book amount | 248,167 | 1,279,951 | 723,205 | 23,029 | 2,274,352 |
| Currency translation differences | — | — | (10,049) | (106) | (10,155) |
| Additions | 33,923 | 71,723 | 110,283 | 116,949 | 332,878 |
| Disposals | — | (7,190) | — | — | (7,190) |
| Amortization charge (Note 8) | — | (332,071) | (155,520) | (41,102) | (528,693) |
| **Closing net book amount** | 282,090 | 1,012,413 | 667,919 | 98,770 | 2,061,192 |
| **At December 31, 2018** | | | | | |
| Cost | 282,090 | 1,408,219 | 1,084,466 | 224,578 | 2,999,353 |
| Accumulated amortization | — | (395,806) | (416,547) | (125,808) | (938,161) |
| **Net book amount** | 282,090 | 1,012,413 | 667,919 | 98,770 | 2,061,192 |

Note:

(a) For the purpose of impairment tests of goodwill, goodwill is allocated to groups of cash-generating units. Such groups of cash-generating units represent the lowest level within the Group for which the goodwill is monitored for internal management purpose.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 15 Intangible assets (continued)

Note (continued):

Impairment review on the goodwill of the Group has been conducted by the management as of December 31, 2019 and 2018 according to IAS 36 "Impairment of assets". For the purposes of impairment review, the recoverable amount of goodwill is determined based on value-in-use calculations by using the discounted cash flow method. Management forecasted the average annual revenue growth rate in five-year period is 5%, and the cash flows beyond the five-year period were extrapolated using the estimated annual growth rates of 2%. Pre-tax discount rate of 20% was used to reflect market assessment of time value and the specific risks relating to the CGUs.

The management performed impairment test for the goodwill and determined such goodwill was not impaired. Reasonably possible changes in key assumptions will not lead to the goodwill impairment loss as of December 31, 2019 and 2018.

Amortization charges were expensed off in the following categories in the consolidated income statement:

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Administrative expenses | 33,968 | 77,468 |
| Selling and marketing expenses | 1,080 | 648 |
| Research and development expenses | 450,738 | 450,577 |
| | 485,786 | 528,693 |

The Group tests annually whether goodwill and other intangible assets with an indefinite useful life have suffered any impairment. During the years ended December 31, 2019 and 2018, no goodwill or other identifiable intangible assets have been impaired.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 16 Leases

| | As of December 31, 2019 RMB'000 | As of January 1, 2019 RMB'000 |
|---|---|---|
| *(i) The consolidated balance sheet includes the following amounts relating to leases:* | | |
| **Right-of-use assets (Note(a))** | | |
| Land use rights | 2,859,297 | 3,389,731 |
| Properties | 915,581 | 859,454 |
| Other assets | 58,222 | 32,754 |
| | 3,833,100 | 4,281,939 |
| **Lease liabilities (Note(b))** | | |
| Current | (399,444) | (285,402) |
| Non-current | (560,804) | (573,431) |
| | (960,248) | (858,833) |

Notes:

(a) Included in the line item 'Other non-current assets' in the consolidated balance sheet.

(b) Current lease liabilities and non-current lease liabilities are included in the line item 'Other payables and accruals' and 'Other non-current liabilities' in the consolidated balance sheet, respectively.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 16 Leases (continued)

| | Year ended December 31, 2019 RMB'000 |
|---|---|
| *(ii) The consolidated income statement shows the following amounts relating to leases:* | |
| Depreciation charge of right-of-use assets | 571,336 |
| Interest expense (included in finance income, net) | 45,881 |
| Expense relating to short-term leases not included in lease liabilities (included in cost of sales and expenses) | 563,400 |
| | 1,180,617 |

Besides land use rights, the Group leases offices, warehouses, retail stores and servers. No variable lease payments were contained in lease contracts during the year ended December 31, 2019.

The total cash outflow in financing activities for leases during the year ended December 31, 2019 was RMB578,063,000, including principal elements of lease payments of approximately RMB532,182,000 and related interest paid of approximately RMB45,881,000, respectively.

## 17 Other non-current assets

| | As of December 31, | |
|---|---|---|
| | 2019 RMB'000 | 2018 RMB'000 |
| Right-of-use assets (Note 16) | 3,833,100 | — |
| Investment properties (Note (a)) | 1,250,932 | — |
| Long-term bank deposits | 590,157 | 992 |
| Others | 488,314 | 94,493 |
| | 6,162,503 | 95,485 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 17 Other non-current assets (continued)

Note:

(a) Investment properties

| | Buildings and facilities RMB'000 | Land use right RMB'000 | Investment properties in constructions RMB'000 | Total RMB'000 |
|---|---|---|---|---|
| COST | | | | |
| At January 1, 2019 | — | — | — | — |
| Transfer from property and equipment | 711,432 | — | 52,512 | 763,944 |
| Transfer from right-of-use assets | — | 504,895 | — | 504,895 |
| Addition | — | — | 26,801 | 26,801 |
| **At December 31, 2019** | 711,432 | 504,895 | 79,313 | 1,295,640 |
| ACCUMULATED DEPRECIATION | | | | |
| At January 1, 2019 | — | — | — | — |
| Charge for the year (Note 8) | (26) | — | — | (26) |
| Transfer from property and equipment | (4,164) | — | — | (4,164) |
| Transfer from right-of-use assets | — | (40,518) | — | (40,518) |
| **At December 31, 2019** | (4,190) | (40,518) | — | (44,708) |
| NET BOOK VALUE | | | | |
| **At December 31, 2019** | 707,242 | 464,377 | 79,313 | 1,250,932 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 17 Other non-current assets (continued)

Note (continued):

(a) Investment properties (continued)

(i) Details of the Group's main investment properties and information about the fair value hierarchy as of December 31, 2019 are as follows:

| | As of December 31, 2019 | |
|---|---|---|
| | Carrying amount RMB'000 | Fair value (level 3) RMB'000 |
| Investment property units located in Haidian, Beijing | 1,148,225 | 1,557,120 |

The investment property units located in Haidian, Beijing were valued at December 31, 2019 by Asia-Pacific Consulting and Appraisal Limited, which is an independent qualified valuer. The valuation was determined on the basis of capitalisation of the net rental income with due provisions for reversionary income potential of the respective properties as of December 31, 2019. The key inputs were term yield and reversionary yield.

The above investment properties are leased to tenants under operating leases with rentals payable semiannually. Lease payments for the contracts include CPI increases, but there are no other variable lease payments that depend on an index or rate. Although the Group is exposed to changes in the residual value at the end of the current leases, the Group typically enters into new operating leases and therefore will not immediately realize any reduction in residual value at the end of these leases. Expectations about the future residual values are reflected in the fair value of the properties as disclosed above.

(ii) Property rental income earned during the year ended December 31, 2019 was approximately RMB8,746,000. The investment property units located in Haidian, Beijing has committed tenants for the next 6 years. The investment properties in constructions located in Yizhuang, Beijing has committed tenants for the next 14 years. As of December 31, 2019, the Group had future minimum lease receipts under non-cancellable operating leases as follows:

| | As of December 31, 2019 RMB'000 |
|---|---|
| No later than 1 year | 94,722 |
| Later than 1 year and no later than 14 years | 570,070 |
| | 664,792 |

(iii) Depreciation charges of approximately RMB26,000 for the year ended December 31, 2019 have been charged in profit or loss.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 18 Financial instruments by category

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| **Assets as per balance sheet** | | |
| Financial assets measured at fair value through profit or loss: | | |
| — Long-term investments measured at fair value through profit or loss (Note 19) | 20,679,363 | 18,636,208 |
| — Short-term investments measured at fair value through profit or loss (Note 19) | 16,463,390 | 6,648,526 |
| Financial assets measured at amortized costs: | | |
| — Trade receivables (Note 21) | 6,948,567 | 5,598,443 |
| — Loan receivables (Note 20) | 12,723,503 | 10,293,645 |
| — Other receivables | 12,246,498 | 12,408,170 |
| — Long-term bank deposits (Note 17) | 590,157 | 992 |
| — Short-term bank deposits (Note 24(c)) | 21,523,043 | 1,365,991 |
| — Restricted cash (Note 24(b)) | 1,538,266 | 1,480,178 |
| — Cash and cash equivalents (Note 24(a)) | 25,919,861 | 30,230,147 |
| | 118,632,648 | 86,662,300 |
| **Liabilities as per balance sheet** | | |
| Financial liabilities measured at amortized cost: | | |
| — Trade payables (Note 30) | 59,527,940 | 46,287,271 |
| — Other payables | 6,080,191 | 4,805,101 |
| — Borrowings (Note 33) | 17,623,411 | 10,931,337 |
| — Investment from fund investors (Note 29) | 3,074,210 | 2,823,504 |
| — Lease liabilities (Note 16) | 960,248 | — |
| | 87,266,000 | 64,847,213 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 19 Investments

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| **Current assets** | | |
| Short-term investments measured at fair value through profit or loss (i) | 16,463,390 | 6,648,526 |
| **Non-current assets** | | |
| Long-term investments measured at fair value through profit or loss | | |
| — Equity investments (ii) | 7,272,454 | 7,629,929 |
| — Preferred shares investments (iii) | 13,406,909 | 11,006,279 |
| | 20,679,363 | 18,636,208 |

### (i) Short-term investments measured at fair value through profit or loss

The short-term investments measured at fair value through profit or loss are wealth management products, denominated in RMB, with expected rates of return ranging from 1.76% to 4.60% per annum for the year ended December 31, 2019 (2018: 2.20% to 5.15%). The returns on all of these wealth management products are not guaranteed, hence their contractual cash flows do not qualify for solely payments of principal and interest. Therefore they are measured at fair value through profit or loss. None of these investments are past due.

The fair values are based on cash flow discounted using the expected return based on management judgment and are within level 3 of the fair value hierarchy.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 19 Investments (continued)

### (ii) Equity investments

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Listed | **4,778,263** | 5,215,898 |
| Unlisted | **2,494,191** | 2,414,031 |
| | **7,272,454** | 7,629,929 |

The fair values of the listed securities are determined based on the closing prices quoted in active markets. They are accounted for using their fair values based on quoted market prices (level 1: quoted price (unadjusted) in active markets) without any deduction for transaction costs. For certain listed securities which are restricted for sale in a specified period, their fair values are determined based on quoted market prices and unobservable inputs (i.e. discount rate for lack of marketability) and hence classified as level 3 of the fair value hierarchy. And as of December 31, 2019, the Group has not elected to recognize the fair value gains or losses on equity investments in OCI.

The fair values of unlisted securities are measured using a valuation technique with unobservable inputs and hence classified as level 3 of the fair value hierarchy. The major assumptions used in the valuation for investment in private companies refer to Note 3.3.

### (iii) Preferred shares investments

During the year ended December 31, 2019, the Group made aggregate preferred shares investments of RMB2,675,086,000 (2018: RMB1,102,118,000). These investees are principally engaged in sales of goods and provision of internet services.

All of these investments are convertible redeemable preferred shares or ordinary shares with preferential rights. The Group has the right to require and demand the investees to redeem all of the shares held by the Group at guaranteed predetermined fixed amount upon redemption events which are out of control of issuers. Hence, these investments are accounted for as debt instruments and are measured at financial assets at fair value through profit or loss.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 19 Investments (continued)

### (iii) Preferred shares investments (continued)

The conversion of the preference shares in Ninebot and Sunmi owned by the Group into ordinary shares was completed on April 17, 2019 and June 28, 2019, respectively, following which the Group reclassifies the investments to be accounted for using the equity method (Note 11(b)).

### (iv) Amounts recognized in profit or loss

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Fair value changes on equity investments | 2,322,349 | (1,386,967) |
| Fair value changes on preferred shares investments | 1,452,273 | 5,793,800 |
| Fair value changes on short-term investments measured at fair value through profit or loss | 38,390 | 23,526 |
| | 3,813,012 | 4,430,359 |

## 20 Loan receivables

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Unsecured loan | 14,393,240 | 10,995,510 |
| Less: credit loss allowance | (1,669,737) | (701,865) |
| | 12,723,503 | 10,293,645 |

Loan receivables are loans derived from subsidiaries of the Group which engages in the fintech business. Such amounts are recorded at the principal amount less credit loss allowance. The loan periods extended by the Group to the individuals generally range from 3 months to 12 months. Loan receivables are mainly denominated in RMB.

Detail of the credit risk assessment of loan receivables is disclosed in Note 3.1.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 21 Trade receivables

Trade receivables analysis is as follows:

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Third parties | 6,740,321 | 5,302,432 |
| Related parties | 324,027 | 364,608 |
| | 7,064,348 | 5,667,040 |
| Less: credit loss allowance | (115,781) | (68,597) |
| | 6,948,567 | 5,598,443 |

The carrying amounts of the Group's trade receivables are denominated in the following currencies:

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| RMB | 3,757,863 | 3,285,845 |
| INR | 1,758,770 | 1,464,621 |
| US$ | 1,239,122 | 795,971 |
| Others | 192,812 | 52,006 |
| | 6,948,567 | 5,598,443 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 21 Trade receivables (continued)

Movements on the Group's credit loss allowance of trade receivables are as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| At the beginning of the year | (68,597) | (56,820) |
| Credit loss allowance recognized, net | (79,712) | (11,777) |
| Receivables written off during the year as uncollectable | 32,528 | — |
| At the end of the year | (115,781) | (68,597) |

(a) The Group generally allows a credit period within 180 days to its customers. Aging analysis of trade receivables based on invoice date is as follows:

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| **Trade receivables** | | |
| Up to 3 months | 6,076,873 | 5,094,390 |
| 3 to 6 months | 550,929 | 392,868 |
| 6 months to 1 year | 308,197 | 116,279 |
| 1 to 2 years | 98,643 | 16,630 |
| Over 2 years | 29,706 | 46,873 |
| | 7,064,348 | 5,667,040 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 21 Trade receivables (continued)

(b) The Group applies the simplified approach to providing for expected credit losses prescribed by IFRS 9, which permits the use of the lifetime expected loss provision for all trade receivables. To measure the expected credit losses, trade receivables have been grouped based on shared credit risk characteristics and the days past due. The expected credit losses below also incorporate forward looking information. The loss provisions as of December 31, 2018 and 2019 are determined as follows:

| | Current | Up to 3 months past due | 3 to 6 months past due | Over 6 months past due | Total |
|---|---|---|---|---|---|
| **December 31, 2019:** | | | | | |
| Expected loss rate | 0.03% | 1.29% | 9.55% | 50.14% | |
| Gross carrying amount (in thousand) | 5,822,380 | 856,086 | 222,699 | 163,183 | 7,064,348 |
| Loss provision (in thousand) | 1,627 | 11,066 | 21,269 | 81,819 | 115,781 |
| **December 31, 2018:** | | | | | |
| Expected loss rate | 0.01% | 0.99% | 34.22% | 52.85% | |
| Gross carrying amount (in thousand) | 4,992,793 | 532,901 | 64,006 | 77,340 | 5,667,040 |
| Loss provision (in thousand) | 562 | 5,261 | 21,902 | 40,872 | 68,597 |

As of December 31, 2019 and 2018, the majority of the balance of receivables are due from certain channel distributors and customers in mainland China and India who usually settle the amounts due by them within 180 days.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 22 Prepayments and other receivables

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Receivables from subcontractors for outsourcing of raw materials and amounts paid for third parties | 9,292,072 | 10,043,378 |
| Recoverable value-added tax and other taxes | 6,782,745 | 7,811,161 |
| Prepayments to suppliers | 394,090 | 467,418 |
| Deposits to suppliers | 375,868 | 569,598 |
| Receivables from market development fund | 895,773 | 822,809 |
| Prepaid fees for patent expenses and other prepaid expenses | 413,685 | 228,197 |
| Receivables from import and export agents | 186 | 52,263 |
| Receivables from employees related to Employee Fund (Note (a)) | 103,900 | 110,950 |
| Interest receivables | 254,912 | 231,819 |
| Receivables from disposal of investments | 4,306 | 35,226 |
| Loans to related parties (Note (b)) | 37,802 | 7,979 |
| Receivables related to share options and RSUs granted to employees | 862,545 | — |
| Others | 419,134 | 534,148 |
| | 19,837,018 | 20,914,946 |

Notes:

(a) Receivables from employees related to Employee Fund is interest bearing and repayable when the employee resign from the Group. Further detail included in Note 28.

(b) Loans to related parties were unsecured, repayable on demand and carried interest rate at ceiling of 8% per annum (2018: 8%).

As of December 31, 2019 and 2018, the carrying amounts of other receivables were primarily denominated in RMB and US$ and approximated their fair value at each of the reporting dates. Other receivables that are measured at amortized costs included receivables from subcontractors for outsourcing of raw materials and amounts paid for third parties, receivables from import and export agents, receivables from market development fund, receivables from employees related to Employee Fund, receivables from disposal of investments, interest receivables, loans to related parties, receivables related to share options and RSUs granted to employees and others were considered to be of low credit risk, and thus credit loss allowance recognized during the year ended December 31, 2019 and 2018 was limited to 12 months expected losses.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 23 Inventories

| | As of December 31, 2019 RMB'000 | 2018 RMB'000 |
|---|---|---|
| Raw materials | 9,347,930 | 7,343,118 |
| Finished goods | 18,030,136 | 19,112,105 |
| Work in progress | 2,422,504 | 2,068,834 |
| Spare parts | 1,733,042 | 1,156,825 |
| Others | 1,925,785 | 1,651,854 |
| | 33,459,397 | 31,332,736 |
| Less: provision for impairment (Note (a)) | (873,959) | (1,852,051) |
| | 32,585,438 | 29,480,685 |

Note:

(a) Provision for impairment was recognized for the amount by which the carrying amount of the inventories exceeds its net realizable value, and was recorded in "cost of sales" in the consolidated income statements. The provision for impairment expense of inventory amounted to RMB3,859,675,000 for the year ended December 31, 2019 (2018: RMB3,006,525,000).

Provision for impairment movements for the years ended December 31, 2019 and 2018 are as below:

| | Year ended December 31, 2019 RMB'000 | 2018 RMB'000 |
|---|---|---|
| At the beginning of the year | (1,852,051) | (668,142) |
| Provision for impairment | (3,859,675) | (3,006,525) |
| Transfer to cost of sales upon sold | 4,837,767 | 1,822,616 |
| At the end of the year | (873,959) | (1,852,051) |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 24 Cash and bank balances

### (a) Cash and cash equivalents

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Cash at bank and in hand | 13,355,455 | 10,958,910 |
| Short-term bank deposits with initial terms within three months | 12,564,406 | 19,271,237 |
| | 25,919,861 | 30,230,147 |

Cash and cash equivalents are denominated in the following currencies:

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| US$ | 10,322,132 | 22,189,594 |
| RMB | 9,217,142 | 7,192,491 |
| INR | 3,500,056 | 532,838 |
| Others | 2,880,531 | 315,224 |
| | 25,919,861 | 30,230,147 |

The weighted average effective interest rate for the short-term bank deposits with initial terms within three months was 2.76% per annum for the year ended December 31, 2019 (2018: 3.24%).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 24 Cash and bank balances (continued)

### (b) Restricted cash

As of December 31, 2019, among of the restricted cash, RMB700,987,000 was held at bank to meet requirements of People's Bank of China for reserves of payment institutions, US$84,260,000 (equivalent to approximately RMB587,815,000) was held at Bank of China as guarantee for bank loans. RMB149,427,000 was held at Bank of Ningbo as guarantee for bank acceptance bills.

### (c) Short-term bank deposits

An analysis of the Group's short-term bank deposits as of December 31, 2019 and 2018 are listed as below:

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Short-term bank deposits denominated in RMB | — | 460,000 |
| Short-term bank deposits denominated in INR | 392,823 | 49 |
| Short-term bank deposits denominated in US$ | 20,597,231 | 905,942 |
| Short-term bank deposits denominated in HK$ | 532,989 | — |
| | 21,523,043 | 1,365,991 |

Short-term bank deposits are bank deposits with original maturities over three months and redeemable on maturity.

The effective interest rate of the short-term bank deposits of the Group ranges from 2.38% to 7.30% per annum for the year ended December 31, 2019 (2018: from 2.25% to 6.00%).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 25 Share capital and treasury shares

### (a) Share capital

Authorized:

| | Note | Number of ordinary shares '000 | Nominal value of ordinary shares US$'000 | Number of Preferred Shares '000 | Nominal value of Preferred Shares US$'000 |
|---|---|---|---|---|---|
| **As of January 1, 2018** | | 3,489,594 | 87 | 1,051,251 | 26 |
| Effect of Share Subdivision | (a) | 31,406,344 | — | 9,461,254 | — |
| Conversion of Preferred Shares to ordinary shares | (b) | 10,512,505 | 26 | (10,512,505) | (26) |
| Increase of authorized ordinary shares | (c) | 224,591,557 | 561 | — | — |
| **As of December 31, 2018 and 2019** | | **270,000,000** | **674** | **—** | **—** |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 25 Share capital and treasury shares (continued)

### (a) Share capital (continued)

Issued:

| | Note | Number of ordinary shares '000 | Nominal value of ordinary shares US$'000 | Equivalent nominal value of ordinary shares RMB'000 | Share premium RMB'000 |
|---|---|---|---|---|---|
| **As of January 1, 2018** | | 978,217 | 24 | 150 | 742,760 |
| Acquisition of additional equity interests in non-wholly owned subsidiaries | (d) | 1,500 | — | — | 230,899 |
| Issuance of ordinary shares | (e) | 63,960 | 2 | 11 | 9,827,146 |
| Effect of Share Subdivision | (a) | 9,393,092 | — | — | — |
| Issuance of ordinary shares relating to initial public offering, net of underwriting commissions and other issuance costs | (f) | 1,635,926 | 4 | 27 | 23,248,593 |
| Conversion of Preferred Shares to ordinary shares | (b) | 10,504,922 | 26 | 174 | 151,100,334 |
| Release of ordinary shares from Share Scheme Trust | (g) | — | 2 | 15 | 933,592 |
| Issuance of ordinary shares to Share Scheme Trust | (g) | 1,048,806 | — | — | — |
| Share premium set off the accumulated losses and other reserves | (h) | — | — | — | (142,232,042) |
| **As of December 31, 2018** | | 23,626,423 | 58 | 377 | 43,851,282 |
| Exercise of share options and RSUs | | 690,361 | 1 | 9 | 1,442,634 |
| Shares repurchased and cancelled | | (227,956) | — | 1 | (1,882,527) |
| Issuance of ordinary shares to Share Scheme Trusts | (g) | 18,567 | — | — | — |
| Release of ordinary shares from Share Scheme Trusts | (g) | — | — | 1 | 167,447 |
| **As of December 31, 2019** | | 24,107,395 | 59 | 388 | 43,578,836 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 25 Share capital and treasury shares (continued)

### (a) Share capital (continued)

Notes:

(a) On June 17, 2018, pursuant to the shareholders' resolution, each existing issued and unissued share of US$0.000025 each in the share capital of the Company were subdivided into 10 shares of US$0.0000025 each.

(b) Upon completion of the initial public offering ("**IPO**"), each issued Preferred Share converted into one Class B ordinary share by re-designation and reclassification of every Preferred Share in issue as an Class B ordinary share on a one for one basis and all the unissued and authorized Preferred Shares were re-designated and reclassified as Class B ordinary shares. As a result, the financial liabilities for Preferred Shares were derecognized and recorded as share capital and share premium.

(c) Upon completion of the re-designation and reclassification noted in (b), the authorized share capital of the Company increased 63,116,143,000 Class A ordinary shares of nominal value of US$0.0000025 each and 161,475,414,000 Class B ordinary shares of nominal value of US$0.0000025 each.

(d) Pursuant to the shareholders' resolution passed on March 30, 2018, 1,500,000 Class B ordinary shares (or 15,000,000 Class B ordinary shares following the Share Subdivision) were issued as consideration shares in exchange for certain indirect equity interests in subsidiary Timi Personal Computing Co., Ltd..

(e) On April 2, 2018, the Company issued 63,959,619 Class B ordinary shares (or 639,596,190 Class B ordinary shares following the Share Subdivision) at par value to Smart Mobile Holdings Limited, an entity whose interest is held on trust for the benefit of Lei Jun and his family members, to reward Lei Jun for his contribution to the Company. Accordingly, RMB9,827,157,000 was recognized as share-based compensation expenses on April 2, 2018 by the Group.

(f) Upon completion of the IPO, the Company issued 1,635,926,000 new shares at par value of US$0.0000025 each for cash consideration of HK$17.00 each, and raised gross proceeds of approximately HK$27,810,742,000 (equivalent to RMB23,525,107,000). The respective share capital amount was approximately RMB27,000 and share premium arising from the issuance was approximately RMB23,248,593,000, net of the share issuance costs. The share issuance costs paid and payable mainly include share underwriting commissions, lawyers' fees, reporting accountant's fee and other related costs, which are incremental costs directly attributable to the issuance of the new shares. These costs amounting to RMB276,487,000 were treated as a deduction against the share premium arising from the issuance.

(g) The Company issued ordinary shares with respect to the share options and RSUs under the employees share-based compensation scheme to be exercised by certain grantees of the Company to trusts, which were established to hold the shares for and on behalf of the grantees (collectively, "**Share Scheme Trusts**").

(h) On December 27, 2018, the Board of Directors passed a resolution that the sum of approximately of RMB142,232,042,000 standing to the credit of the share premium account of the Company was applied to set off the accumulated losses and other reserves of the Company. The accumulated losses of RMB136,652,570,000 was set off and the related currency translation difference of RMB5,579,472,000 was released.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 25 Share capital and treasury shares (continued)

### (b) Treasury shares

| | Number of shares '000 | Amounts RMB'000 |
|---|---|---|
| **As of January 1, 2018 and 2019** | — | — |
| Shares repurchased | 358,196 | 2,932,111 |
| Shares cancelled | (227,956) | (1,879,289) |
| **As of December 31, 2019** | 130,240 | 1,052,822 |

During the year ended December 31, 2019, the Company repurchased its own ordinary shares on the Stock Exchange of Hong Kong Limited as follows:

| Month/Year | Number of shares '000 | Highest price paid per share HK$ | Lowest price paid per share HK$ | Aggregate price paid HK$ |
|---|---|---|---|---|
| January 2019 | 19,972 | 10.20 | 9.74 | 199,931,233 |
| June 2019 | 97,928 | 10.04 | 8.96 | 925,210,318 |
| July 2019 | 7,610 | 10.00 | 9.70 | 74,840,553 |
| September 2019 | 91,254 | 9.38 | 8.73 | 824,790,890 |
| October 2019 | 31,115 | 9.12 | 8.82 | 280,023,901 |
| November 2019 | 44,828 | 9.00 | 8.79 | 399,982,282 |
| December 2019 | 65,489 | 9.09 | 8.85 | 589,464,196 |
| Total | 358,196 | | | 3,294,243,373 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 26 Other reserves

| | Share-based compensation reserve RMB'000 | Currency translation differences RMB'000 | Statutory surplus reserve RMB'000 | General reserve RMB'000 | Capital reserve RMB'000 | Others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|---|
| At January 1, 2019 | 5,333,233 | 43,442 | 862,680 | — | (55,913) | 263,973 | 6,447,415 |
| Appropriation to statutory reserves (Note (a)) | — | — | 295,047 | — | — | — | 295,047 |
| Appropriation to general reserves | — | — | | 2 | — | — | 2 |
| Employees share-based compensation scheme: | | | | | | | |
| — value of employee services (Note (c) and Note 28) | 2,127,878 | — | — | — | — | — | 2,127,878 |
| — exercise of share options and restricted stock units | (1,184,767) | — | — | — | — | — | (1,184,767) |
| Share of other comprehensive income of investments accounted for using the equity method (Note 11(b)) | — | — | — | — | — | 9,279 | 9,279 |
| Share of other reserves of investments accounted for using the equity method (Note 11(b)) | — | — | — | — | 229,740 | — | 229,740 |
| Acquisition of additional equity interests in non-wholly owned subsidiaries | — | — | — | — | (173,904) | — | (173,904) |
| Currency translation differences (Note (b)) | — | 419,471 | — | — | — | — | 419,471 |
| Release of ordinary shares from Share Scheme Trust (Note 25(a)(g)) | (139,015) | — | — | — | — | — | (139,015) |
| At December 31, 2019 | 6,137,329 | 462,913 | 1,157,727 | 2 | (77) | 273,252 | 8,031,146 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 26 Other reserves (continued)

| | Share-based compensation reserve RMB'000 | Currency translation differences RMB'000 | Statutory surplus reserve RMB'000 | Capital reserve RMB'000 | Others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|
| **At January 1, 2018** | 3,816,153 | (3,779,938) | 805,180 | 33,501 | 72,524 | 947,420 |
| Appropriation to statutory reserves (Note (a)) | — | — | 57,808 | — | — | 57,808 |
| Employees share-based compensation scheme: | | | | | | |
| — value of employee services (Note (c) and Note 28) | 2,358,720 | — | — | — | — | 2,358,720 |
| Share of other comprehensive income of investments accounted for using the equity method (Note 11(b)) | — | — | — | — | 191,449 | 191,449 |
| Share of other reserves of investments accounted for using the equity method (Note 11(b)) | — | — | — | 62,657 | — | 62,657 |
| Acquisition of additional equity interests in non-wholly owned subsidiaries | — | — | — | (152,071) | — | (152,071) |
| Currency translation differences (Note (b)) | — | (1,756,092) | — | — | — | (1,756,092) |
| Share premium set off the accumulated losses and other reserves (Note 25(a)(h)) | — | 5,579,472 | — | — | — | 5,579,472 |
| Release of ordinary shares from Share Scheme Trust (Note 25(a)(g)) | (841,640) | — | — | — | — | (841,640) |
| Others | — | — | (308) | — | — | (308) |
| **At December 31, 2018** | 5,333,233 | 43,442 | 862,680 | (55,913) | 263,973 | 6,447,415 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 26 Other reserves (continued)

Notes:

(a) In accordance with the Company Law of the People's Republic of China and the stipulated provisions of the articles of association of subsidiaries with limited liabilities in mainland China, appropriation of net profits (after offsetting accumulated losses from prior years) should be made by these companies to their respective statutory surplus reserve funds and discretionary reserve funds before distributions are made to the owners. The percentage of appropriation to statutory surplus reserve fund is 10%. The amount to be transferred to discretionary reserve fund is determined by the equity owners of these companies. When the balance of the statutory surplus reserve fund reaches 50% of the registered capital, such transfer needs not to be made. Both statutory surplus reserve fund and discretionary reserves fund can be capitalized as capital of an enterprise, provided that the remaining statutory surplus reserve fund shall not be less than 25% of the registered capital.

In addition, in accordance with the Law of the People's Republic of China on Enterprises with Foreign Investments and the stipulated provisions of the articles of association of wholly owned foreign subsidiaries in mainland China, appropriation from net profits (after offsetting accumulated losses brought forward from prior years) should be made by these companies to their respective reserve fund. The percentage of net profit to be appropriated to the reserve fund is not less than 10% of the net profit. When the balance of the reserve fund reaches 50% of the registered capital, such transfer needs not to be made. With approvals obtained from respective boards of directors of these companies, the Reserve Fund can be used to offset accumulated deficit or to increase capital.

(b) Foreign currency translation reserve represents the difference arising from the translation of the financial statements of companies within the Group that have a functional currency different from the presentation currency of RMB for the financial statements of the Company and the Group.

A majority of the currency translation differences are arising from the Company when it translates the financial statements from the functional currency of US$ to presentation currency of RMB.

(c) Share-based compensation reserve arises from share-based payments granted to employees of the Group, see Note 28 for detail.

## 27 Dividends

No dividends have been paid or declared by the Company during the years ended December 31, 2019 and 2018.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 28 Share-Based Payments

On May 5, 2011, the Board of Directors of the Company approved the establishment of the "Xiaomi Corporation 2011 Employee Stock Option Plan" ("**2011 Plan**") with the purpose of attracting, motivating, retaining and rewarding certain employees and directors. The 2011 Plan is valid and effective for 10 years from the approval of the Board of Directors. The maximum number of shares that may be issued under 2011 Plan shall be 35,905,172 Class B ordinary shares (which were adjusted to 1,436,206,880 shares after the 1 to 4 share split on March 14, 2014 and further 1 to 10 Share Subdivision on June 17, 2018). The 2011 Plan permits the awards of options and RSUs.

Subsequently in August 2012, the 2011 Plan was superseded in its entirety as the "2012 Employee Stock Incentive Plan" ("**Pre-IPO ESOP**"). The purpose of Pre-IPO ESOP is same as the 2011 Plan. The Pre-IPO ESOP is valid and effective for 10 years from the approval of the Board of Directors. Through Pre-IPO ESOP, the Company may grant equity-based incentive up to 45,905,172 Class B ordinary shares initially (which were adjusted to 1,836,206,880 shares after the 1 to 4 share split on March 14, 2014 and further 1 to 10 Share Subdivision on June 17, 2018). The aggregate number of reserved Class B ordinary shares approved was 2,512,694,900 as of December 31, 2019 and 2018. The Pre-IPO ESOP permits the awards of options and RSUs.

On June 17, 2018, the Board of Directors of the Company adopted the principal terms of the Post-IPO Share Option Scheme. The purpose of Post-IPO Share Option Scheme is to provide selected participants with the opportunity to acquire proprietary interests in the Company and to encourage selected participants to work towards enhancing the value of the Company and its shares for the benefit of the Company and its shareholders as a whole. The total number of Class B ordinary shares available for grant under Post-IPO Share Option Scheme was 2,237,613,083 Class B ordinary shares. As of December 31, 2019, no option has been granted or agreed to be granted pursuant to Post-IPO Share Option Scheme.

On June 17, 2018, the Board of Directors of the Company adopted the principal terms of the Share Award Scheme. The purpose of the Share Award Scheme are (1) to align the interests of eligible persons with those of the Group through ownership of Class B ordinary shares, dividends and other distributions paid on Shares and/or the increase in value of the Class B ordinary shares, and (2) to encourage and retain eligible persons to make contributions to the long-term growth and profits of the Group. The aggregate number of Class B ordinary shares underlying all grants made pursuant to the Share Award Scheme will not exceed 1,118,806,541 shares without shareholders' approval.

Upon the Share Subdivision became effective, pro-rata adjustments have been made to the number of outstanding awarded shares, so as to give the participants the same proportion of the equity capital as that they were entitled to before the effect of the Share Subdivision. However, the number of share options, average exercise price per share option, fair value of share options, key assumptions of fair value of share options, number of RSUs and weighted average grant date fair value per RSU for the year ended December 31, 2018 stated below were before the adjustment for the Share Subdivision.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 28 Share-based payments (continued)

### Pre-IPO ESOP

**Share options granted to employees**

The share options have graded vesting terms, and vest in different schedules from the grant date over one year, 2 years, 4 years, 5 years and 10 years, on condition that employees remain in service without any performance requirements. For vesting schedule as one year, all granted share options are vested on the first anniversary of the grant date. For vesting schedule as 2 years, 50% of the aggregate number of granted share options are vested on the first anniversary of the grant date, and remaining granted share options are vested in equal tranches every month over the next twelve months. For vesting schedule as 4 years, 50% of granted share options are vested on the second anniversary of the grant date, 25% of granted share options are vested on the third anniversary of the grant date, the remaining granted share options are vested on the fourth anniversary of the grant date. For vesting schedule as 5 years, 40% of granted share options are vested on the second anniversary of the grant date, and every 20% of granted share options are vested on the third, fourth and fifth anniversary of the grant date respectively. For vesting schedule as 10 years, the granted share options are vested through 10 years with 6% to 15% shares vested each year unequally.

Under Pre-IPO ESOP, the Company also granted performance-based share options to certain employees, which are generally vested over a 10-year term. The performance goals are determined by the Board of Directors. For those awards, evaluations are made as of each reporting period to assess the likelihood of performance criteria being met. Share-based compensation expenses are then adjusted to reflect the revision of original estimates.

The options may be exercised at any time and from time to time only after the closing of the QPO or upon the approval of Board of Directors for all or any portion of the share options that have become vested.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 28 Share-based payments (continued)

### Pre-IPO ESOP (continued)

**Share options granted to employees (continued)**

Movements in the number of share options granted to employees and their related weighted average exercise prices are as below:

| | Number of share options | Average exercise price per share option (US$) |
|---|---|---|
| Outstanding as of January 1, 2019 | **1,433,597,913** | **0.10** |
| Forfeited during the year | **(54,982,220)** | **0.31** |
| Transferred to Share Scheme Trust (Note 25(a)(g)) | **(42,306,480)** | **0.10** |
| Exercised during the year | **(480,507,306)** | **0.04** |
| Outstanding as of December 31, 2019 | **855,801,907** | **0.12** |
| Exercisable as of December 31, 2019 | **340,290,647** | **0.20** |
| Outstanding as of January 1, 2018 (Note (a)) | 189,755,311 | 1.05 |
| Granted during the year (Note (a)) | 42,500,561 | 1.98 |
| Forfeited during the year (Note (a)) | (3,857,990) | 3.26 |
| Transferred to Share Scheme Trust (Note (a), Note 25(a)(g)) | (85,038,091) | 1.58 |
| Effect of Share Subdivision (Note (b)) | 1,290,238,122 | |
| Outstanding as of December 31, 2018 | 1,433,597,913 | 0.10 |
| Exercisable as of December 31, 2018 | 703,071,315 | 0.09 |

Notes:

(a) The numbers of shares were presented as before the effect of the Share Subdivision.

(b) It represented the effects of adjustments made to the numbers of shares as a result of the Share Subdivision.

The weighted-average remaining contract life for outstanding share options was 6.22 years as of December 31, 2019 (2018: 6.60 years).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 28 Share-based payments (continued)

### Pre-IPO ESOP (continued)

**Share options granted to employees (continued)**

***Fair value of share options***

Prior to the completion of IPO on July 9, 2018, the Group has used the discounted cash flow method to determine the underlying equity fair value of the Company and adopted equity allocation model to determine the fair value of the underlying ordinary shares. Key assumptions, such as discount rate and projections of future performance, are determined by the Group with best estimate.

Based on fair value of the underlying ordinary shares, the Group has used Binomial option-pricing model to determine the fair value of the share option as of the grant date. Key assumptions are set as below:

| | Year ended December 31, 2018 |
|---|---|
| Fair value per share (Note (a)) | US$22.99–24.48 |
| Exercise price (Note (a)) | US$1.02–3.44 |
| Risk-free interest rate | 3.12%–3.68% |
| Dividend yield | — |
| Expected volatility | 41.57%–43.21% |
| Expected terms | 10 years |

Note:

(a) The fair value per share and the exercise price presented was before the effect of the Share Subdivision.

The weighted-average fair value of granted shares was US$21.80 (which was adjusted to US$2.18 after the Share Subdivision on June 17, 2018) per share for the year ended December 31, 2018.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 28 Share-based payments (continued)

### Pre-IPO ESOP (continued)

**RSUs granted to employees**

The Company also granted RSUs to the Company's employees under Pre-IPO ESOP. The RSUs granted would vest on the second anniversary from the grant date, and in equal tranches over the remaining years of total vesting period as four or five years, on condition that employees remain in service without any performance requirements.

The RSUs may be settled at any time and from time to time only after the closing of the QPO or upon the approval of Board of Directors for all or any portion of the RSUs that have become vested.

Movements in the number of RSUs granted to the Company's employees under Pre-IPO ESOP and the respective weighted-average grant date fair value are as follows:

| | Number of RSUs | Weighted average grant date fair value per RSU (US$) |
|---|---|---|
| Outstanding as of January 1, 2019 | **207,161,980** | **0.23** |
| Exercised during the year | **(207,161,980)** | **0.23** |
| Outstanding as of December 31, 2019 | **—** | **—** |
| Vested as of December 31, 2019 | **—** | **—** |
| Outstanding as of January 1, 2018 (Note (a)) | 24,492,747 | 2.94 |
| Forfeited during the year (Note (a)) | (3,776,549) | 6.36 |
| Effect of Share Subdivision (Note (b)) | 186,445,782 | |
| Outstanding as of December 31, 2018 | 207,161,980 | 0.23 |
| Vested as of December 31, 2018 | 206,921,978 | 0.23 |

Notes:

(a) The numbers of shares were presented as before the effect of the Share Subdivision.

(b) It represented the effects of adjustments made to the numbers of shares as a result of the Share Subdivision.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 28 Share-based payments (continued)

### Pre-IPO ESOP (continued)

**RSUs granted to employees (continued)**

Prior to the completion of IPO on July 9, 2018, the Group has used the discounted cash flow method to determine the underlying equity fair value of the Company and adopted equity allocation model to determine the fair value of the underlying ordinary share. Key assumptions, such as discount rate and projections of future performance, are required to be determined by the Group with best estimate.

The fair value of each RSU at the grant dates were determined by reference to the fair value of the ordinary shares of the Company that issued to its shareholders.

The total expenses recognized in the consolidated income statement for aforementioned share-based awards granted to the Group's employees are RMB1,898,081,000 for the year ended December 31, 2019 (2018: RMB2,358,917,000).

**Share based awards granted to Lei Jun**

On April 2, 2018, the Company issued 63,959,619 Class B ordinary shares (or 639,596,190 Class B ordinary shares following the Share Subdivision) at par value to Smart Mobile Holdings Limited, an entity whose interest is held on trust for the benefit of Lei Jun and his family members, to reward Lei Jun for his contribution to the Company. Accordingly, RMB9,827,157,000 was recognized as share-based compensation expenses on April 2, 2018 by the Group.

On June 17, 2018, Lei Jun was granted 42,070,000 share options in Xiaomi Finance Inc. ("**Xiaomi Finance**") pursuant to the first share option scheme adopted by Xiaomi Finance. Such share options were vested immediately and Lei Jun can exercise these share options with exercise price of RMB3.8325 for each share option for the following 20 years commencing on June 17, 2018. Based on fair value of the underlying ordinary shares, the Group has used Binomial option-pricing model to determine the fair value of the share option as the grant date. Key valuation assumptions include discount rate (post-tax) of 18.5%, risk-free interest rate of 3.99%, volatility of 46%. Accordingly, RMB102,608,000 was recognized as share-based compensation expenses on June 17, 2018 by the Group.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 28 Share-based payments (continued)

### Share Award Scheme

**RSUs granted to employees**

The Company granted performance-based RSUs to the Company's employees under Share Award Scheme. The RSUs granted would vest in different schedules from the service commencement date over one year, 4 years, 5 years and 10 years, on condition that employees remain in service and certain performance criteria is met. For vesting schedule as one year, all granted RSUs are vested on the first anniversary of the service commencement date. For vesting schedule as 4 years, 25% of granted RSUs are vested on every anniversary of the service commencement date over the vesting period. For vesting schedule as 5 years, 40% of granted RSUs are vested on the second anniversary of the service commencement date, and every 20% of granted RSUs are vested on the third, fourth and fifth anniversary of the service commencement date respectively. For vesting schedule as 10 years, 20% of granted RSUs are vested on the second anniversary of the service commencement date, and every 10% of granted RSUs are vested on anniversaries of the service commencement date over the rest of the vesting period. The performance goals are determined by the Board of Directors. Evaluations are made as of each reporting period to assess the likelihood of performance criteria being met. Share-based compensation expenses are then adjusted to reflect the revision of original estimates.

Movements in the number of RSUs granted to the Company's employees granted under Share Award Scheme and the respective weighted average grant date fair value are as below:

| | Number of RSUs | Weighted average grant date fair value per RSU (US$) |
|---|---|---|
| Outstanding as of January 1, 2019 | — | — |
| Granted during the year | 98,449,031 | 1.20 |
| Forfeited during the year | (5,415,702) | 1.22 |
| Transferred to Share Scheme Trust (Note 25(a)(g)) | (234,396) | 1.45 |
| Exercised during the year | (2,692,000) | 1.39 |
| Outstanding as of December 31, 2019 | 90,106,933 | 1.20 |
| Exercisable as of December 31, 2019 | 40,000 | 1.45 |

The weighted-average remaining contract life for outstanding RSUs granted under Share Award Scheme was 9.45 years as of December 31, 2019.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 28 Share-based payments (continued)

### Share Award Scheme (continued)

**RSUs granted to employees (continued)**

The fair value of the awarded shares was calculated based on the market price of the Company's shares at the respective grant date.

The total expenses recognized in the consolidated income statement for RSUs granted to the Group's employees under Share Award Scheme are RMB229,886,000 for the year ended December 31, 2019.

### Employee fund

On August 31, 2014, the Board of Directors of the Company approved the establishment of the Employee Fund with the purpose of which is to invest in companies within the business ecosystem of the Group. The Company invited certain employees to participate, with the condition that they would only receive the original investment sum with interest should they decide to resign from the Group within 5 years from the establishment date (the "**Lockup Period**"). Upon the end of the Lockup Period, the holders would become the equity holders of the Employee Fund. According to the arrangement of Employee Fund, the equity holders of the Employee Fund can demand the Company to buy back the shares at fair value or continue to hold the shares when they resign after the Lockup Period. The Group measures the liability related to cash-settled share-based payments at fair value as of December 31, 2019.

The total expenses recognized in the consolidated income statement for the Employee Fund granted to the Group's employees are RMB73,755,000 for the year ended December 31, 2019 (2018: RMB91,986,000).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 29 Other non-current liabilities

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Liabilities to fund investors (Note (a)) | 3,074,210 | 2,823,504 |
| Lease liability (Note 16) | 560,804 | — |
| Others | 121,197 | 21,355 |
| | 3,756,211 | 2,844,859 |

Note:

(a) It represents the funds raised by the third party investors under Hubei Xiaomi Yangtze River Industry Investment Fund Partners (Limited Partnership) (湖北小米長江產業基金合夥企業(有限合夥)) (the "**Hubei Fund**"). The Group controls the Hubei Fund as the Group is exposed to and has rights to variable returns from its involvement with the Hubei Fund and has the ability to affect those returns through its power over the Hubei Fund. For the amount raised from limited partners, the Group has contractual obligation to settle the liability with the limited partners and therefore is classified as a financial liability measured at amortized cost in the consolidated financial statements. The carrying amount of this financial liability approximates to its fair value.

## 30 Trade payables

Trade payables primarily include payables for inventories and royalty fees. As of December 31, 2019 and 2018, the carrying amounts of trade payables were primarily denominated in RMB, US$ and INR.

Trade payables and their aging analysis based on invoice date are as follows:

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Up to 3 months | 57,942,872 | 44,312,748 |
| 3 to 6 months | 1,136,595 | 1,656,699 |
| 6 months to 1 year | 342,864 | 266,623 |
| 1 to 2 years | 55,709 | 50,350 |
| Over 2 years | 49,900 | 851 |
| | 59,527,940 | 46,287,271 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 31 Other payables and accruals

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Amounts collected for third parties | 1,428,500 | 1,628,230 |
| Payroll and welfare payables | 1,165,183 | 795,593 |
| Deposits payable | 1,114,853 | 953,132 |
| Employee Fund (Note 28) | 604,187 | 553,108 |
| Accrual expenses | 1,202,807 | 499,295 |
| Payables for construction cost | 1,275,467 | 619,935 |
| Payables for investments | 2,500 | 222,382 |
| Other taxes payables | 624,350 | 192,182 |
| Lease liabilities (Note 16) | 399,444 | — |
| Payables related to share options and RSUs granted to employees | 484,896 | — |
| Others | 799,156 | 848,913 |
| | 9,101,343 | 6,312,770 |

The carrying amounts of other payables were primarily denominated in RMB and approximate their fair values as of December 31, 2019 and 2018.

## 32 Advance from customers

Advance from customers primarily includes advance from customers when the Group receives payments in advance of the delivery of products or performance of services.

Contract liabilities are presented in advance from customers, which are the Group's obligations to transfer goods or services to a customer for which the Group has received consideration (or an amount of consideration is due) from the customer. As of December 31, 2019, the total contract liabilities amounted to RMB7,248,982,000 (2018: RMB4,054,595,000), which will be recognized as revenue within one year.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 33 Borrowings

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| **Included in non-current liabilities** | | |
| Asset-backed securities (Note (a)) | 2,305,000 | 2,752,815 |
| Fund raised through trusts (Note (b)) | 450,000 | — |
| Secured borrowings (Note (c)) | 1,825,856 | 1,260,941 |
| Unsecured borrowings (Note (d)) | 206,000 | 3,842,387 |
| | 4,786,856 | 7,856,143 |
| **Included in current liabilities** | | |
| Asset-backed securities (Note (a)) | 2,647,641 | 586,282 |
| Fund raised through trusts (Note (b)) | 420,000 | 648,390 |
| Secured borrowings (Note (c)) | 1,796,701 | — |
| Unsecured borrowings (Note (d)) | 7,972,213 | 1,840,522 |
| | 12,836,555 | 3,075,194 |

Notes:

(a) The Group has securitized certain loan receivables and completed several rounds of issuance of its asset-backed securities ("**ABS**"). As of December 31, 2019, the total ABS amounting to RMB4,952,641,000 (2018: RMB3,339,097,000) bore interest at 4.15%-7.74% per annum.

(b) The Group has securitized certain loan receivables and raised several rounds of funds through third party trusts. As of December 31, 2019, the fund raised through trust amounting to RMB870,000,000 (2018: RMB648,390,000) bore interest at 7.29%-8.00% per annum in 2019. The Group is committed to unconditionally repurchase the aforementioned securitized loan receivables. The balance will mature in 2020 and 2021.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 33 Borrowings (continued)

Notes (continued):

(c) As of December 31, 2019, RMB2,225,856,000 (2018: RMB1,260,941,000) of borrowings were secured by construction in progress and land use rights amounting to approximately RMB4,082,853,000 (2018: RMB4,082,853,000). The interest rate of these borrowings was 4.66%-4.90% per annum. RMB400,000,000 of these borrowings should be repaid in 2020, the remaining amounts with RMB1,443,920,000 should be repaid by the end of March 23, 2027, RMB63,387,000 should be repaid by the end of December 12,2027 and RMB318,549,000 should be repaid by the end of September 27, 2032.

As of December 31, 2019, RMB808,886,000 (2018: nil) of short term borrowings were secured by commercial paper, RMB587,815,000 (2018: nil) of short term borrowings were secured by restricted deposits.

(d) As of December 31, 2019, the Group had US$500,000,000 (equivalent to approximately RMB3,488,100,000) unsecured borrowings relating to a three-year bank loan facility agreement entered into on July 26, 2017 with the available commitment US$1,000,000,000 (equivalent to approximately RMB6,976,200,000) including US$500,000,000 (equivalent to approximately RMB3,488,100,000) term loan and US$500,000,000 (equivalent to approximately RMB3,488,100,000) revolving loan, which should be repaid by the Group on July 25, 2020.

The Group had RMB1,411,718,000 (2018: nil) unsecured borrowings with interest rate 4.20% per annum, RMB77,923,000 (2018: nil) unsecured borrowings with interest rate 2.82% per annum, RMB249,216,000 (2018: nil) unsecured borrowings with interest rate 4.13% per annum, RMB190,000,000 (2018: nil) unsecured borrowings with interest rate 6.43% per annum, RMB1,500,000,000 (2018: nil) unsecured borrowings with interest rate 2.92% per annum, RMB667,763,000 (2018: nil) unsecured borrowings with interest rate 6-month London Inter Bank Offered Rate ("**LIBOR**") + 1% per annum. All of these borrowings should be repaid by the Group in 2020.

The Group had RMB400,000,000 (2018: nil) of borrowings with interest rate 6.00% per annum secured by intra-group companies, which should be repaid by the Group in 2020.

The Group had RMB206,000,000 (2018: nil) unsecured borrowings with interest rate 4.66% per annum which should be repaid by the end of November 26, 2029.

For the year ended December 31, 2019, the interest rate of the interest-bearing liabilities ranges from 2.82% to 8.00% per annum (2018: from 2.22% to 9.00%).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 34 Deferred income taxes

Deferred income taxes are calculated in full on temporary differences under the liability method using the tax rates at which are expected to be applied at the time of reversal of the temporary differences.

The amount of offsetting deferred income tax assets and liabilities is RMB122,961,000 as of December 31, 2019 (2018: RMB93,750,000). The analysis of deferred income tax assets and liabilities before offsetting is as follows:

| | As of December 31, | |
|---|---|---|
| | **2019** | 2018 |
| | **RMB'000** | RMB'000 |
| **Deferred income tax assets:** | | |
| — to be recovered after 12 months | **560,577** | 625,671 |
| — to be recovered within 12 months | **845,799** | 780,324 |
| | **1,406,376** | 1,405,995 |
| **Deferred income tax liabilities:** | | |
| — to be settled after 12 months | **(700,275)** | (870,082) |
| — to be settled within 12 months | **(2,588)** | (1,313) |
| | **(702,863)** | (871,395) |

The gross movement on the deferred income tax assets is as follows:

| | Year ended December 31, | |
|---|---|---|
| | **2019** | 2018 |
| | **RMB'000** | RMB'000 |
| **At the beginning of the year** | **1,405,995** | 721,389 |
| Credited to the consolidated income statement | **381** | 684,606 |
| **At the end of the year** | **1,406,376** | 1,405,995 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 34 Deferred income taxes (continued)

The gross movement on the deferred income tax liabilities is as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| **At the beginning of the year** | **(871,395)** | (1,148,464) |
| Credited to the consolidated income statement | **168,532** | 280,619 |
| Acquisition of a subsidiary | **—** | (3,550) |
| **At the end of the year** | **(702,863)** | (871,395) |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 34 Deferred income taxes (continued)

The movement in deferred income tax assets and liabilities during the years without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

Deferred income tax assets:

| | Accrued liabilities and provisions RMB'000 | Provision for impairment of inventories RMB'000 | Depreciation of property and amortization of intangible assets RMB'000 | Tax losses RMB'000 | Fair value changes of financial assets RMB'000 | Credit loss allowance RMB'000 | Unrealized gain on intra-group transactions RMB'000 | Others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|---|---|---|
| At January 1, 2019 | 231,460 | 385,369 | 93,677 | 359,199 | 80,341 | 92,961 | 156,440 | 6,548 | 1,405,995 |
| Credited/(debited) to consolidated income statement | 100,898 | (265,570) | (4,192) | 13,707 | 274 | 49,892 | 94,350 | 11,022 | 381 |
| At December 31, 2019 | 332,358 | 119,799 | 89,485 | 372,906 | 80,615 | 142,853 | 250,790 | 17,570 | 1,406,376 |
| At January 1, 2018 | 267,649 | 148,193 | 93,119 | 62,019 | 55,991 | 41,186 | 44,696 | 8,536 | 721,389 |
| (Debited)/credited to consolidated income statement | (36,189) | 237,176 | 558 | 297,180 | 24,350 | 51,775 | 111,744 | (1,988) | 684,606 |
| At December 31, 2018 | 231,460 | 385,369 | 93,677 | 359,199 | 80,341 | 92,961 | 156,440 | 6,548 | 1,405,995 |

Deferred income tax assets are recognized for deductible temporary differences to the extent that the realization of the related tax benefits through future taxable profits is probable.

As of December 31, 2019, the Group did not recognize deferred income tax assets of RMB966,068,000 (2018: RMB520,995,000), in respect of deductible temporary differences and cumulative tax losses amounting RMB3,479,308,000 (2018: RMB2,293,425,000), that can be carried forward against future taxable income. The tax losses as of December 31, 2019 amounting to RMB27,395,000 (2018: RMB11,237,000) can be carried forward indefinitely, and the remaining amount of RMB3,377,006,000 (2018: RMB2,025,938,000) will expire within 9 years (2018: 10 years).

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 34 Deferred income taxes (continued)

The movement in deferred income tax assets and liabilities during the years without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows (continued):

Deferred income tax liabilities:

| | Changes in fair value of financial assets RMB'000 | Business combination RMB'000 | Total RMB'000 |
|---|---|---|---|
| **At January 1, 2019** | (868,381) | (3,014) | (871,395) |
| Credited to consolidated income statement | 168,106 | 426 | 168,532 |
| **At December 31, 2019** | (700,275) | (2,588) | (702,863) |
| **At January 1, 2018** | (1,147,419) | (1,045) | (1,148,464) |
| Credited to consolidated income statement | 279,038 | 1,581 | 280,619 |
| Acquisition of a subsidiary | — | (3,550) | (3,550) |
| **At December 31, 2018** | (868,381) | (3,014) | (871,395) |

## 35 Convertible redeemable preferred shares

Since the date of incorporation, the Company has completed several rounds of financing by issuing Preferred Shares. On July 9, 2018, the Company was listed on the Main Board of The Stock Exchange of Hong Kong Limited and made an offering of 2,179,585,000 Class B ordinary shares (excluding any Class B ordinary shares issued pursuant to the exercise of the over-allotment option) at a price at HK$17.00 per share. All Preferred Shares were converted into Class B ordinary shares upon completion of the IPO on July 9, 2018. The fair value of each of Preferred Share on the conversion date is the Offer Price in the Global Offering. The movement of the Preferred Shares for the year ended December 31, 2018 is set out as below:

| | RMB'000 |
|---|---|
| **At January 1, 2018** | 161,451,203 |
| Changes in fair value | (12,514,279) |
| Currency translation differences | 2,163,584 |
| Conversion to ordinary shares | (151,100,508) |
| **At December 31, 2018** | — |

Changes in fair value of Preferred Shares were recorded in "fair value changes of convertible redeemable preferred shares" in the consolidated income statement. Management considered that fair value changes in the Preferred Shares that are attributable to changes of credit risk of this liability are not significant.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 36 Cash flow information

### (a) Cash generated from operations

| | Year Ended December 31, 2019 RMB'000 | Year Ended December 31, 2018 RMB'000 |
|---|---|---|
| **Profit before income tax** | **12,162,646** | 13,927,124 |
| Adjustments for: | | |
| — Depreciation of property and equipment, right-of-use assets and investment properties | **895,273** | 219,523 |
| — Amortization of intangible assets | **485,786** | 528,693 |
| — Gain on disposal of property and equipment | **(5,909)** | (10,295) |
| — Credit loss allowance for trade and other receivables | **83,357** | 33,211 |
| — Credit loss allowance for loan receivables | **1,015,619** | 607,180 |
| — Impairment provision for inventories | **3,859,675** | 3,006,525 |
| — Interest income | **(930,889)** | (601,065) |
| — Interest expense | **528,460** | 384,692 |
| — Dividend income | **(347,205)** | (131,804) |
| — Share of losses of investments accounted for using the equity method | **671,822** | 614,920 |
| — Remeasurement of investments transferring from financial assets measured at fair value through profit or loss to investments accounted for using the equity method | **—** | (126,614) |
| — Net gains on disposals of long-term investments measured at fair value through profit or loss | **—** | (28,176) |
| — Losses on disposal of an investment accounted for using the equity method | **13,376** | — |
| — Fair value changes of convertible redeemable preferred shares | **—** | (12,514,279) |
| — Fair value gains on long-term investments measured at fair value through profit or loss | **(3,813,012)** | (4,430,359) |
| — Share-based compensation | **2,201,722** | 12,380,668 |
| — Foreign exchanges (gains)/losses, net | **(34,632)** | 14,550 |
| — Investment income from short-term investments measured at fair value through profit or loss | **(386,461)** | (335,695) |
| — Investment income from short-term investments measured at amortized cost | **—** | (20,199) |
| Operating cash flows before changes in working capital | | |
| — Increase in inventories | **(6,964,428)** | (16,114,975) |
| — Increase in trade receivables | **(1,276,714)** | (91,003) |
| — Increase in loan receivables | **(3,448,312)** | (2,752,183) |
| — Decrease/(increase) in prepayments and other receivables | **1,956,740** | (9,463,591) |
| — (Increase)/decrease in restricted cash | **(136,394)** | 294,753 |
| — Increase in trade payables | **13,534,575** | 12,627,385 |
| — Increase in advance from customers | **3,758,590** | 1,050,583 |
| — Increase/(decrease) in warranty provision | **983,654** | (51,600) |
| — Increase in other payables and accruals | **1,045,058** | 1,118,058 |
| — Increase/(decrease) in other non-current liabilities | **99,842** | (13,856) |
| **Cash generated from operations** | **25,952,239** | 122,171 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 36 Cash flow information (continued)

### (b) Proceeds from disposal of property and equipment

In the consolidated statement of cash flows, proceeds from sale of property and equipment comprise:

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Net book amount (Note 14) | 61,826 | 17,072 |
| Gain on disposal of property and equipment | 5,909 | 10,295 |
| **Proceeds from disposal of property and equipment** | 67,735 | 27,367 |

### (c) Non-cash transactions

Other than the addition of right-of-use assets and lease liabilities described in Note 16, and the reclassification of the investment in associates measured at fair value through profit or loss to investment accounted for using the equity method as described in Note 11(b), there were no material non-cash transactions for the year ended December 31, 2019.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 36 Cash flow information (continued)

### (d) Reconciliation of liabilities generated from financing activities

| | Liabilities from financing activities | | | | | |
|---|---|---|---|---|---|---|
| | Borrowing due within 1 year RMB'000 | Borrowing due after 1 year RMB'000 | Convertible redeemable preferred shares RMB'000 | Interest payable RMB'000 | Lease liabilities RMB'000 | Total RMB'000 |
| **Liabilities from financing activities as of January 1, 2019** | 3,075,194 | 7,856,143 | — | 96,192 | 858,833 | 11,886,362 |
| Cash flows | 1,790,061 | 4,829,238 | — | (218,994) | (578,063) | 5,822,242 |
| Accrued interest expenses | — | — | — | 201,761 | — | 201,761 |
| Foreign exchange adjustments | (52,214) | 108,711 | — | — | — | 56,497 |
| Reclassification from non-current to current | 8,024,034 | (8,024,034) | — | — | — | — |
| Leases | — | — | — | — | 679,478 | 679,478 |
| Others | (520) | 16,798 | — | — | — | 16,278 |
| **Liabilities from financing activities as of December 31, 2019** | 12,836,555 | 4,786,856 | — | 78,959 | 960,248 | 18,662,618 |
| **Liabilities from financing activities as of January 1, 2018** | 3,550,801 | 7,251,312 | 161,451,203 | 5,742 | — | 172,259,058 |
| Cash flows | (5,928,062) | 5,691,840 | — | (243,966) | — | (480,188) |
| Accrued interest expenses | — | — | — | 334,416 | — | 334,416 |
| Fair value changes of convertible redeemable preferred shares | — | — | (12,514,279) | — | — | (12,514,279) |
| Foreign exchange adjustments | (14,290) | 418,950 | 2,163,584 | — | — | 2,568,244 |
| Conversion of Preferred Shares to ordinary shares | — | — | (151,100,508) | — | — | (151,100,508) |
| Reclassification from non-current to current | 5,466,745 | (5,466,745) | — | — | — | — |
| Others | — | (39,214) | — | — | — | (39,214) |
| **Liabilities from financing activities as of December 31, 2018** | 3,075,194 | 7,856,143 | — | 96,192 | — | 11,027,529 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 37 Contingencies

The Group did not have any material contingent liabilities as of December 31, 2019 and 2018.

## 38 Commitments

### (a) Capital commitments

Capital expenditure contracted for at the end of the years but not yet incurred is as follows:

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Property and equipment | **1,747,044** | 1,825,343 |
| Intangible assets | **28,810** | 57,778 |
| Investments | **217,506** | 137,176 |
| | **1,993,360** | 2,020,297 |

### (b) Operating lease commitments

The Group leases offices, warehouses, retail stores and servers under non-cancellable operating lease agreements. The Group's future aggregate minimum lease payments under non-cancellable operating leases are as follows:

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Not later than 1 year | **305,186** | 560,926 |
| Later than 1 year and not later than 5 years | **—** | 385,038 |
| Later than 5 years | **—** | 83,276 |
| | **305,186** | 1,029,240 |

From January 1, 2019, in accordance with IFRS 16, the Group has recognized right-of-use assets for these leases, except for certain short-term leases, see Note 16 for further information.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operational decisions. Parties are also considered to be related if they are subject to common control. Members of key management and their close family members of the Group are also considered as related parties.

The following significant transactions were carried out between the Group and its related parties during the periods presented. In the opinion of the directors of the Company, the related party transactions were carried out in the normal course of business and at terms negotiated between the Group and the respective related parties.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions (continued)

### (a) Names and relationships with related parties

The following companies are related parties of the Group that had significant transactions and/or balances with the Group during the year.

| Company | Relationship |
|---|---|
| Nanchang Blackshark Technology Co.,Ltd. (Note 11(b)) | Associate of the Group |
| Beijing iQIYI Science & Technology Co., Ltd. (Note 11(b)) | Associate of the Group |
| Shanghai iQIYI Culture Media Co., Ltd. (Note 11(b)) | Associate of the Group |
| Beijing Particle Information Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Foshan Yunmi Electric Appliances Technology Co., Ltd. (Note 11(b)) | Associate of the Group |
| Zhuhai Kingsoft Online Game Technology Co., Ltd. | Associate of the Group |
| Beijing Kingsoft Cloud Technology Co., Ltd. | Associate of the Group |
| Chengdu Qushui Science and Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Anhui Huami Information Technology Co., Ltd. (Note 11(b)) | Associate of the Group |
| Beijing SmartMi Electronic Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Jiangsu Zimi Electronic Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Shenzhen Rock Times Technology Co., Ltd. (Note 11(b)) | Associate of the Group |
| Tiinlab Acoustic Technology Ltd. (Note (a)) | Associate of the Group |
| Dongguan Yingsheng Electronic Technology Co., Ltd. | Associate of the Group |
| Shanghai Chuangmi Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Shanghai Runmi Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Soocare (Shenzhen) Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Ningbo Minij Trading Co., Ltd. | Associate of the Group |
| Shenzhen Lumi Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Zimi Communication Technology (Jiangsu) Co., Ltd. | Associate of the Group |
| Longcheer Technology (Huizhou) Co., Ltd. (Note 11(b)) | Associate of the Group |
| Shanghai Chunmi Electronic Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Qingdao Yeelink Information Technology Co., Ltd. (Note (a)) | Associate of the Group |
| 21 Vianet Group Inc. | Associate of the Group |
| Beijing Fengmi Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Liesheng Technology (Dongguan) Co.,Ltd. | Associate of the Group |
| Chunmi Technology (Wuhu) Co., Ltd. (Note (a)) | Associate of the Group |
| Nanchang Longcheer Technology Co., Ltd. (Note 11(b)) | Associate of the Group |
| Forewin FPC (Suzhou) Co., Ltd. (Note (a)) | Associate of the Group |
| ChingMi (Beijing) Technology Co., Ltd. (Note 11(b)) | Associate of the Group |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions (continued)

### (a) Names and relationships with related parties (continued)

| Company | Relationship |
|---|---|
| Shanghai Minij Internet Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Guolong Information Technology (Shanghai) Co., Ltd. | Associate of the Group |
| Dreame Technology (Tianjin) Ltd. (Note (a)) | Associate of the Group |
| Hannto Technology Co., Ltd. (Note (a)) | Associate of the Group |
| LeXiu Technology (Hangzhou) Co., Ltd. (Note (a)) | Associate of the Group |
| Zhejiang Xingyue Electric Equipment Co., Ltd. (Note (a)) | Associate of the Group |
| PL-Mi (Shanghai) Co., Ltd. (Note 11(b)) | Associate of the Group |
| Beijing Yuemi Technology Co., Ltd. (Note 11(b)) | Associate of the Group |
| QingHeXiaoBei (Wuxi) Inc. | Associate of the Group |
| Nanjing Jiqidao Smart Technology Co., Ltd. | Associate of the Group |
| Miaobo Software Technology (Shanghai) Co., Ltd. (Note 11(b)) | Associate of the Group |
| Beijing Miiiw Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Dongguan Powerise Fashion Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Qiji (Xiamen) Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Turok Steinhardt (Beijing) Optical Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Tianjin Smate Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Beijing KingSmith Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Shanghai Kaco Industrial Co., Ltd. (Note (a)) | Associate of the Group |
| Beijing Madv Technology Co., Ltd. (Note (a)) | Associate of the Group |
| XiaoHou Technology Co., Ltd. (Note (a)) | Associate of the Group |
| Shoulder Electronics Ltd. (Note (a)) | Associate of the Group |
| Qingping Technology (Beijing) Co., Ltd. (Note (a)) | Associate of the Group |
| Ningbo Sawadika Electrical Appliance Co., Ltd. (Note (a)) | Associate of the Group |
| Shanghai Sunmi Technology Co., Ltd. (Note (a)) | Associate of the Group |
| MiaoMiaoCe Technology (Beijing) Co., Ltd. (Note (a)) | Associate of the Group |
| Sichuan Xin Wang Bank Co., Ltd. (Note 11(b)) | Associate of the Group |
| Shanghai Longcheer Technology Co., Ltd. (Note 11(b)) | Associate of the Group |
| Beijing Runzhi Commercial Management Co., Ltd. | Associate of the Group |
| Shunwei Ventures II (Hong Kong) Ltd. | Controlled by a director |
| China Resources Land Construction Business Unit | Associate of the Group |
| Nanjing Bigfish Semiconductor Company Ltd. (Note 11(b)) | Associate of the Group |
| Zhuhai Samyou Environmental Technology Co., Ltd. (Note 11(b)) | Associate of the Group |
| Khorgos Puli Network Technology Co., Ltd. | Associate of the Group |
| Blackshark H.K Ltd. (Note 11(b)) | Associate of the Group |
| Beijing Xiaomi Insurance Co., Ltd. (Note 11(b)) | Associate of the Group |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions (continued)

### (a) Names and relationships with related parties (continued)

Notes:

(a) The Group's investments were made in the form of ordinary shares with preferential rights or convertible redeemable preferred shares which are accounted as financial assets measured at fair value through profit or loss.

### (b) Significant transactions with related parties

| | Year ended December 31, | |
|---|---|---|
| | **2019** | 2018 |
| | **RMB'000** | RMB'000 |
| **(i) Sales of goods and services** | | |
| Associates of the Group | **1,666,141** | 1,153,491 |
| Associates of Lei Jun | **2,156** | 25,376 |
| | **1,668,297** | 1,178,867 |
| **(ii) Purchases of goods and services** | | |
| Associates of the Group | **27,221,258** | 18,634,514 |
| Associates of Lei Jun | **517** | 14,768 |
| | **27,221,775** | 18,649,282 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions (continued)

### (c) Year end balances with related parties

| | As of December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| (i) Trade receivables from related parties | | |
| Associates of the Group | 324,027 | 361,792 |
| Associates of Lei Jun | — | 2,816 |
| | 324,027 | 364,608 |
| (ii) Trade payables to related parties | | |
| Associates of the Group | 6,061,497 | 4,004,778 |
| Associates of Lei Jun | 1,829 | 1,916 |
| | 6,063,326 | 4,006,694 |
| (iii) Other receivables from related parties | | |
| Associates of the Group | 373,071 | 243,126 |
| (iv) Other payables to related parties | | |
| Associates of the Group | 861,736 | 770,032 |
| Controlled by a director | 79,466 | 76,966 |
| Associates of Lei Jun | 7,476 | 7,652 |
| | 948,678 | 854,650 |
| (v) Prepayments | | |
| Associates of the Group | 136,899 | 88,289 |
| (vi) Advance from customers | | |
| Associates of the Group | 28,308 | 35,862 |
| Associates of the Lei Jun | 14 | 14 |
| | 28,322 | 35,876 |

All the balances with related parties above were unsecured, non-interest bearing and repayable within one year.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions (continued)

### (d) Loans to related parties

| | Year ended December 31, 2019 RMB'000 | 2018 RMB'000 |
|---|---|---|
| **Loans to associates:** | | |
| At the beginning of the year | 7,979 | 62,143 |
| Loans advanced | 34,934 | 50,000 |
| Loans repaid | (6,000) | (103,116) |
| Interest charged | 962 | 1,921 |
| Interest received | (70) | (2,210) |
| Currency translation differences | (3) | (759) |
| At the end of the year | 37,802 | 7,979 |

### (e) Loans from related parties

| | Year ended December 31, 2019 RMB'000 | 2018 RMB'000 |
|---|---|---|
| **Loans from associates:** | | |
| At the beginning of the year | — | 51,336 |
| Loans repaid | — | (50,958) |
| Interest charged | — | 146 |
| Interest paid | — | (855) |
| Currency translation differences | — | 331 |
| At the end of the year | — | — |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 39 Related party transactions (continued)

### (f) Key management compensation

| | Year ended December 31, | |
|---|---|---|
| | 2019 | 2018 |
| | RMB'000 | RMB'000 |
| Salaries | 11,676 | 15,124 |
| Discretionary bonuses | 7,600 | 1,200 |
| Share-based compensation | 428,811 | 10,464,196 |
| Employer's contribution to pension schedule | 1,159 | 989 |
| | 449,246 | 10,481,509 |

## 40 Events after the reporting period

An outbreak of Coronavirus Disease 2019 ("**COVID-19**") has been emerged since January 2020, and has been declared as a Public Health Emergency of International Concern on January 30, 2020 and subsequently characterized as a pandemic on March 11, 2020 by the World Health Organization. The Group has been paying close attention to the development of the COVID-19 outbreak and has conducted an assessment of its impact on the financial position and operating results of the Group.

As of the date on which this set of financial statements were authorized for issue, the Group has identified some factors which might have impact on the Group's financial performance, including offline hardware sales, supply chains, and overseas demand, etc. The Group will closely monitor the latest development of the COVID-19 outbreak so as to adopt positive counter-measures to overcome any challenges arising and to assess the related impact to the Group on a continuous basis.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 41 Financial position and reserve movement of the Company

### (a) Financial position of the Company

| | As of December 31, 2019 RMB'000 | 2018 RMB'000 |
|---|---|---|
| **Assets** | | |
| **Non-current assets** | | |
| Property and equipment | 35 | 35 |
| Investment in subsidiaries | 17,854,701 | 13,434,702 |
| Other assets | 78 | 77 |
| | 17,854,814 | 13,434,814 |
| **Current assets** | | |
| Prepayments and other receivables | 21,319,432 | 30,217,183 |
| Cash and cash equivalents | 58,359 | 5,707 |
| | 21,377,791 | 30,222,890 |
| **Total assets** | 39,232,605 | 43,657,704 |
| **Equity and liabilities** | | |
| **Equity attributable to owners of the Company** | | |
| Share capital | 388 | 377 |
| Reserves (Note 41(b)) | 39,223,583 | 39,159,983 |
| **Total equity** | 39,223,971 | 39,160,360 |
| **Liabilities** | | |
| **Current liabilities** | | |
| Other payables and accruals | 8,634 | 4,497,344 |
| | 8,634 | 4,497,344 |
| **Total liabilities** | 8,634 | 4,497,344 |
| **Total equity and liabilities** | 39,232,605 | 43,657,704 |

The balance sheet of the Company was approved by the Board of Directors on March 31, 2020 and was signed on its behalf:

Lei Jun

Lin Bin

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 41 Financial position and reserve movement of the Company (continued)

### (b) Reserve movement of the Company

| | Treasury shares RMB'000 | Share premium RMB'000 | Share-based compensation reserve RMB'000 | Currency translation differences RMB'000 | Capital reserve RMB'000 | Accumulated losses RMB'000 | Others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|---|---|
| At January 1, 2019 | — | 43,851,282 | 5,436,038 | 985,481 | 25,950 | (11,148,160) | 9,392 | 39,159,983 |
| Purchase of own shares | (2,932,111) | — | — | — | — | — | — | (2,932,111) |
| Cancellation of shares | 1,879,289 | (1,882,527) | — | — | — | — | — | (3,238) |
| Release of ordinary shares from Share Scheme Trust | — | 167,447 | (139,015) | — | — | — | — | 28,432 |
| Employees share-based compensation scheme: | | | | | | | | |
| — value of employee services (Note 28) | — | — | 2,127,967 | — | — | — | — | 2,127,967 |
| — exercise of share options and restricted stock units (Note 28) | — | 1,442,634 | (1,184,767) | — | — | — | — | 257,867 |
| Currency translation differences (Note (a)) | — | — | — | 508,584 | — | — | — | 508,584 |
| Profit for the year | — | — | — | — | — | 76,099 | — | 76,099 |
| At December 31, 2019 | (1,052,822) | 43,578,836 | 6,240,223 | 1,494,065 | 25,950 | (11,072,061) | 9,392 | 39,223,583 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in RMB unless otherwise indicated)

## 41 Financial position and reserve movement of the Company (continued)

### (b) Reserve movement of the Company (continued)

| | Share premium RMB'000 | Share-based compensation reserve RMB'000 | Currency translation differences RMB'000 | Capital reserve RMB'000 | Accumulated losses RMB'000 | Others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|---|
| **At January 1, 2018** | 742,760 | 3,816,153 | (3,495,173) | 25,950 | (150,421,487) | 9,392 | (149,322,405) |
| Issuance of ordinary shares | 9,827,146 | – | – | – | – | – | 9,827,146 |
| Issuance of ordinary shares relating to initial public offering, net of underwriting commissions and other issuance costs | 23,248,593 | – | – | – | – | – | 23,248,593 |
| Release of ordinary shares from Share Scheme Trust | 933,592 | (841,640) | – | – | – | – | 91,952 |
| Conversion of convertible redeemable preferred shares to ordinary shares | 151,100,334 | – | – | – | – | – | 151,100,334 |
| Employees share-based compensation scheme: | | | | | | | |
| – value of employee services (Note 28) | – | 2,461,525 | – | – | – | – | 2,461,525 |
| Acquisition of additional equity interests in non-wholly owned subsidiaries | 230,899 | – | – | – | – | – | 230,899 |
| Currency translation differences (Note (a)) | – | – | (1,098,818) | – | – | – | (1,098,818) |
| Share premium set off the accumulated losses and other reserves | (142,232,042) | – | 5,579,472 | – | 136,652,570 | – | – |
| Profit for the year | – | – | – | – | 2,620,757 | – | 2,620,757 |
| **At December 31, 2018** | 43,851,282 | 5,436,038 | 985,481 | 25,950 | (11,148,160) | 9,392 | 39,159,983 |

Note:

(a) Foreign currency translation reserve represents the difference arising from the translation of the financial statements of the Company as its functional currency in US$, different from its presentation currency as RMB.

**CONDENSED CONSOLIDATED INCOME STATEMENTS**
*For the three months and nine months ended September 30, 2020*
*(Expressed in Renminbi (“**RMB**”))*

| | Note | **Unaudited Three months ended September 30, 2020 RMB’000** | Unaudited Three months ended September 30, 2019 RMB’000 | **Unaudited Nine months ended September 30, 2020 RMB’000** | Unaudited Nine months ended September 30, 2019 RMB’000 |
|---|---|---|---|---|---|
| **Revenue** | 2 | **72,162,777** | 53,661,006 | **175,402,749** | 149,368,958 |
| Cost of sales | 2, 3 | **(61,997,121)** | (45,424,572) | **(149,977,190)** | (128,658,228) |
| **Gross profit** | | **10,165,656** | 8,236,434 | **25,425,559** | 20,710,730 |
| Selling and marketing expenses | 3 | **(3,600,582)** | (2,537,037) | **(9,449,131)** | (6,677,015) |
| Administrative expenses | 3 | **(852,715)** | (843,760) | **(2,470,674)** | (2,199,295) |
| Research and development expenses | 3 | **(2,321,264)** | (2,033,115) | **(6,150,520)** | (5,239,839) |
| Fair value changes on investments measured at fair value through profit or loss | 4 | **3,417,924** | 32,533 | **6,131,958** | 1,994,595 |
| Share of (losses)/gains of investments accounted for using the equity method | | **(10,696)** | (240,560) | **1,012,687** | (398,032) |
| Other income | | **139,291** | 448,379 | **396,069** | 914,979 |
| Other (losses)/gains, net | | **(240,995)** | 49,906 | **(463,114)** | (43,060) |
| **Operating profit** | | **6,696,619** | 3,112,780 | **14,432,834** | 9,063,063 |
| Finance (expenses)/income, net | | **(1,245,938)** | 182,068 | **(1,660,268)** | 383,243 |
| **Profit before income tax** | | **5,450,681** | 3,294,848 | **12,772,566** | 9,446,306 |
| Income tax expenses | | **(586,333)** | (775,419) | **(1,254,851)** | (1,779,575) |
| **Profit for the period** | | **4,864,348** | 2,519,429 | **11,517,715** | 7,666,731 |
| **Attributable to:** | | | | | |
| — Owners of the Company | | **4,880,596** | 2,525,063 | **11,542,239** | 7,602,978 |
| — Non-controlling interests | | **(16,248)** | (5,634) | **(24,524)** | 63,753 |
| | | **4,864,348** | 2,519,429 | **11,517,715** | 7,666,731 |
| **Earnings per share (expressed in RMB per share):** | | | | | |
| Basic | | **0.203** | 0.106 | **0.483** | 0.320 |
| Diluted | | **0.198** | 0.102 | **0.472** | 0.308 |

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

*For the three months and nine months ended September 30, 2020*
*(Expressed in RMB)*

| | Note | Unaudited Three months ended September 30, 2020 RMB'000 | Unaudited Three months ended September 30, 2019 RMB'000 | Unaudited Nine months ended September 30, 2020 RMB'000 | Unaudited Nine months ended September 30, 2019 RMB'000 |
|---|---|---|---|---|---|
| **Profit for the period** | | **4,864,348** | 2,519,429 | **11,517,715** | 7,666,731 |
| **Other comprehensive (loss)/income:** | | | | | |
| *Items that may be reclassified subsequently to profit or loss* | | | | | |
| Share of other comprehensive (loss)/income of investments accounted for using the equity method | | **(44,809)** | 59,914 | **(27,826)** | 45,384 |
| Transfer of share of other comprehensive income to profit or loss upon deemed disposal of an associate | | **—** | — | **(4,773)** | — |
| Net losses from changes in fair value of financial assets at fair value through other comprehensive income | | **(5,925)** | — | **(3,824)** | — |
| Currency translation differences | | **(44,066)** | (18,935) | **(7,943)** | 14,701 |
| *Item that will not be reclassified subsequently to profit or loss* | | | | | |
| Currency translation differences | | **(1,223,904)** | 869,667 | **(784,348)** | 951,276 |
| **Other comprehensive (loss)/income for the period, net of tax** | | **(1,318,704)** | 910,646 | **(828,714)** | 1,011,361 |
| **Total comprehensive income for the period** | | **3,545,644** | 3,430,075 | **10,689,001** | 8,678,092 |
| **Attributable to:** | | | | | |
| — Owners of the Company | | **3,561,639** | 3,425,235 | **10,707,497** | 8,601,235 |
| — Non-controlling interests | | **(15,995)** | 4,840 | **(18,496)** | 76,857 |
| | | **3,545,644** | 3,430,075 | **10,689,001** | 8,678,092 |

**CONDENSED CONSOLIDATED BALANCE SHEET**

*As of September 30, 2020*

*(Expressed in RMB)*

| | Note | **Unaudited As of September 30, 2020 RMB'000** | Audited As of December 31, 2019 RMB'000 |
|---|---|---|---|
| **Assets** | | | |
| **Non-current assets** | | | |
| Property and equipment | | **6,990,443** | 6,992,331 |
| Intangible assets | | **1,355,619** | 1,672,002 |
| Long-term bank deposits | | **6,395,493** | 590,157 |
| Investments accounted for using the equity method | | **12,415,403** | 9,300,507 |
| Long-term investments measured at fair value through profit or loss | 4 | **27,039,639** | 20,679,363 |
| Deferred income tax assets | | **1,714,694** | 1,283,415 |
| Other non-current assets | | **5,767,076** | 5,572,346 |
| | | **61,678,367** | 46,090,121 |
| **Current assets** | | | |
| Inventories | 6 | **34,996,234** | 32,585,438 |
| Trade receivables | 5 | **13,482,432** | 6,948,567 |
| Loan receivables | | **11,139,407** | 12,723,503 |
| Prepayments and other receivables | | **20,336,208** | 19,837,018 |
| Short-term investments measured at amortized cost | 4 | **341,527** | — |
| Short-term investments measured at fair value through other comprehensive income | 4 | **862,149** | — |
| Short-term investments measured at fair value through profit or loss | 4 | **21,097,732** | 16,463,390 |
| Short-term bank deposits | | **14,156,263** | 21,523,043 |
| Restricted cash | | **3,257,432** | 1,538,266 |
| Cash and cash equivalents | | **30,257,712** | 25,919,861 |
| | | **149,927,096** | 137,539,086 |
| **Total assets** | | **211,605,463** | 183,629,207 |

| | Note | Unaudited As of September 30, 2020 RMB'000 | Audited As of December 31, 2019 RMB'000 |
|---|---|---|---|
| **Equity and liabilities** | | | |
| **Equity attributable to owners of the Company** | | | |
| Share capital | | **392** | 388 |
| Reserves | | **94,228,146** | 81,330,186 |
| | | **94,228,538** | 81,330,574 |
| **Non-controlling interests** | | **339,840** | 327,102 |
| **Total equity** | | **94,568,378** | 81,657,676 |
| **Liabilities** | | | |
| **Non-current liabilities** | | | |
| Borrowings | 7 | **7,183,648** | 4,786,856 |
| Deferred income tax liabilities | | **419,568** | 579,902 |
| Warranty provision | | **750,523** | 667,857 |
| Other non-current liabilities | | **9,147,534** | 3,756,211 |
| | | **17,501,273** | 9,790,826 |
| **Current liabilities** | | | |
| Trade payables | 8 | **63,256,578** | 59,527,940 |
| Other payables and accruals | | **11,253,648** | 9,101,343 |
| Advance from customers | | **10,085,567** | 8,237,119 |
| Borrowings | 7 | **11,385,210** | 12,836,555 |
| Income tax liabilities | | **835,543** | 479,350 |
| Warranty provision | | **2,719,266** | 1,998,398 |
| | | **99,535,812** | 92,180,705 |
| **Total liabilities** | | **117,037,085** | 101,971,531 |
| **Total equity and liabilities** | | **211,605,463** | 183,629,207 |

**CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS**
*For the nine months ended September 30, 2020*
*(Expressed in RMB)*

| | **Unaudited Nine months ended September 30, 2020 RMB'000** | 2019 RMB'000 |
|---|---|---|
| Net cash generated from operating activities | **8,350,998** | 13,908,001 |
| Net cash used in investing activities | **(7,173,063)** | (11,768,862) |
| Net cash generated from financing activities | **3,839,898** | 2,576,968 |
| **Net increase in cash and cash equivalents** | **5,017,833** | 4,716,107 |
| Cash and cash equivalents at the beginning of the period | **25,919,861** | 30,230,147 |
| Effects of exchange rate changes on cash and cash equivalents | **(679,982)** | 592,910 |
| **Cash and cash equivalents at the end of the period** | **30,257,712** | 35,539,164 |

## 1 Basis of preparation

The condensed consolidated interim financial information comprises the condensed consolidated balance sheet as of September 30, 2020, the condensed consolidated income statements and the condensed consolidated statements of comprehensive income for the three-month and nine-month periods then ended, the condensed consolidated statement of changes in equity and the condensed consolidated statement of cash flows for the nine-month period then ended, and a summary of significant accounting policies and other explanatory notes (the "**Interim Financial Information**"). The Interim Financial Information is presented in RMB, unless otherwise stated.

The Interim Financial Information has been prepared in accordance with International Accounting Standard ("**IAS**") 34, "Interim Financial Reporting", issued by the International Accounting Standards Board ("**IASB**").

The Interim Financial Information does not include all the notes of the type normally included in annual financial statements. The Interim Financial Information should be read in conjunction with the annual audited financial statements of the Group for the year ended December 31, 2019 which have been prepared in accordance with International Financial Reporting Standards ("**IFRS**") by the Group as set out in the 2019 annual report of the Company dated March 31, 2020 (the "**2019 Financial Statements**").

The accounting policies and methods of computations used in the preparation of the Interim Financial Information are consistent with those used in the preparation of the annual financial statements for the year ended December 31, 2019, as described in the 2019 Financial Statements, except for the adoption of certain new and amended standards which has had no significant impact on the results and the financial position of the Group.

## 2 Segment information

The Group's business activities, for which discrete financial statements are available, are regularly reviewed and evaluated by the Chief Operating Decision Maker ("**CODM**"). The CODM, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Chief Executive Officer that makes strategic decisions. As a result of this evaluation, the Group determined that it has operating segments as follows:

- Smartphones
- IoT and lifestyle products
- Internet services
- Others

The CODM assesses the performance of the operating segments mainly based on segment revenue and gross profit of each operating segment. There were no material inter-segment sales during the three months and nine months ended September 30, 2020 and 2019. The revenues from external customers reported to the CODM are measured in a manner consistent with that applied in the consolidated income statement.

The segment results for the three months and nine months ended September 30, 2020 and 2019 are as follows:

| | **Three months ended September 30, 2020** | | | | |
|---|---|---|---|---|---|
| | **Smartphones RMB'000** | **IoT and lifestyle products RMB'000** | **Internet services RMB'000** | **Others RMB'000** | **Total RMB'000** |
| **(Unaudited)** | | | | | |
| Segment revenues | **47,604,133** | **18,119,021** | **5,771,890** | **667,733** | **72,162,777** |
| Cost of sales | **(43,615,083)** | **(15,538,630)** | **(2,283,348)** | **(560,060)** | **(61,997,121)** |
| Gross profit | **3,989,050** | **2,580,391** | **3,488,542** | **107,673** | **10,165,656** |

| | Three months ended September 30, 2019 | | | | |
|---|---|---|---|---|---|
| | Smartphones RMB'000 | IoT and lifestyle products RMB'000 | Internet services RMB'000 | Others RMB'000 | Total RMB'000 |
| **(Unaudited)** | | | | | |
| Segment revenues | 32,268,379 | 15,606,310 | 5,309,025 | 477,292 | 53,661,006 |
| Cost of sales | (29,375,158) | (13,608,046) | (1,967,285) | (474,083) | (45,424,572) |
| Gross profit | 2,893,221 | 1,998,264 | 3,341,740 | 3,209 | 8,236,434 |

| | **Nine months ended September 30, 2020** | | | | |
|---|---|---|---|---|---|
| | **Smartphones RMB'000** | **IoT and lifestyle products RMB'000** | **Internet services RMB'000** | **Others RMB'000** | **Total RMB'000** |
| **(Unaudited)** | | | | | |
| Segment revenues | **109,556,405** | **46,356,097** | **17,580,207** | **1,910,040** | **175,402,749** |
| Cost of sales | **(100,824,007)** | **(40,296,735)** | **(7,159,991)** | **(1,696,457)** | **(149,977,190)** |
| Gross profit | **8,732,398** | **6,059,362** | **10,420,216** | **213,583** | **25,425,559** |

| | Nine months ended September 30, 2019 | | | | |
|---|---|---|---|---|---|
| | Smartphones RMB'000 | IoT and lifestyle products RMB'000 | Internet services RMB'000 | Others RMB'000 | Total RMB'000 |
| **(Unaudited)** | | | | | |
| Segment revenues | 91,298,070 | 42,593,957 | 14,146,516 | 1,330,415 | 149,368,958 |
| Cost of sales | (84,930,288) | (37,475,124) | (4,929,716) | (1,323,100) | (128,658,228) |
| Gross profit | 6,367,782 | 5,118,833 | 9,216,800 | 7,315 | 20,710,730 |

The Company is domiciled in the Cayman Islands while the Group mainly operates its businesses in mainland China and other countries or regions. For the three months and nine months ended September 30, 2020 and 2019, the geographical information on the total revenues is as follows:

| | Three months ended September 30, | | | | Nine months ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|
| | **2020** | | 2019 | | **2020** | | 2019 | |
| | **RMB'000** | **%** | RMB'000 | % | **RMB'000** | **%** | RMB'000 | % |
| | **(Unaudited)** | | (Unaudited) | | **(Unaudited)** | | (Unaudited) | |
| Mainland China | **32,393,887** | **44.9** | 27,519,935 | 51.3 | **86,773,126** | **49.5** | 84,580,522 | 56.6 |
| Rest of the world (Note(a)) | **39,768,890** | **55.1** | 26,141,071 | 48.7 | **88,629,623** | **50.5** | 64,788,436 | 43.4 |
| | **72,162,777** | | 53,661,006 | | **175,402,749** | | 149,368,958 | |

*Note:*

(a) Revenues outside mainland China are mainly from India and Europe.

## 3 Expenses by nature

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | **2020** | 2019 | **2020** | 2019 |
| | **RMB'000** | RMB'000 | **RMB'000** | RMB'000 |
| | **(Unaudited)** | (Unaudited) | **(Unaudited)** | (Unaudited) |
| Cost of inventories sold | **55,583,881** | 40,447,770 | **132,383,272** | 114,274,999 |
| Provision for impairment of inventories | **1,021,402** | 640,751 | **2,528,191** | 3,112,135 |
| Royalty fees | **1,739,479** | 1,391,398 | **4,798,279** | 3,633,643 |
| Employee benefit expenses | **2,470,659** | 2,121,071 | **6,852,363** | 5,939,590 |
| Depreciation of property and equipment, right-of-use assets and investment properties | **270,577** | 239,416 | **751,129** | 668,915 |
| Amortization of intangible assets | **123,135** | 116,414 | **367,619** | 364,201 |
| Promotion and advertising expenses | **1,295,182** | 849,946 | **3,215,560** | 1,827,730 |
| Content fees to game developers and video providers | **571,052** | 484,044 | **1,815,080** | 1,226,764 |
| Credit loss allowance for loan receivables | **415,978** | 414,858 | **1,599,295** | 868,086 |
| Consultancy and professional service fees | **224,209** | 209,054 | **643,029** | 487,501 |
| Cloud service, bandwidth and server custody fees | **549,610** | 372,472 | **1,467,712** | 1,318,501 |
| Warranty expenses | **1,063,454** | 752,792 | **2,385,742** | 2,080,224 |

## 4 Investments

| | As of September 30, 2020 RMB'000 (Unaudited) | As of December 31, 2019 RMB'000 (Audited) |
|---|---|---|
| **Current assets** | | |
| Short-term investments measured at fair value through profit or loss | **21,097,732** | 16,463,390 |
| Short-term investments measured at fair value through other comprehensive income | **862,149** | — |
| Short-term investments measured at amortized cost | **341,527** | — |
| | **22,301,408** | 16,463,390 |
| **Non-current assets** | | |
| Long-term investments measured at fair value through profit or loss | | |
| — Equity investments | **10,086,063** | 7,272,454 |
| — Preferred shares investments | **16,953,576** | 13,406,909 |
| | **27,039,639** | 20,679,363 |

Amounts recognized in profit or loss

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | **2020 RMB'000 (Unaudited)** | 2019 RMB'000 (Unaudited) | **2020 RMB'000 (Unaudited)** | 2019 RMB'000 (Unaudited) |
| Fair value changes on equity investments | **2,978,297** | 208,240 | **5,142,793** | 1,738,986 |
| Fair value changes on preferred shares investments | **274,789** | (146,237) | **549,396** | 231,785 |
| Fair value changes on short-term investments measured at fair value through profit or loss | **164,838** | (29,470) | **439,769** | 23,824 |
| | **3,417,924** | 32,533 | **6,131,958** | 1,994,595 |

## 5 Trade receivables

The Group usually allows a credit period within 180 days to its customers. Aging analysis of trade receivables based on invoice date is as follows:

| | **As of September 30, 2020 RMB'000 (Unaudited)** | As of December 31, 2019 RMB'000 (Audited) |
|---|---|---|
| **Trade receivables** | | |
| Up to 3 months | **12,611,451** | 6,076,873 |
| 3 to 6 months | **631,348** | 550,929 |
| 6 months to 1 year | **339,355** | 308,197 |
| 1 to 2 years | **56,135** | 98,643 |
| Over 2 years | **68,422** | 29,706 |
| | **13,706,711** | 7,064,348 |
| Less: credit loss allowance | **(224,279)** | (115,781) |
| | **13,482,432** | 6,948,567 |

## 6 Inventories

| | **As of September 30, 2020 RMB'000 (Unaudited)** | As of December 31, 2019 RMB'000 (Audited) |
|---|---|---|
| Raw materials | **12,841,353** | 9,347,930 |
| Finished goods | **14,626,519** | 18,030,136 |
| Work in progress | **3,186,201** | 2,422,504 |
| Spare parts | **1,995,659** | 1,733,042 |
| Others | **3,482,828** | 1,925,785 |
| | **36,132,560** | 33,459,397 |
| Less: provision for impairment | **(1,136,326)** | (873,959) |
| | **34,996,234** | 32,585,438 |

## 7 Borrowings

| | As of September 30, 2020 RMB'000 (Unaudited) | As of December 31, 2019 RMB'000 (Audited) |
|---|---|---|
| **Included in non-current liabilities** | | |
| Asset-backed securities | **930,000** | 2,305,000 |
| Fund raised through trusts | **262,500** | 450,000 |
| Secured borrowings | **1,772,757** | 1,825,856 |
| Unsecured borrowings | **4,218,391** | 206,000 |
| | **7,183,648** | 4,786,856 |
| **Included in current liabilities** | | |
| Asset-backed securities | **4,338,851** | 2,647,641 |
| Fund raised through trusts | **338,070** | 420,000 |
| Secured borrowings | **1,607,280** | 1,796,701 |
| Unsecured borrowings | **5,101,009** | 7,972,213 |
| | **11,385,210** | 12,836,555 |

## 8 Trade payables

Trade payables primarily include payables for inventories. As of September 30, 2020 and December 31, 2019, the carrying amounts of trade payables were primarily denominated in RMB, US$ and India Rupees.

Trade payables and their aging analysis based on invoice date are as follows:

| | As of September 30, 2020 RMB'000 (Unaudited) | As of December 31, 2019 RMB'000 (Audited) |
|---|---|---|
| Up to 3 months | **60,395,802** | 57,942,872 |
| 3 to 6 months | **2,141,113** | 1,136,595 |
| 6 months to 1 year | **575,759** | 342,864 |
| 1 to 2 years | **48,206** | 55,709 |
| Over 2 years | **95,698** | 49,900 |
| | **63,256,578** | 59,527,940 |

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