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Post Hearing Information Pack of



Baidu, Inc.

百度集團股份有限公司

(the “Company”)

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

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Baidu, Inc.
百度集團股份有限公司

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

[REDACTED]

Number of [REDACTED] under the [REDACTED] : [REDACTED] (subject to the [REDACTED])
Number of [REDACTED] : [REDACTED] (subject to adjustment)
Number of [REDACTED] : [REDACTED] (subject to adjustment and the [REDACTED])
Maximum [REDACTED] : [REDACTED]
Par Value : US\$[0.000000625] per Share
Stock Code : [REDACTED]

Joint Sponsors

[(In alphabetical order)]



[REDACTED]

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The Company is controlled through weighted voting rights. Prospective [REDACTED] should be aware of the potential risks of [REDACTED] in a company with a WVR structure, in particular that the WVR beneficiaries, whose interests may not necessarily be aligned with those of our Shareholders as a whole, will be in a position to exert significant influence over the outcome of Shareholders' resolutions, irrespective of how other Shareholders vote. For further information about the risks associated with our WVR structure, please refer to "Risk Factors—Risks Related to Our Corporate Structure." Prospective [REDACTED] should make the decision to [REDACTED] in the Company only after due and careful consideration.

[REDACTED]

[REDACTED]

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IMPORTANT

[REDACTED]

EXPECTED TIMETABLE⁽¹⁾

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EXPECTED TIMETABLE⁽¹⁾

[REDACTED]

EXPECTED TIMETABLE⁽¹⁾

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SUMMARY

This summary aims to give you an overview of the information contained in this document. As it is a summary, it does not contain all the information that may be important to you and is qualified in its entirety by and should be read in conjunction with, the full document. You should read the whole document before you decide to [REDACTED] in the [REDACTED]. There are risks associated with any [REDACTED]. Some of the particular risks in [REDACTED] in the [REDACTED] are set forth in “Risk Factors”. You should read that section carefully before you decide to [REDACTED] in the [REDACTED].

Overview

Our mission is to make the complicated world simpler through technology.

We are a leading AI company with a strong Internet foundation. We have been investing in AI since 2010, to improve search and ad monetization, and have used “Baidu Brain,” our core AI technology engine to develop new AI businesses. The breadth and depth of our AI capabilities provide the differentiating foundational technologies that power all of our businesses. According to the CIC Report, our AI leadership in China is evidenced in the following aspects:

- We hold the largest portfolio of AI patents and AI patent applications in China as of October 30, 2020;
- Our deep learning framework, PaddlePaddle, is the No. 1 deep learning framework in China and No. 2 globally behind Facebook Pytorch in terms of cumulative pull requests as of December 31, 2020;
- Our Baidu Open AI Platform, with a developer community of over 2.65 million members, is the largest open AI platform in China, based on the number of developers as of December 31, 2020; and
- Baidu OSChina, which runs on Baidu cloud infrastructure, is the largest development platform for open source activities of in China and No. 3 globally (behind GitHub and Gitlab), in terms of the number of developers as of December 31, 2020.

We are one of the very few companies that offers a full AI stack, encompassing an infrastructure consists of AI chips, deep learning framework, core AI capabilities, such as natural language processing, knowledge graph, speech recognition, computer vision and augmented reality, as well as an open AI platform to facilitate wide application and usage. Our technological innovation in AI has been well recognized by the global community. For instance, ERNIE, our natural language processing framework, became the first AI model to score above 90 on GLUE (General Language Understanding Evaluation), which is widely considered as the benchmark for testing AI language understanding, and won the SAIL (Super AI Leader) award, the highest honorary recognition at the 2020 World Artificial Intelligence Conference. We have put our leading AI into innovative use. For example, we are the first to receive driverless licenses in China and the U.S. and we are testing driverless vehicles in China.

Baidu was founded as a search engine business in 2000 with the belief that technology can change the way people discover and consume information. At the heart of Baidu search is its ability to better understand a users’ search queries and to answer these queries by matching the most relevant information in ranked search results. To achieve this, we continuously innovate and develop new technologies and products that enhance Baidu search user experience. We began to use AI a decade ago to power these technologies in order to better match user search intent with the large amount of information on the Internet. For instance, our natural language processing, an AI capability, enables the understanding of important details of a query, particularly in complex conversational queries. This helps optimize search results returned and increase the satisfaction rate of users. Years of tagging,

SUMMARY

understanding and intelligently processing all forms of content on the Internet—text, images and videos—with AI has helped us develop Baidu Brain, our core AI technology engine, which in turn has enabled us to further develop leading AI technologies and commercialize them through products and services for consumers, enterprises and the public sector. Our ability to continuously invest heavily in research and development is made possible by the durable revenue that we generated as a leading Internet platform.

The widespread usage of our open AI platform by developers and businesses creates a network effect for our AI technologies, products and services. The more developers and businesses use our AI models, tool kits and services, the better our AI capabilities become, which in turn further increase the attractiveness of our AI platform to developers and business communities. This network effect helps us obtain unique insights into different kinds of products and services that are in demand and have real-world application across different industries, setting a strong foundation for us to make investment decisions and lead with technology, products and services in the markets that we have entered.

Our large portfolio of products and services is accessed by over one billion devices monthly, and our business spans across an ecosystem of hundreds of millions of users, millions of developers and hundreds of thousands of enterprises. Our usage of a strong technology foundation to support an open platform business model not only draws more participants into our ecosystem, but also adds richness and vibrancy to our ecosystem, strengthening the long-term prospect and vitality of our business overall. We usually start the development of a business with a strong technology platform, on which we build products and services for our customers and users, and through an open platform architecture, we attract a wide array of partners to our ecosystem to expand the offerings to our customers and users. The platform could then grow organically and by leveraging the power of our partners in the ecosystem, which over time feed into a virtuous cycle.

Over the past two decades, we have demonstrated a track record for long-term growth and strong profitability, which has enabled us to invest in a diversified portfolio of products and services with large market opportunities and further improve our long-term growth prospects. Through years of investment in research, AI chip design, developer community, patents and talent development, we are turning AI into innovative use cases. Powered by AI, Baidu Core, which excludes iQIYI and contributed over 70% of our total revenues during the Track Record Period, mainly provides search-based, feed-based, and other online marketing services, as well as products and services from new AI initiatives in the following three growth engines:

- *Mobile Ecosystem*: a portfolio of over one dozen apps, including Baidu App, Haokan and Baidu Post, which provides an open platform that aggregates a wide range of third-party, long-tail content and services through our AI building blocks and which helps communities connect and share knowledge and information;
- *AI Cloud*: a full suite of cloud services and solutions, including PaaS, SaaS and IaaS and uniquely differentiated by our AI solutions; and
- *Intelligent Driving & Other Growth Initiatives (OGI)*: our growth initiatives include intelligent driving (self-driving services, including HD Maps, automated valet parking and autonomous navigation pilot, intelligent electric vehicles and robotaxi fleets), as well as Xiaodu smart devices powered by DuerOS smart assistant and AI chip development.

SUMMARY

At the core of our Mobile Ecosystem is Baidu App, which is the No. 1 search-plus-feed app in China with an MAU of 544 million in December 2020. Unlike most mobile apps, which direct traffic to a closed content ecosystem, Baidu App, through our AI building blocks, aggregates content and services from third-party apps and websites, and directs traffic to third-party content and service providers with native-app like experience. Under an open-platform model, Baidu App can continue to grow our huge offering of third-party content and services, by leveraging our network partners of BJH Accounts, Smart Mini Program and Managed Page. Our decade-long experience with AI and the development of a powerful knowledge graph allow us to match user intent with long-tail, third-party content and services on our open platform.

Our Mobile Ecosystem also includes a portfolio of over one dozen apps, including Haokan and Baidu Post, providing a platform for people to discover and consume information through search and feed, interact and engage with creators, publishers, service providers and merchants. This native-app like experience from user acquisition to user relationship management to closed loop transactions demonstrates our value to merchants, enabling them to perform user life-time management on our platform, and has made Baidu App a leading online marketing services provider for both search and feed. Within our Mobile Ecosystem, we serve half-a-million customers by enabling them to tap into our massive user base. We monetize primarily through offering comprehensive and effective marketing services to fulfill our customers’ needs. We generate revenue primarily from providing search, feed and other marketing services, which account for a majority of our total revenues during the Track Record Period. We have made extensive use of AI technologies to develop innovative marketing services, such as dynamic ads, which recommends products from our marketing customers most fitting to each search user. Our marketing cloud also provides innovative AI capabilities to our marketing customers, so that users can still make product inquiries during non-business hours and Baidu Brain can automatically carry a conversation with users to facilitate transactions. In addition, the user engagement and user logins that have developed on our platform are enabling us to diversify monetization beyond online marketing into other services, such as live broadcasting, online games and membership.

Our AI Cloud is the leading AI public cloud service provider and a top four public cloud service provider in China in 2019, according to the CIC Report. Our AI Cloud offers a full suite of cloud services and solutions, including PaaS, SaaS and IaaS, and is differentiated with our AI solutions. Leveraging Baidu Brain, our AI solutions provide customers and developers with a comprehensive library of modularized solutions, including open source codes, pre-trained models, end-to-end development kits, tools and components. In addition, our AI Cloud customers can leverage our large library of key AI capabilities, such as knowledge graph, speech recognition and synthesis, natural language processing and computer vision. Our products and services, such as EasyDL and Baidu ML, make it easier for customers to use deep learning and machine learning to solve real world problems, and our cloud services are formulated to serve across different industries, including Internet, media, telecom, financial services, transportation and logistics, education and manufacturing.

Our Intelligent Driving & OGI consist of promising businesses in development with huge market opportunities, and some are at early-stage commercialization with a growing customer base. We are a market leader in intelligent driving and smart devices, and we are pursuing these large growth opportunities by leveraging our unique AI capabilities, data insights and internally developed chips. For example, in autonomous driving, Apollo is the market leader in China with 4.3 million accumulated test miles and 199 autonomous driving licenses across China, as of December 31, 2020. Our 199 autonomous driving licenses reflect the geographic reach of Apollo testing scenarios in China, compared to the second player with approximately 20 licenses. There are currently three Apollo robotaxi pilot programs running in China. Our strong brand and market leadership in autonomous

SUMMARY

driving has carried over to intelligent driving. Apollo is a well-recognized brand among automakers. We have signed strategic agreements with 10 leading automakers to power their passenger vehicles with Apollo Self Driving services, which includes Baidu high definition (HD) Maps and automated valet parking (AVP), and we recently announced the availability of Apollo autonomous navigation pilot (ANP). Under smart display, Xiaodu was ranked No. 1 in shipments globally for 2019. We also develop AI chips internally customized for Baidu Brain and specific AI usages to improve performance and costs. We believe these initiatives will strengthen our revenue drivers for long-term growth.

iQIYI produces, aggregates and distributes a wide variety of professionally produced content, as well as a broad spectrum of other entertainment-oriented video content.

We believe we have built a large and strong portfolio of products and services to give Baidu the scale necessary to invest heavily in technology, while optimizing our future for sustainable long-term growth. We derive significant synergies by incorporating the AI developed for search into other parts of our business. For example, large daily use of our visual search and voice search may be used to improve Apollo computer vision and DuerOS speech recognition capabilities.

We generated total revenues of RMB102.3 billion, RMB107.4 billion and RMB107.1 billion (US\$16.4 billion) in 2018, 2019 and 2020, respectively. Our revenue in 2020 was impacted by the COVID-19 pandemic, and we experienced revenue change of -7%, -1%, +1% and +5% year over year for the three months ended March 31, June 30, September 30 and December 31, 2020, respectively. We generated net income attributable to Baidu, Inc. of RMB27.6 billion, RMB2.1 billion and RMB22.5 billion (US\$3.4 billion) in 2018, 2019 and 2020, respectively. Net income attributed to Baidu, Inc. in 2019 included a non-cash impairment loss of RMB8.9 billion from investment in Trip.com.

Baidu Core generated revenues of RMB78.3 billion, RMB79.7 billion and RMB78.7 billion (US\$12.1 billion) in 2018, 2019 and 2020, respectively. Baidu Core’s revenue in 2020 was impacted by the COVID-19 pandemic, and Baidu Core experienced revenue change of -13%, -3%, +2% and +6% year over year for the three months ended March 31, June 30, September 30 and December 31, 2020, respectively. We generated net income attributable to Baidu Core of RMB33.6 billion, RMB7.6 billion and RMB26.5 billion (US\$4.1 billion) in 2018, 2019 and 2020, respectively. Net income attributed to Baidu Core in 2019 included a non-cash impairment loss of RMB8.9 billion from investment in Trip.com.

iQIYI generated revenues of RMB25.0 billion, RMB29.0 billion and RMB29.7 billion (US\$4.6 billion) in 2018, 2019 and 2020, respectively. We generated net loss attributable to iQIYI of RMB9.1 billion, RMB10.3 billion and RMB7.0 billion (US\$1.1 billion) in 2018, 2019 and 2020, respectively.

SUMMARY

Key Financial and Operating Metrics

Baidu Core

| | For the Month Ended December 31, | | |
|--|-------------------------------------|--------|--------|
| | 2018 | 2019 | 2020 |
| MAU of Baidu App (in millions) | 435 | 500 | 544 |
| DAU of Baidu App (in millions) | 161 | 195 | 202 |
| | For the Year Ended December 31, | | |
| | 2018 | 2019 | 2020 |
| Revenue (RMB in millions) | 78,271 | 79,711 | 78,684 |
| Operating profit (RMB in millions) | 23,808 | 15,261 | 20,538 |

iQIYI

| | As of December 31, | | |
|---|------------------------------------|---------|---------|
| | 2018 | 2019 | 2020 |
| Subscribing Members (in millions) | 87.4 | 106.9 | 101.7 |
| | For the Year Ended December 31, | | |
| | 2018 | 2019 | 2020 |
| Revenue (RMB in millions) | 24,989 | 28,994 | 29,707 |
| Operating loss (RMB in millions) | (8,306) | (9,258) | (6,041) |

OUR STRENGTHS

We believe the following competitive strengths contribute to our success and set us apart from our peers:

- leading technology company with world-class AI capabilities;
- Mobile Ecosystem: China’s leading content and services discovery ecosystem;
- AI Cloud: China’s leading AI cloud service provider;
- Intelligent Driving & Other Growth Initiatives: strong leadership in large AI-powered markets;
- platform-centric model cultivating vibrant ecosystems and capturing huge market opportunities;
- strong synergies across our AI-powered markets and offerings; and
- management team with decades-long proven track record of technology innovation and commercialization.

OUR STRATEGIES

We intend to pursue the following strategies to further grow our business:

- continue to invest in technology;
- continue to scale our AI Cloud;
- further develop and commercialize intelligent driving and other growth initiatives;
- continue to grow our Mobile Ecosystem; and
- selectively pursue M&A and strategic investments.

SUMMARY

Our Technology Innovation

We focus on technology and innovation. To stay at the forefront of the internet and AI, and to achieve long-term growth and success, we invest heavily in research and development. We have established several research AI labs in China and the United States to enhance our research and development capabilities, and to focus on AI, quantum computing and other areas. We have developed a proprietary AI technological infrastructure, which also powers other technologies, such as search technologies and large-scale systems. Our established infrastructure serves as the backbone for our AI, mobile and PC platforms.

Throughout our two-decade history, we have innovated and developed successful businesses. We have been at the forefront of technological innovation in the internet industry, evidenced by our pioneering search product offering since our founding, adoption of user preference algorithms and personalized product delivery in 2007, transition from personal computer (PC) to mobile in 2012, integration of search and related products and functionalities, like maps voice search and visual search into our offerings, deepening our investment in deep learning to enhance user experience and customer return-on-investment (ROI), focusing on AI as the engine to drive long-term growth and initiatives on deploying AI technologies beyond search and feed, into smart assistant, AI cloud solutions, AI chip design and autonomous driving. With a culture of innovation in mind, we have been a trailblazer in China’s search-plus-feed and other AI fields and offer a number of innovative technologies and services, such as auction-based P4P services, search plus feed, multi-source heterogeneous knowledge graph, and PaddlePaddle.

SUMMARY OF HISTORICAL FINANCIAL INFORMATION

Rule 13.46(2) of the Hong Kong Listing Rules requires an overseas issuer to send an annual report or a summary financial report within four months after the end of the financial year to which the report relates. As an issuer seeking a listing as a Grandfathered Greater China Issuer pursuant to Chapter 19C of the Hong Kong Listing Rules, we are not subject to the disclosure requirements under notes 4(a) and (b) to Rule 13.46(2) of the Hong Kong Listing Rules. As this document already includes the financial information of the Company for the year ended December 31, 2020, the Company will not separately prepare and send an annual report to its shareholders for the year ended December 31, 2020, which will not be in breach of its constitutional documents, laws and regulations of the Cayman Islands or other regulatory requirements.

SUMMARY

Selected Consolidated Statements of Comprehensive Income (Loss)

| | Year ended December 31, | | | |
|--|-------------------------|----------------|----------------|---------------|
| | 2018 | 2019 | 2020 | |
| | RMB | RMB | RMB | US\$ |
| | (in millions) | | | |
| Revenues: | | | | |
| Online marketing services | 81,912 | 78,093 | 72,840 | 11,163 |
| Others | 20,365 | 29,320 | 34,234 | 5,247 |
| Total revenues | 102,277 | 107,413 | 107,074 | 16,410 |
| Operating costs and expenses⁽¹⁾: | | | | |
| Cost of revenues | 51,744 | 62,850 | 55,158 | 8,454 |
| Selling, general and administrative | 19,231 | 19,910 | 18,063 | 2,769 |
| Research and development | 15,772 | 18,346 | 19,513 | 2,989 |
| Total operating costs and expenses | 86,747 | 101,106 | 92,734 | 14,212 |
| Operating profit | 15,530 | 6,307 | 14,340 | 2,198 |
| Total other income (loss), net | 11,795 | (6,647) | 8,750 | 1,341 |
| Income (loss) before income taxes | 27,325 | (340) | 23,090 | 3,539 |
| Income taxes | 4,743 | 1,948 | 4,064 | 623 |
| Net income (loss) | 22,582 | (2,288) | 19,026 | 2,916 |
| Less: Net loss attributable to non-controlling interests | (4,991) | (4,345) | (3,446) | (528) |
| Net income attributable to Baidu, Inc. | 27,573 | 2,057 | 22,472 | 3,444 |

Note:

(1) Share-based compensation expenses are allocated in operating costs and expenses as follows:

| | | | | |
|---|--------------|--------------|--------------|--------------|
| Cost of revenues | 224 | 327 | 360 | 55 |
| Selling, general and administrative | 1,725 | 1,768 | 1,897 | 290 |
| Research and development | 2,727 | 3,531 | 4,471 | 686 |
| Total | 4,676 | 5,626 | 6,728 | 1,031 |

Net income attributable to Baidu, Inc. increased from RMB2.1 billion in 2019 to RMB22.5 billion (US\$3.4 billion) in 2020. The increase primarily resulted from (i) total operating costs and expenses decreasing by RMB8.4 billion, from RMB101.1 billion 2019 to RMB92.7 billion (US\$14.2 billion) in 2020 (ii) total other income, net amounting to RMB8.8 billion (US\$1.3 billion) in 2020, compared to a total other loss, net of RMB6.6 billion in 2019, which included a non-cash impairment loss of RMB8.9 billion from investment in Trip.com.

Net income attributable to Baidu, Inc. decreased from RMB27.6 billion in 2018 to RMB2.1 billion in 2019. The decrease was primarily attributable to (i) total operating costs and expenses increasing by RMB14.4 billion, from RMB86.7 billion 2018 to RMB101.1 billion in 2019, and (ii) total other loss, net amounting to RMB6.6 billion in 2019, compared to a total other income, net of RMB11.8 billion in 2018, which mainly comprises gains from the disposal of Du Xiaoman (financial services business) and fair value gains on private company equity investments.

For more information, see “Financial Information” and Appendix IA Accountants’ Report.

SUMMARY

Selected Consolidated Balance Sheets Data

| | As of December 31, | | | |
|---|--------------------|----------------|----------------|---------------|
| | 2018 | 2019 | 2020 | |
| | RMB | RMB | RMB | US\$ |
| | (in millions) | | | |
| Cash and cash equivalents | 27,638 | 33,443 | 35,782 | 5,484 |
| Restricted cash | 2,189 | 996 | 758 | 117 |
| Short-term investments, net | 111,626 | 112,924 | 126,402 | 19,372 |
| Accounts receivable, net | 6,015 | 7,416 | 8,668 | 1,328 |
| Fixed assets, net | 17,903 | 18,311 | 17,508 | 2,683 |
| Goodwill | 18,536 | 18,250 | 22,248 | 3,410 |
| Long-term investments, net | 80,454 | 69,410 | 76,233 | 11,683 |
| Total assets | 297,566 | 301,316 | 332,708 | 50,990 |
| Short-term loans | 3,046 | 2,618 | 3,016 | 462 |
| Accounts payable and accrued liabilities | 35,381 | 32,701 | 36,716 | 5,627 |
| Customer deposits and deferred revenue | 9,221 | 11,062 | 12,626 | 1,935 |
| Long-term loans | 7,540 | 8,541 | 7,427 | 1,138 |
| Notes payable | 49,606 | 43,309 | 48,408 | 7,419 |
| Convertible senior notes | 4,712 | 12,297 | 16,679 | 2,556 |
| Total liabilities | 121,814 | 128,501 | 140,865 | 21,589 |
| Total equity | 175,036 | 171,706 | 188,741 | 28,926 |
| Noncontrolling interests | 12,139 | 8,107 | 6,045 | 927 |
| Total Baidu, Inc. shareholders' equity | 162,897 | 163,599 | 182,696 | 27,999 |
| Net current assets | 98,241 | 108,182 | 114,957 | 17,618 |

For a detailed discussion on our cash position as well as material changes in the various working capital items, see “Financial Information—Liquidity and Capital Resources.”

Our total shareholders' equity increased by 12% from RMB163.6 billion as of December 31, 2019 to RMB182.7 billion (US\$28.0 billion) as of December 31, 2020, primarily due to net income attributable to Baidu, Inc of RMB22.5 billion (US\$3.4 billion), share-based compensation of RMB5.7 billion (US\$881 million) and issuance of shares by our subsidiaries to noncontrolling interest of RMB2.3 billion (US\$346 million), and partially offset by repurchase and retirement of ordinary shares of RMB13.1 billion (US\$2.0 billion) for the year ended December 31, 2020.

Our total shareholders' equity slightly increased from RMB162.9 billion as of December 31, 2018 to RMB163.6 billion as of December 31, 2019, primarily due to net income attributable to Baidu, Inc of RMB2.1 billion and share-based compensation of RMB5.0 billion, and offset by other comprehensive loss of RMB1.6 billion and repurchase and retirement of ordinary shares of RMB5.0 billion in 2019.

Selected Consolidated Cash Flows Data

| | Year ended December 31, | | | |
|---|-------------------------|----------|----------|---------|
| | 2018 | 2019 | 2020 | |
| | RMB | RMB | RMB | US\$ |
| | (in millions) | | | |
| Net cash provided by operating activities | 35,967 | 28,458 | 24,200 | 3,709 |
| Net cash used in investing activities | (34,460) | (19,974) | (27,552) | (4,223) |
| Net cash provided by (used in) financing activities | 15,082 | (3,873) | 5,665 | 869 |
| Effect of exchange rate changes on cash, cash equivalents and restricted cash | 1,902 | 1 | (212) | (32) |
| Net increase in cash, cash equivalents and restricted cash | 18,491 | 4,612 | 2,101 | 323 |
| Cash, cash equivalents and restricted cash at beginning of the year | 11,336 | 29,827 | 34,439 | 5,278 |
| Cash, cash equivalents and restricted cash at end of the year | 29,827 | 34,439 | 36,540 | 5,601 |

SUMMARY

OUR SHAREHOLDING AND CORPORATE STRUCTURE

Our Major Shareholders and Relationship with Controlling Shareholders

As of the Latest Practicable Date, Mr. Robin Yanhong Li, our chairman and chief executive officer, is interested in and controls through: (i) 3,013,200 Class A Ordinary Shares directly held by Mr. Robin Yanhong Li on record, (ii) 2,232,000 Class A ordinary shares in the form of ADSs held by Mr. Robin Yanhong Li in the brokerage account of the administrator of the issuer’s employee stock option program, (iii) 342,320 Class A Ordinary Shares issuable to Mr. Robin Yanhong Li upon exercise of options within 60 days after the Latest Practicable Date, (iv) 14,560 Class A Ordinary Shares issuable to Mr. Robin Yanhong Li upon vesting of restricted shares within 60 days after the Latest Practicable Date, (v) 439,200,000 Class B Ordinary Shares held on record by Handsome Reward Limited, a British Virgin Islands company wholly owned by Mr. Robin Yanhong Li, (vi) 5,772,720 Class A ordinary shares in the form of ADSs held by Handsome Reward Limited in the brokerage account of the administrator of the issuer’s employee stock option program, (vii) 6,916,480 Class A Ordinary Shares issuable to Handsome Reward Limited upon exercise of options within 60 days after the Latest Practicable Date. As of the Latest Practicable Date, Mr. Li holds approximately 57.0% of the voting rights in the Company through shares beneficially owned by him and capable of being exercised on resolutions in general meetings.

For further details, please see “Major Shareholders” and “Relationship with the Controlling Shareholders.”

Weighted Voting Rights Structure and WVR Beneficiaries

Under our weighted voting rights structure, our share capital comprises Class A ordinary shares and Class B ordinary shares. Each Class A ordinary share entitles the holder to exercise one vote, and each Class B ordinary share entitles the holder to exercise 10 votes, respectively, on all matters subject to the vote at general meetings of the Company. For further details, please see “Share Capital—Weighted Voting Rights Structure.”

Pursuant to the Articles, the directors of our board may, from time to time subject to their fiduciary duties to act in the best interests of the Company and for a proper purpose, cause the Company to issue preferred shares and determine, among others, their conversion rights, which may include conversion to Class A and/or Class B ordinary shares. Such rights are subject to the approval and discretion of the board.

As we are seeking a listing as a Grandfathered Greater China Issuer pursuant to Chapter 19C of the Hong Kong Listing Rules (Secondary Listings of Qualifying Issuers) with a WVR structure, certain shareholder protection measures and governance safeguards under Chapter 8A of the Hong Kong Listing Rules (Weighted Voting Rights) do not apply to us pursuant to Rule 19C.12 and our Articles differ from Chapter 8A in a number of ways, including the following:

- Chapter 8A prohibits the increase in the proportion of shares with WVRs after the Listing and, where there is a reduction in the number of issued shares, requires shares with WVRs to be reduced proportionately. Our Articles do not contain such restrictions on the Class B ordinary shares;
- Our Articles do not provide for WVRs to terminate in the circumstances specified in Chapter 8A, such as where the WVR beneficiary is deceased or no longer a director. For more details of the circumstances in which weighted voting rights would be terminated, please see “Share Capital—Weighted Voting Rights Structure”;

SUMMARY

- Chapter 8A requires (a) amendments to a listed issuer’s constitutional documents, (b) variation of rights attached to any class of shares, (c) the appointment or removal of an independent non-executive director, (d) the appointment or removal of auditors and (e) the voluntary winding-up of a listed issuer to be subject to shareholder approval on a one vote per share basis. Our Articles do not contain such provisions;
- the charter of our corporate governance and nominating committee does not contain the terms otherwise required under Rule 8A.30 and Code Provision D.3.1 of Appendix 14 to the Hong Kong Listing Rules. For more details of the charter of our corporate governance committee, please see “Directors and Senior Management—Board Practices”; and
- the independent non-executive directors of a listed issuer with a WVR structure must be subject to retirement by rotation at least once every three years under Chapter 8A, whereas our Articles do not provide for a term of office for our directors.

Prospective [REDACTED] are advised to be aware of the potential risks of [REDACTED] in companies with a WVR structure, in particular that the interests of the WVR beneficiaries may not necessarily always be aligned with those of our Shareholders as a whole, and that the WVR beneficiaries will be in a position to exercise their higher voting power to influence the affairs of our Company and the outcome of shareholders’ resolutions, irrespective of how other shareholders vote. Prospective [REDACTED] should make the decision to [REDACTED] in the Company only after due and careful consideration. For further information about the risks associated with the WVR structure adopted by the Company, please refer to “Risk Factors—Risks Related to Our Corporate Structure.”

As a result, our Articles provide less shareholder protection and have fewer governance safeguards than if our Company were subject to Chapter 8A in its entirety.

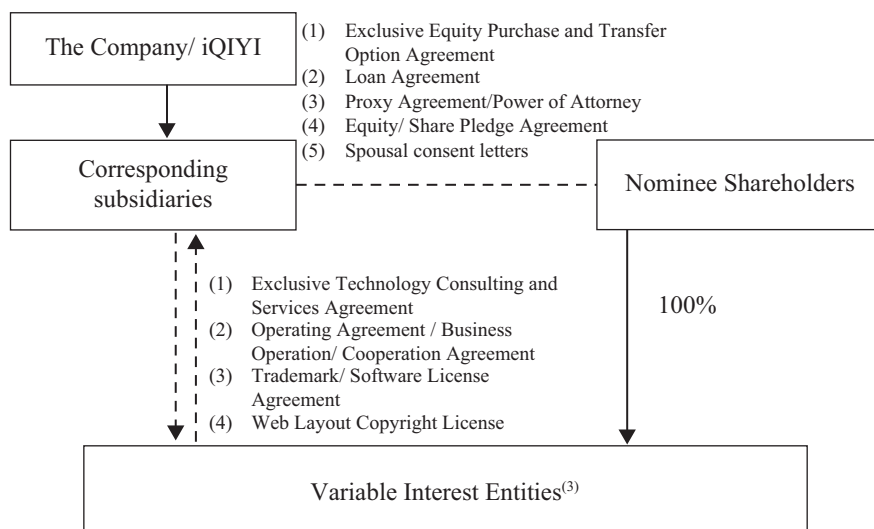
Our VIE Structure

Due to the PRC legal restrictions on foreign ownership in companies that provide value-added telecommunication-based online marketing services in China, we conduct our operations in China principally through Baidu Online and Beijing QIYI Century, our subsidiaries, and Baidu Netcom, Beijing Perusal and Beijing iQIYI, consolidated affiliated entities, which holds the material licenses and approvals necessary to operate our and iQIYI platforms and provide such services.

We have entered into certain contractual arrangements, as described in more detail in “History and Corporate Structure,” which collectively enable us to exercise effective control over Baidu Netcom, Beijing Perusal and Beijing iQIYI and realize substantially all of the economic benefits arising from them. We therefore include the financial results of these consolidated affiliated entities in our consolidated financial statements in accordance with U.S. GAAP as if they were our wholly-owned subsidiaries.

SUMMARY

The diagram below illustrates the general structure of the economic flow and control under the VIE structure created by the contractual arrangements described above:



Notes:

- (1) “→” denotes the direction of legal and beneficial ownership.
- (2) “...” denotes the contractual arrangements among the variable interest entities, their nominee shareholders, and corresponding subsidiaries (being Baidu Online and Beijing QIYI Century).
- (3) Baidu Netcom, Beijing Perusal and Beijing iQIYI.

LEGAL PROCEEDINGS

In April 2020, a short seller report was published by Wolfpack Research (the Wolfpack Report). In sum and substance, the Wolfpack Report alleges that iQIYI inflated its user numbers, inflated its revenue and deferred revenue in connection with certain parts of iQIYI’s business, inflated its expenses and the purchase prices of certain assets to conceal revenue inflation, and provided misleading financial statements of cash flows by adopting an incorrect accounting method. Following the publication of the Wolfpack Report, the SEC requested iQIYI to produce certain financial, operating, and other documents and records primarily relating to the allegations in the Wolfpack Report. In particular, the SEC requested that iQIYI voluntarily provides it with documents and information relating to, among other things, iQIYI’s organizational charts, accounting policies, and financial books and records from 2018 to the present, as well as documents relating to iQIYI’s acquisition or investments in certain entities mentioned in the Wolfpack Report and the valuation of those entities at the time of those transactions. On April 7, 2020, iQIYI publicly addressed the allegations contained in the Wolfpack Report in a press release on its website, noting that iQIYI “believes that the report contains numerous errors, unsubstantiated statements and misleading conclusions and interpretations regarding information relating to the Company.” iQIYI also reiterated that “it has always been and will remain committed to maintaining high standards of corporate governance and internal control, as well as transparent and timely disclosure in compliance with the applicable rules and regulations of the Securities and Exchange Commission and the Nasdaq Global Select Market.” On August 13, 2020, iQIYI issued another press release announcing its second quarter financial results, and also disclosed that the SEC’s Division of Enforcement is seeking the production of certain financial and operating records dating from January 1, 2018, as well as documents related to certain acquisitions and investments that were identified in a report issued the Wolfpack Report. In addition, iQIYI disclosed that shortly after the publication of the Wolfpack Report, iQIYI engaged professional advisers to conduct an internal review into certain of the key allegations in the Wolfpack Report and to report their findings to its audit committee. These professional advisers examined iQIYI’s books and records and

SUMMARY

undertook testing procedures that, in their judgment, were necessary and appropriate to evaluating the key allegations in the Wolfpack Report, including accounting policy analysis, data analytics on whether iQIYI manufactured orders and inflated revenues and/or expenses. On October 5, 2020, iQIYI publicly disclosed that the internal review within the agreed scope has been substantially completed and did not uncover any evidence that would substantiate the allegations. The SEC has also sought the production of certain documents and records from iQIYI related to such internal review and other related information. iQIYI is cooperating with the SEC’s investigation. iQIYI has voluntarily and publicly disclosed the SEC’s request for information, and, through its legal counsel, it has been providing the SEC with requested documents and information. As a matter of U.S. law, as confirmed by iQiyi’s U.S. legal counsel, the initiation of a request for information is not a finding of fact or an indication by the SEC or its enforcement staff that any violation of the federal securities laws has occurred. We understand that iQIYI intends to continue cooperating with the SEC if and when it receives further inquiries. We are unable to predict the timing, outcome, or consequences of the SEC investigation of iQIYI, or from the SEC’s review of the documents and records requested from iQIYI. Because the SEC has not charged iQIYI or any of its officers and directors with any wrongdoing, there is no factual basis to offer even aspeculative prognosis as to what the “worst case scenario” may be. As advised by iQIYI’s U.S. legal counsel, successful enforcement actions by the SEC (which can pursue only civil and administrative, not criminal, remedies) against other companies in the past have typically resulted in civil fines and disgorgement and other equitable remedies such as injunctions to refrain from further violations of law. However, there is no basis to conclude at this point whether there will be an enforcement action brought against iQIYI, whether any such action will be successful, or what the “worst case scenario” will be.

Furthermore, starting in April 2020, iQIYI and certain of its current and former officers and directors were named as defendants in four federal putative securities class actions alleging that they made material misstatements and omissions in documents filed with the SEC regarding certain of the key allegations contained in the Wolfpack Report. Starting in August 2020, we and certain of our current officers were named as defendants in two federal putative securities class actions alleging that defendants made material misstatements and omissions in documents filed with the SEC regarding certain of the key allegations contained in the Wolfpack Report. In the view of the Directors, which is based on Baidu’s and iQIYI’s U.S. legal counsel, in the event that a court finds that iQIYI, Baidu and/or other defendants violated any of these securities laws, or in the event that iQIYI, Baidu and/or other defendants choose to reach a settlement with plaintiffs, iQIYI and/or Baidu may be liable for civil monetary damages and the potential financial, operational and reputational impact on iQIYI and/or Baidu may be material. However, we cannot predict the timing, outcome or consequences of these class actions, and there is no basis to conclude at this point whether such actions will be successful or whether the Company will be subject to any damages, let alone how much. See “Business—Legal Proceedings.”

RISK FACTORS

Our business and the [REDACTED] involve certain risks and uncertainties, some of which are beyond our control and may affect your decision to [REDACTED] in us and/or the value of your [REDACTED]. See “Risk Factors” for details of our risk factors, which we strongly urge you to read in full before making an [REDACTED] in our Shares. Some of the major risks we face include:

- If we fail to retain existing customers or attract new customers for our online marketing services, our business, results of operations and growth prospects could be seriously harmed;
- Our business and results of operations could continue to be materially and adversely affected by the challenging macroeconomic environment impacting online marketing demand;

SUMMARY

- Our business depends on a strong brand, and if we are unable to maintain and enhance our brand, our business and results of operations may be harmed;
- We face risks associated with our investments and acquisitions, including our acquisition of YY Live;
- We face significant competition and may suffer from loss of users and customers as a result;
- If our expansions into new businesses are not successful, our future results of operations and growth prospects may be materially and adversely affected; and
- We have been and may again be subject to legal proceedings, claims and investigations in the ordinary course of business and could be adversely impacted by unfavorable results of legal proceedings and investigations.

USE OF [REDACTED]

We estimate that we will receive [REDACTED] from the [REDACTED] of approximately HK\$[REDACTED] billion after deducting estimated [REDACTED] fees and the estimated [REDACTED] payable by us and based upon an indicative [REDACTED] of HK\$[REDACTED] per [REDACTED] for both [REDACTED] and [REDACTED], and assuming the [REDACTED] is not exercised, or approximately HK\$[REDACTED] billion if the [REDACTED] is exercised in full.

The [REDACTED] in the [REDACTED] may be higher than, or the same as, the [REDACTED] in the [REDACTED]. See “Structure of the [REDACTED]—[REDACTED].”

We plan to use the [REDACTED] we will receive from the [REDACTED] for the following purposes:

- **approximately [REDACTED] (approximately HK\$[REDACTED], assuming that the [REDACTED] is not exercised) for continuing to invest in technology and enhance commercialization of our innovations centered around AI, including to:**
 - Attract and retain talents, in particular artificial intelligence and software engineers, data scientists, as well as other research and development staff, in order to improve our AI capabilities including but not limited to natural language processing, knowledge graph, speech recognition and synthesis, computer vision;
 - Strengthen the commercialization of AI cloud solutions and expand our portfolio of industry-specific AI cloud solutions by developing more AI capabilities, increasing cross-selling opportunities of various solutions to existing customers, acquiring new customers across industry verticals, and growing computing, storage, network, database and delivery capabilities;
 - Enhance the development and commercialization of intelligent driving and other growth initiatives, and continue to explore new and innovative application and monetization initiatives for our AI technology. For instance, we will continue to grow the accumulated test miles and improve simulation models with data from real world to increase the accuracy and effectiveness of our solutions to further enhance our L3 and L4 self-driving technology and to work with more automakers to power more passenger vehicles. We plan to invest in research and development of intelligent electric vehicles to achieve the mass production. We will also grow our fleet size of Apollo Robotaxi, obtain more driving licenses and expand geographic reach;

SUMMARY

- Invest in AI chips and scale IT infrastructure, including but not limited to investing more resources in chips design, procuring more servers and network equipment, and purchasing more cloud computing bandwidth, that collectively help optimize Baidu Brain and enhance our technology capabilities, as well as to improve the capacity of our operational flows and our external service capabilities; and
- Selectively pursue suitable strategic partnerships, alliances, acquisitions and investments that have synergies with our business, such as those leveraging our AI capabilities, and our large user base to complement our organic growth. As of the Latest Practicable Date, we have not identified any other target of potential acquisition.
- **approximately [REDACTED] (approximately [REDACTED], assuming that the [REDACTED] is not exercised) for further growing Baidu Mobile Ecosystem and enhancing and diversifying monetization, including to:**
 - Continue improving functionalities and features of our mobile ecosystem to enhance our user engagement. For example, we will continue to improve Baidu App functionalities, and enhance the three AI building blocks—Baijiahao (BJH) Accounts, Smart Mini Program and Managed Page to improve overall mobile ecosystem;
 - Continue investing in and purchasing more dynamic and diversified content and service offerings to build a closed-loop content and service ecosystem, and optimize the AI building blocks for third-party content by attracting more content and service providers and users, as well as acquiring more licensed content. We will incentivize and attract more premium content creators to create high-quality content at our platform in a variety of formats such as short video and live streaming, as well as enrich the comprehensiveness of the content library of our knowledge and information products, such as Baidu Wiki, Baidu Knows;
 - Further expand user reach through branding and marketing activities, such as conducting targeted and precise marketing and promotional campaigns driven by insights into user preferences in the form of app store advertisements and collaborations with targeted brand. We will also continuously invest in product development to launch more products and services to meet our users’ evolving needs; and
 - Further strengthen our vertical and community offerings to provide superior experience to users, merchants and content providers. We will continue to improve the effectiveness of our online marketing services with our AI technology, and plan to further diversify monetization channels of our mobile ecosystem. In addition to growing our mobile ecosystem organically, we also plan to selectively pursue suitable strategic partnerships, alliances, acquisitions and investments.
- **approximately [REDACTED] (approximately [REDACTED], assuming that the [REDACTED] is not exercised) for general corporate purposes.** We will use the remaining [REDACTED] for working capital and general corporate purposes to support our business operation and growth.

To the extent that the [REDACTED] of the [REDACTED] are not immediately required for the above purposes or if we are unable to put into effect any part of our plan as intended, we may hold such unused [REDACTED] in cash or short term deposits at authorized financial institutions and/or licensed banks.

SUMMARY

THE LISTING

Our ADSs have been listed and traded on Nasdaq since August 5, 2005. Dealings in our ADSs on Nasdaq are conducted in U.S. dollars. We have applied for a listing of our Class A ordinary shares on the Main Board under Chapter 19C (Secondary Listings of Qualifying Issuers). Dealings in our Class A ordinary shares on the Hong Kong Stock Exchange will be conducted in Hong Kong dollars. Our Class A ordinary shares will be traded on the Hong Kong Stock Exchange in [REDACTED] of [REDACTED] Class A ordinary shares. For additional information, see “Information about This Document and the [REDACTED].”

WAIVERS AND EXEMPTIONS

As we are applying for listing under Chapter 19C of the Hong Kong Listing Rules, we will not be subject to certain provisions of the Hong Kong Listing Rules, including, among others, rules on notifiable transactions, connected transactions, share option schemes, content of financial statements as well as certain other continuing obligations. In addition, in connection with the Listing, we have applied for a number of waivers and/or exemptions from strict compliance with the Hong Kong Listing Rules, the Companies (Winding Up and Miscellaneous Provisions) Ordinance and the SFO and a ruling under the Takeovers Codes. For additional information, see “Waivers and Exemptions.”

Among the various waivers that we have applied for, we have applied to the Hong Kong Stock Exchange for a waiver from strict compliance with the requirements in Paragraph 3(b) of Practice Note 15 to the Hong Kong Listing Rules such that we are able to spin off a subsidiary entity and list it on the Hong Kong Stock Exchange within three years of the Listing. While we do not have any specific plans with respect to the timing or details of any potential spin-off listing on the Hong Kong Stock Exchange as at the date of this document, in light of the Group’s overall business scale, we may consider spinning off one or more of our mature business units through a listing on the Hong Kong Stock Exchange within three years after the Listing, if there are clear commercial benefits both to the Company and the businesses to be potentially spun-off and there will be no adverse impact on the interests of shareholders of the Company. The waiver granted by the Hong Kong Stock Exchange is conditional upon us confirming to the Hong Kong Stock Exchange in advance of any spin-off that it would not render our Company, excluding the business to be spun off, incapable of fulfilling the eligibility or suitability requirements under Rules 19C.02 and 19C.05 of the Hong Kong Listing Rules based on the financial information of the entity to be spun off at the time of the Listing (calculated cumulatively where more than one entity is to be spun off). We cannot assure you that any spin-off will ultimately be consummated, whether within the three-year period after the Listing or otherwise, and any such spin-off will be subject to market conditions at the relevant time and approval by the Listing Committee of the Hong Kong Stock Exchange. In the event that we proceed with a spin-off, the Company’s interest in the entity to be spun off (and its corresponding contribution to the financial results of our Group) will be reduced accordingly.

We enjoy exemptions from certain obligations under U.S. securities laws and Nasdaq rules as a foreign private issuer as defined under the U.S. Exchange Act. [REDACTED]

ARTICLES OF ASSOCIATION

We are an exempted company incorporated in the Cayman Islands with limited liability and our affairs are governed by our Articles of Association, the Cayman Companies Act, as well as the common law

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of the Cayman Islands. The laws of Hong Kong differ in certain respects from the Cayman Companies Act, and our Articles of Association are specific to us and include certain provisions that may be different from common practices in Hong Kong.

As such, we have applied for, [and the Hong Kong Stock Exchange has granted us], among others, a waiver from strict compliance with:

(a) Rule 19C.07(3) of the Hong Kong Listing Rules, which requires that the appointment, removal and remuneration of auditors must be approved by a majority of a Qualifying Issuer’s members or other body that is independent of the issuer’s board of directors; and

(b) Rule 19C.07(7) of the Hong Kong Listing Rules, on the condition that:

- (i) we will convene an extraordinary general meeting of our Company by December 31, 2021 (the “**2021 EGM**”), for which at least 14 days’ notice will be given to our members, and put forth resolutions to revise the Articles, so that sub-Paragraphs (i) to (iv) below shall collectively be the “**Proposed Resolutions**”):
 - (i) we are required to convene an annual general meeting each year;
 - (ii) we are required to provide at least 14 days’ notice for any general meetings of the Company;
 - (iii) a member’s right to vote is subject to the requirements under the Hong Kong Listing Rules regarding circumstances requiring a member to abstain from voting to approve a matter under consideration; and
 - (iv) the minimum stake required to convene an extraordinary general meeting and add resolutions to a meeting agenda will be 10% of the voting rights, on a one vote per share basis, in the share capital of our Company;
- (ii) we will convene general meetings at the request of our Shareholders holding in aggregate not less than 10% of our Company’s voting rights, on a one vote per share basis, prior to the Proposed Resolutions being passed;
- (iii) we will provide 14 days’ notice for any general meetings after the Listing, prior to the Proposed Resolutions being passed;
- (iv) in the event that the Proposed Resolutions are not passed at the 2021 EGM, we will convene an annual general meeting each year with at least 14 days of notice beginning from 2022 and, for so long as we remain listed on the Hong Kong Stock Exchange, to continue to put forth the Proposed Resolutions (to the extent not yet passed) at each of the annual general meetings after the 2021 EGM, until the Proposed Resolutions are passed; and
- (v) we will obtain an irrevocable undertaking prior to the Listing from Mr. Robin Yanhong Li, Handsome Reward Limited and Ms. Melissa Ma, Mr. Robin Yanhong Li’s spouse, that they will use their voting rights to vote in favor of the Proposed Resolutions.

See “Risk Factors—Risks Related to our Shares, ADSs and the Listing—As a company applying for listing under Chapter 19C, we adopt different practices as to certain matters as compared with many other companies listed on the Hong Kong Stock Exchange.” See “Information about the Listing” and “Waivers and Exemptions—Shareholder Protection Requirements” for further details.

SUMMARY

[REDACTED]

SUMMARY

[REDACTED]

LISTING EXPENSES

We expect to incur listing expenses of up to approximately RMB[REDACTED] million (assuming that the [REDACTED] is conducted at the indicative [REDACTED] per [REDACTED] of HK\$[REDACTED] for both [REDACTED] and [REDACTED] and the [REDACTED] is not exercised). We expect to recognize RMB[REDACTED] million as general and administrative expenses in the fiscal year ending December 31, 2021 and RMB[REDACTED] million as a deduction in equity directly.

NO MATERIAL ADVERSE CHANGE

Our Directors confirm that, as of the date of this document, except as disclosed in “—Impact of COVID-19 on Our Operations” and elsewhere in this document, there has been no material adverse change in our financial or trading position or prospects since December 31, 2020 and there has been no event since December 31, 2020 which would materially affect the information shown in our consolidated financial statements included in the Accountants’ Report in Appendix IA to this document.

RECENT DEVELOPMENT AND IMPACT OF COVID-19

There have been certain business updates since the end of the Track Record Period, and our results of operations have been, and could continue to be adversely, and may be materially, affected, to the extent that the COVID-19 or any other epidemic harms the Chinese and global economy in general. For a detailed discussion of business updates and the impact of COVID-19 on our operations after the Track Record Period, please refer to “Recent Developments.”

RECENT DEVELOPMENTS

Business Updates

On November 16, 2020, Baidu (Hong Kong) Limited, our wholly-owned subsidiary, entered into a share purchase agreement with JOYY Inc. and certain of its affiliates, which are collectively referred to as JOYY, and subsequently amended the share purchase agreement on February 7, 2021. Pursuant to the agreement, we agreed to acquire JOYY’s domestic video-based entertainment live streaming business in China, which is referred to as YY Live, for an aggregate purchase price of approximately US\$3.6 billion in cash, subject to certain adjustments. Approximately US\$2.0 billion of the purchase price would be payable to JOYY at the closing of the acquisition, subject to certain adjustments. After the closing, subject to certain conditions and adjustments, approximately US\$1.0 billion would be payable no later than the later of the closing and April 30, 2021, and approximately US\$300 million would be payable no later than the later of the closing and June 30, 2021 and a maximum amount of US\$300 million would be payable subject to the achievement of certain conditions. The closing is subject to certain conditions, including, among others, there not having been any material adverse effect on YY Live, the financial statements of YY Live fairly representing its results of operations in all material respects, obtaining necessary regulatory approvals from governmental authorities, JOYY completing certain restructuring steps in relation to YY Live, and JOYY entering into a non-compete undertaking, pursuant to which JOYY would agree to not compete with us in certain areas of YY Live for a term of ten years. The share purchase agreement is subject to termination if the closing does not occur within a specified period of time. We have paid an aggregate of US\$1.9 billion, after considering working capital adjustment of US\$0.1 billion, to JOYY and its designated escrow account, and deposited an aggregate of US\$1.6 billion into several escrow accounts, in accordance with the terms and schedule set forth in the share repurchase agreement, with certain customary matters remaining to be completed in the near future.

On November 18, 2020, Muddy Waters issued a short seller report containing certain allegations against JOYY, including YY Live business. The short seller report alleged that JOYY’s, including YY Live’s, revenue appears fraudulent, and JOYY committed fraud through methods such as using paying user bots from JOYY’s own servers, and colluding with top performers and large channel owners recycling the gifts back into the system. Based on public records, JOYY and certain of its current and former officers and directors were named as defendants in a federal putative securities class action filed in November 2020 alleging that they made material misstatements and omissions in documents filed with the SEC regarding certain of the allegations contained in the Muddy Waters short seller report. We conducted financial, legal and commercial due diligence both prior to the execution of the share purchase agreement in relation to the acquisition, and after the release of Muddy Waters short seller report in relation to JOYY. In addition, we further negotiated with JOYY and entered into the amended and restated share purchase agreement on February 7, 2021, modifying certain terms and conditions in the original share purchase agreement. On February 8, 2021, JOYY publicly disclosed that its audit committee conducted an independent review of the allegations raised in the report related to the YY Live business, with the assistance of independent counsel, working with a team of experienced forensic auditors and data analytics experts, and that the review concluded that the allegations raised and conclusions reached in the report about the YY Live business were not substantiated. We had also maintained frequent and substantive communications with JOYY and its independent professional advisers. In light of these and also taking into consideration the potential synergies that YY Live may bring to our own business, we believe that it is in the commercial interest of our Company to proceed to complete the transaction pursuant to the terms and conditions in the amended and restated share purchase agreement. The acquisition has been substantially completed, with certain customary matters remaining to be completed in the near future. We are currently unable to predict the possible or further consequence that may arise from or relate in any way to the allegations contained in the Muddy Waters short seller report. There might be other class actions or

RECENT DEVELOPMENTS

regulatory enforcement actions in connection with such allegations. Any adverse outcome as a result of the short seller report, or any class action or regulatory enforcement action in connection thereof, could have a material adverse effect on YY Live’s business, financial condition, results of operation, cash flows, and reputation, and we may record impairment charges or write-offs of intangible assets and goodwill in connection with the acquisition in the future. For more information on related risk, see “Risk Factors—Risks Related to Our Business and Industry—We face risks associated with our acquisition of YY Live and its online live streaming business.”

In relation to YY Live, the Joint Sponsors with the assistance of counsels, have conducted relevant due diligence work, including but not limited to, (i) reviewing the summary of the key findings of the independent review of the allegations led by the audit committee of JOYY; (ii) interviewing the industry consultant of the Company, to understand the general practice of China’s livestreaming industry; and (iii) discussing with the senior management team of JOYY and YY Live, and the management of the Company, to understand the views of them on the acquisition of YY Live, the business of YY Live, and the MW Report, as applicable.

Having considered the due diligence work conducted by the Company, and the independent due diligence conducted by the Joint Sponsors, nothing material has come to the Joint Sponsors’ attention that the due diligence work conducted by the Company to be insufficient or unreasonable, and to disagree with the Directors’ assessment and view in relation to YY Live and the allegations contained in the MW Report which conclude that it is in the interest of the Company to proceed with the acquisition of YY Live.

YY Live is a video-based live streaming platform in China offering content such as music and dance shows, talk shows, outdoor activities, sports and anime. Users of YY Live may enjoy the live streaming services on YY Live platform through YY mobile app, YY.com website and PC YY. Users access content on the platform free of charge, but are charged for purchases of virtual items. YY Live generates revenue from the sales of in-channel virtual items used on its platform as tips for live streaming hosts.

We expect YY Live to bring synergies to our Mobile Ecosystem, which currently offers various knowledge-and-information-centric products and services, and diversify our monetization capabilities and revenue streams. We may be subject to a variety of risks associated with the online live streaming business of YY Live. See “Risk Factors—Risks Related to Our Business and Industry—We face risks associated with our acquisition of YY Live and its online live streaming business.” YY Live’s net revenues amounted to RMB10,272.7 million, RMB10,962.5 million and RMB9,950.3 million (US\$1,524.9 million), respectively. YY Live’s net income amounted to RMB3,288.6 million, RMB3,700.7 million and RMB3,141.3 million (US\$481.4 million) in the years ended December 31, 2018, 2019 and 2020, respectively. As of December 31, 2020, YY Live had net liabilities of RMB766.8 million (US\$117.5 million). For the year ended December 31, 2020, YY Live’s total net revenues, gross profit and net income accounted for 9.3%, 8.9% and 16.5% of our total net revenues, gross profit and net income, respectively. As of December 31, 2020, YY Live’s total assets accounted for 0.2% of our total assets. For more information, please refer to “Financial Information—Financial Information of YY Live” and Appendix IB—Accountant’s Report of YY Live.

Extraordinary General Meeting of Shareholders to Approve Share Subdivision

[The Company held an extraordinary general meeting of shareholders on March 1, 2021. A proposal of changing the Company’s authorized share capital by one-to-eighty subdivision of shares was submitted to the Company’s shareholders to be considered and voted upon at the meeting. The Company’s board

RECENT DEVELOPMENTS

of directors approved a change in the ADS ratio proportionate to the Share Subdivision from ten (10) ADSs representing one (1) Class A ordinary share to one (1) ADS representing eight (8) Class A ordinary shares, which took effect on March 1, 2021].

Impact of COVID-19 on Our Operations

Our results of operations have been, and could continue to be adversely, and may be materially, affected, to the extent that the COVID-19 or any other epidemic harms the Chinese and global economy in general. Any potential impact to our results will depend on, to a large extent, future developments and new information that may emerge regarding the duration and severity of the COVID-19 and the actions taken by government authorities and other entities to contain the COVID-19 or treat its impact, almost all of which are beyond our control.

The potential downturn brought by and the duration of the COVID-19 pandemic may be difficult to assess or predict where actual effects will depend on many factors beyond our control. The extent to which the COVID-19 pandemic impacts our long-term results remains uncertain, and we are closely monitoring its impact on us. During the year ended December 31, 2020, our operations have been affected by the COVID-19 pandemic. Our online marketing revenues declined compared to the prior period mainly due to weakness in online advertising demand as our customers in certain industries are negatively impacted by COVID-19. We have also provided additional allowance for credit losses for accounts receivable and contract assets, recognized impairment charges on our long-term investments and content assets, and recorded loss from equity method investments in 2020, due to the impact of COVID-19 and other factors. In addition, increased market volatility has contributed to larger fluctuations in the valuation of our equity investments. There are still significant uncertainties of COVID-19’s future impact, and the extent of the impact will depend on a number of factors, including the duration and severity of COVID-19, possibility of new waves in China and other countries, the development and progress of distribution of COVID-19 vaccine and other medical treatment, the potential change in user behavior, especially on internet usage due to the prolonged impact of COVID-19, the actions taken by government authorities, particularly to contain the outbreak, stimulate the economy to improve business condition especially for SMEs, almost all of which are beyond our control. As a result, certain of our estimates and assumptions, including the allowance for credit losses, the valuation of certain debt and equity investments, long-term investments, content assets and long-lived assets subject to impairment assessments, require significant judgments and carry a higher degree of variabilities and volatilities that could result in material changes to our current estimates in future periods. See also “Risk Factors—Risks Related to Our Business and Industry—We face risks related to health epidemics, severe weather conditions and other outbreaks.”

Promulgation of the Guidelines to Anti-Monopoly in the Field of Internet Platforms

On February 7, 2021, the Anti-monopoly Commission of the State Council officially promulgated the Guidelines to Anti-Monopoly in the Field of Internet Platforms, or the Anti-Monopoly Guidelines for Internet Platforms. Pursuant to an official interpretation from the Anti-monopoly Commission of the State Council, the Anti-Monopoly Guidelines for Internet Platforms mainly covers five aspects, including general provisions, monopoly agreements, abusing market dominance, concentration of undertakings, and abusing of administrative powers eliminating or restricting competition. The Anti-Monopoly Guidelines for Internet Platforms prohibits certain monopolistic acts of internet platforms so as to protect market competition and safeguard interests of users and undertakings participating in internet platform economy, including without limitation, prohibiting platforms with dominant position from abusing their market dominance (such as discriminating customers in terms of pricing and other transactional conditions using big data and analytics, coercing counterparties into exclusivity

RECENT DEVELOPMENTS

arrangements, using technology means to block competitors’ interface, favorable positioning in search results of goods displays, using bundle services to sell services or products, compulsory collection of unnecessary user data). In addition, the Anti-Monopoly Guidelines for Internet Platforms also reinforces antitrust merger review for internet platform related transactions to safeguard market competition. As the Anti-Monopoly Guidelines for Internet Platforms was newly promulgated, we are uncertain to estimate its specific impact on our business, financial condition, results of operations and prospects. We cannot assure you that our business operations comply with such regulations and authorities’ requirements in all respects. If any non-compliance is raised by relevant authorities and determined against us, we may be subject to fines and other penalties.

We have received enquiry from the SAMR related to failure to file prior notification of concentrations of undertaking and the possibility of penalty. Relevant cases are still under investigation. We have been cooperating with SAMR and we keep written and oral correspondence with SAMR. In January 2021, we received one official case-filing notification in connection with one case, which required us to provide relevant materials and statements on whether the non-filing constitutes a failure to file prior notification of concentrations of undertaking. We have been cooperating with SAMR and providing the requested documents and information. Recently we received a notification from the SAMR contemplating the imposition of a fine of RMB500,000 in connection with this case. The SAMR will issue an official notice imposing the penalty if no objection was raised within three business days. We did not object to the penalty. We do not expect further penalty from the SAMR in connection with this case after we make full payment of the penalty. There can be no assurance that such enquiry can be resolved in a timely manner to the SAMR’s satisfaction, or that we will not be subject to more enquiries in the future. We may be subject to penalty in connection with any such enquiry, including certain fines up to RMB500,000 per case, and in extreme case being order to terminate the contemplated concentration, to dispose of our equity or asset within a prescribed period, to transfer our business within a prescribed time or to take any other necessary measures to return to the pre-concentration status. We may receive greater scrutiny and attention from regulators and more frequent and rigid investigation or review by regulators, which will increase our compliance costs and subject us to heightened risks and challenges. We may have to spend much more personnel cost and time to evaluate and manage these risks and challenges in connection with our products and services as well as our investments in our ordinary business course to avoid any failure to comply with these regulations. Any failure or perceived failure by us to comply with the enacted Anti-Monopoly Guidelines for Internet Platforms and other anti-monopoly laws and regulations may result in governmental investigations or enforcement actions, litigations or claims against us and could have an adverse effect on our business, financial condition and results of operations. See also “Risk Factors—Risks Related to Doing Business in China—Any failure or perceived failure by us to comply with the enacted Anti-Monopoly Guidelines for Internet Platforms and other anti-monopoly laws and regulations may result in governmental investigations or enforcement actions, litigation or claims against us and could have an adverse effect on our business, financial condition and results of operations.”

DEFINITIONS

In this document, unless the context otherwise requires, the following terms shall have the meanings set out below.

| | |
|---|--|
| “Accountants’ Report” | accountants’ report for the years ended December 31, 2018, 2019 and 2020 in Appendix IA to this document |
| “ADS(s)” | American Depositary Shares (one ADS representing eight Class A ordinary shares) |
| “ADS Ratio Change” | the change in ADS ratio proportionate to the Share Subdivision from 10 ADSs representing one Class A ordinary share to one ADS representing eight Class A ordinary shares, effective on March 1, 2021 |
| “Articles” or “Articles of Association” | our Articles of Association (as amended from time to time), the current form of which was adopted on December 16, 2008, a summary of which is set out in Appendix III to this document |
| “Baidu Netcom” | Beijing Baidu Netcom Science Technology Co., Ltd. (北京百度網訊科技有限公司), a company established under the laws of the PRC on June 5, 2001, one of our variable interest entities and one of our Significant Subsidiaries |
| “Baidu Online” | Baidu Online Network Technology (Beijing) Co., Ltd. (百度在線網絡技術(北京)有限公司), a company established under the laws of the PRC on January 18, 2000, and one of our Significant Subsidiaries |
| “Beijing iQIYI” | Beijing iQIYI Science & Technology Co., Ltd. (北京愛奇藝科技有限公司), a company established under the laws of the PRC on March 27, 2007, one of our variable interest entities and one of our Significant Subsidiaries |
| “Beijing Perusal” | Beijing Perusal Technology Co., Ltd. (北京鼎鹿中原科技有限公司), a company established under the laws of the PRC on June 6, 2006, one of our variable interest entities and one of our Significant Subsidiaries |
| “Beijing QIYI Century” | Beijing QIYI Century Science & Technology Co., Ltd. (北京奇藝世紀科技有限公司), a company established under the laws of the PRC on March 8, 2010, one of our Significant Subsidiaries |
| “board” or “board of directors” | our board of directors |
| “business day” | any day (other than a Saturday, Sunday or public holiday) on which banks in Hong Kong or other relevant jurisdictions are generally open for business |
| “BVI” | British Virgin Islands |

DEFINITIONS

“Cayman Companies Act” or
“Companies Act”

the Companies Act, Cap.22 (Act 3 of 1961, as consolidated and revised) of the Cayman Islands, as amended or supplemented or otherwise modified from time to time

[REDACTED]

“China” or “the PRC”

the People’s Republic of China, excluding, for the purposes of this document only, Taiwan and the special administrative regions of Hong Kong and Macau, except where the context otherwise requires

“Class A ordinary shares”

Class A ordinary shares of the share capital of the Company with a par value of US\$[0.000000625] each, conferring a holder of a Class A ordinary share one vote per share on any resolution tabled at the Company’s general meeting

DEFINITIONS

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|---|---|
| “Class B ordinary shares” | Class B ordinary shares of the share capital of the Company with a par value of US\$[0.000000625] each, conferring weighted voting rights in the Company such that a holder of a Class B ordinary share is entitled to 10 votes per share on all matters subject to the vote at general meetings of the Company |
| “CNNIC” | China Internet Network Information Center (中國互聯網絡信息中心) |
| “Companies (Winding Up and Miscellaneous Provisions) Ordinance” | the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Chapter 32 of the Laws of Hong Kong), as amended or supplemented from time to time |
| “Companies Ordinance” | the Companies Ordinance (Chapter 622 of the Laws of Hong Kong), as amended or supplemented from time to time |
| “Company”, “our Company”, “we”, “our” or “us” | Baidu, Inc., a company incorporated in the Cayman Islands on January 18, 2000 as an exempted company and, where the context requires, its subsidiaries and consolidated affiliated entities from time to time |
| “connected person(s)” | has the meaning ascribed to it under the Hong Kong Listing Rules |
| “connected transaction(s)” | has the meaning ascribed to it under the Hong Kong Listing Rules |
| “Controlling Shareholder(s)” | has the meaning ascribed to it under the Hong Kong Listing Rules and unless the context otherwise requires, refers to Mr. Robin Yanhong Li and Handsome Reward Limited, which is wholly-owned and controlled by him and through which he holds interests in our Company, as set out in “Relationship with the Controlling Shareholders” |
| “CSRC” | the China Securities Regulatory Commission (中國證券監督管理委員會) |
| “Deposit Agreement” | the deposit agreement, dated as of August 10, 2005, as amended, among us, The Bank of New York Mellon and our ADS holders and beneficial owners from time to time |
| “director(s)” | member(s) of our board |
| “DTC” | The Depository Trust Company, the central book-entry clearing and settlement system for equity securities in the United States and the clearance system for our ADSs |
| “EIT” | enterprise income tax |

DEFINITIONS

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| “EIT Law” | the PRC Enterprise Income Tax Law (《中華人民共和國企業所得稅法》), promulgated on March 16, 2007 and further amended on February 24, 2017 and on December 29, 2018 |
| “Extreme Conditions” | any extreme conditions or events, the occurrence of which will cause interruption to the ordinary course of business operations in Hong Kong and/or that may affect the [REDACTED] or the [REDACTED] |
| “Foreign Investment Law” | the PRC Foreign Investment Law (《中華人民共和國外商投資法》), promulgated by the National People’s Congress in March 2019, which became effective on January 1, 2020 |
| “foreign private issuer” | as such term is defined in Rule 3b-4 under the U.S. Exchange Act [REDACTED] |
| “Group”, “our Group”, “the Group”, “we”, “us”, or “our” | our Company, subsidiaries and consolidated affiliated entities from time to time |
| “HK\$” or “Hong Kong dollars” or “HK dollars” | Hong Kong dollars, the lawful currency of Hong Kong [REDACTED] |
| “Hong Kong” or “HK” | the Hong Kong Special Administrative Region of the PRC |
| “Hong Kong Listing Rules” | the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, as amended or supplemented from time to time [REDACTED] |
| “Hong Kong Stock Exchange” | The Stock Exchange of Hong Kong Limited |

DEFINITIONS

[REDACTED]

“ICP(s)”

Internet content provider(s)

“iQIYI”

iQIYI, Inc. (formerly known as “Ding Xin, Inc.” and “Qiyi.com, Inc.”), a company incorporated in the Cayman Islands on November 27, 2009, and listed on Nasdaq under the symbol “IQ” and one of our Significant Subsidiaries

“independent third party(ies)”

person(s) or company(ies) and their respective ultimate beneficial owner(s), who/which, to the best of our directors’ knowledge, information and belief, having made all reasonable enquiries, is/are not connected with our Company

[REDACTED]

DEFINITIONS

[REDACTED]

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| “Joint Policy Statement” | the Joint Policy Statement Regarding the Listing of Overseas Companies jointly issued by the Hong Kong Stock Exchange and the SFC on September 27, 2013 and amended on April 30, 2018 |
| “Joint Sponsors” | the Joint Sponsors of the listing of the [REDACTED] on the Main Board of the Hong Kong Stock Exchange as named in “Directors and Parties Involved in the [REDACTED] ” |
| “Latest Practicable Date” | March 3, 2021, being the latest practicable date prior to the date of this document for the purpose of ascertaining certain information contained in this document |
| “Listing” | the listing we are seeking on the Hong Kong Stock Exchange under Chapter 19C and Chapter 8A of the Hong Kong Listing Rules |
| “Listing Committee” | the Listing Committee of the Hong Kong Stock Exchange |
| “Listing Date” | the date, expected to be on or about [REDACTED] , on which the Shares are listed on the Main Board of the Hong Kong Stock Exchange and from which dealings in the Shares are permitted to commence on the Main Board of the Hong Kong Stock Exchange |
| “M&A Regulations” | the Regulations on the Merger and Acquisitions of Domestic Enterprises by Foreign Investors (《關於外國投資者併購境內企業的規定》), jointly issued by MOFCOM, the State-owned Assets Supervision and Administration Commission, the State Taxation Administration, or the STA, CSRC, SAIC and SAFE on August 8, 2006, effective on September 8, 2006 and further amended on June 22, 2009 by the MOFCOM |
| “Main Board” | the stock market (excluding the option market) operated by the Hong Kong Stock Exchange which is independent from and operated in parallel with the Growth Enterprise Market of the Hong Kong Stock Exchange |
| “Memorandum” or “Memorandum of Association” | our memorandum of association (as amended from time to time), the current form of which was adopted on December 16, 2008, a summary of which is set out in Appendix III to this document |

DEFINITIONS

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| “MIIT” | the Ministry of Industry and Information Technology of the PRC (中華人民共和國工業和信息化部) |
| “MOF” | Ministry of Finance of the PRC (中華人民共和國財政部) |
| “MOFCOM” | Ministry of Commerce of the PRC (中華人民共和國商務部) |
| “Nasdaq” | Nasdaq Global Select Market |
| “NDRC” | National Development and Reform Commission of the PRC (中華人民共和國國家發展和改革委員會) |
| “Negative List” | the Special Administrative Measures (Negative List) for Foreign Investment Access, most recently jointly promulgated by the MOFCOM and the NDRC on June 23, 2020 and which became effective on July 23, 2020, as amended, supplemented or otherwise modified from time to time. |
| “NYSE” | New York Stock Exchange |
| | [REDACTED] |
| “PRC Company Law” | the Company Law of the PRC (《中華人民共和國公司法》), enacted by the Standing Committee of the Eighth National People’s Congress on December 29, 1993 and effective on July 1, 1994, and subsequently amended on December 25, 1999, August 28, 2004, October 27, 2005, December 28, 2013 and October 26, 2018, as amended, supplemented or otherwise modified from time to time |
| “PRC Legal Adviser” | King & Wood Mallesons, our legal adviser as to the laws of the PRC |

[REDACTED]

DEFINITIONS

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|-----------------------------|---|
| | [REDACTED] |
| “Principal Share Registrar” | Maples Fund Services (Cayman) Limited |
| | [REDACTED] |
| “Qualifying Issuer” | has the meaning given to it under Chapter 19C of the Hong Kong Listing Rules |
| “Regulation S” | Regulation S under the U.S. Securities Act |
| “Relevant Persons” | the Joint Sponsors, the [REDACTED] , the [REDACTED] , the [REDACTED] , the [REDACTED] , any of their or the Company’s respective directors, officers, employees, partners, agents, advisers and any other parties involved in the [REDACTED] |
| “RMB” or “Renminbi” | Renminbi, the lawful currency of the PRC |
| “RSU(s)” | restricted share unit(s) |
| “SAFE” | State Administration of Foreign Exchange of the PRC (中華人民共和國國家外匯管理局), the PRC governmental agency responsible for matters relating to foreign exchange administration, including local branches, when applicable |
| “SAFE Circular 37” | the Circular on Relevant Issues Concerning Foreign Exchange Control on Domestic Residents’ Offshore Investment and Financing and Roundtrip Investment through Special Purpose Vehicles (《國家外匯管理局關於境內居民通過特殊目的公司境外投融資及返程投資外匯管理有關問題的通知》) promulgated by SAFE with effect from July 4, 2014 |
| “SAIC” | State Administration for Industry and Commerce of the PRC (中華人民共和國國家工商行政管理總局), currently known as SAMR |
| “SAMR” | the PRC State Administration for Market Regulation (中華人民共和國國家市場監督管理總局), formerly known as the SAIC |

DEFINITIONS

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| “SAT Circular 82” | the Notice Regarding the Determination of Chinese-Controlled Offshore-Incorporated Enterprises as PRC Tax Resident Enterprises on the basis of de facto management bodies (《關於境外註冊中資控股企業依據實際管理機構標準認定為居民企業有關問題的通知》), issued on April 22, 2009 and further amended on December 29, 2017 |
| “SEC” | the United States Securities and Exchange Commission |
| “SFC” | the Securities and Futures Commission of Hong Kong |
| “SFO” or “Securities and Futures Ordinance” | the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong), as amended or supplemented from time to time |
| “Share(s)” | the Class A ordinary shares and Class B ordinary shares in the share capital of the Company, as the context so requires |
| “Share Incentive Plans” | the 2008 Share Incentive Plan and the 2018 Share Incentive Plan, details of which are set out in “Directors and Senior Management — Compensation” |
| “Share Subdivision” | the subdivision of each share of the Company classified as Class A ordinary shares, Class B ordinary shares and preferred shares of a par value of US\$0.00005 each in the share capital of the Company (including authorized issued and unissued class A ordinary shares, class B ordinary shares and preferred shares) into 80 shares with a par value of US\$0.00000625 each, effective on March 1, 2021, such that, following such subdivision, the authorized share capital of the Company became US\$43,520 divided into 66,000,000,000 Class A ordinary shares with a par value of US\$0.00000625 each, 2,832,000,000 Class B ordinary shares with a par value of US\$0.00000625 each and 800,000,000 preferred shares with a par value of US\$0.00000625 each |
| “shareholder(s)” | holder(s) of Shares and, where the context requires, ADSs |
| “Significant Subsidiaries” | our subsidiaries and consolidated affiliated entities as identified in “History and Corporate Structure—Significant Subsidiaries” |
| | [REDACTED] |
| “subsidiaries” | has the meaning ascribed thereto in the Hong Kong Listing Rules |
| “Takeovers Codes” | the Codes on Takeovers and Mergers and Share Buy-backs issued by the SFC |

DEFINITIONS

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|---|--|
| “Track Record Period” | the three years ended December 31, 2018, 2019 and 2020 |
| “U.S.” or “United States” | the United States of America, its territories, its possessions and all areas subject to its jurisdiction |
| “U.S. Exchange Act” | the United States Securities Exchange Act of 1934, as amended, and the rules and regulations promulgated thereunder |
| “U.S. GAAP” | accounting principles generally accepted in the United States |
| “U.S. Securities Act” | the United States Securities Act of 1933, as amended, and the rules and regulations promulgated thereunder |
| | [REDACTED] |
| “US\$” or “U.S. dollars” | United States dollars, the lawful currency of the United States |
| “variable interest entities,” “VIE” or “VIEs” | our variable interest entities, the financial results of which are consolidated into our consolidated financial statements as if they were our subsidiaries |
| “VAT” | value-added tax; all amounts are exclusive of VAT in this document except where indicated otherwise |
| “VIE structure” or “Contractual Arrangements” | variable interest entity structure and, where the context requires, the agreements underlying the structure |
| “weighted voting right” or “WVR” | has the meaning ascribed to it under the Hong Kong Listing Rules |
| | [REDACTED] |
| “WVR beneficiaries” | has the meaning ascribed to it under the Hong Kong Listing Rules and unless the context otherwise requires, refers to the WVR beneficiaries set out in “Share Capital”, holding the Class B ordinary shares, which entitle them to weighted voting rights, details of which are set out in “Share Capital” |

DEFINITIONS

“WVR structure” has the meaning ascribed to it under the Hong Kong Listing Rules

“YY Live” the domestic video-based live streaming business of JOYY Inc. (Nasdaq:YY)

In this document, the terms “associate(s),” “close associate(s),” “controlling shareholder(s),” “core connected person(s)” and “substantial shareholder(s)” shall have the meanings given to such terms in the Hong Kong Listing Rules, unless the context otherwise requires.

Unless otherwise expressly stated or the context otherwise requires, all data in this document is as of the date of this document.

The English names of PRC entities, PRC laws or regulations, and PRC governmental authorities referred to in this document are translations from their Chinese names and are for identification purposes. If there is any inconsistency, the Chinese names shall prevail.

Certain amounts and percentage figures included in this document have been subject to rounding adjustments. Accordingly, figures shown as totals in certain tables may not be an arithmetic aggregation of the figures preceding them.

GLOSSARY OF TECHNICAL TERMS

The following is a glossary of certain terms used in this document in connection with us and/or our business. As such, these terms and their meanings may not correspond to standard industry meanings or usage of these terms.

| | |
|--|--|
| “ADAS” | advanced driver-assistance systems, electronic systems developed to automate, adapt, and enhance vehicle systems for safety and better driving |
| “ACE” | autonomous driving, connected road, efficient mobility |
| “AI” | artificial intelligence, an area of computer science that focuses on mimicking human intelligence by machines |
| “AIoT” | artificial intelligence of things, a combination of AI technologies with IoT infrastructure making possible a network of AI-enabled appliances that can act autonomously or can be controlled through AI technologies such as voice recognition and hand gesture |
| “ANP” | autonomous navigation pilot, a system powered by computer vision-based autonomous driving technology enabling the automatic guidance of the vehicle to follow navigation route in highway, freeway and urban roads |
| “API” | application programming interfaces, a computing interface that defines interactions between multiple software intermediaries |
| “auto infotainment” or “in-vehicle infotainment” | a collection of hardware and software in automobiles that provides audio or video entertainment |
| “automated call center” | an integrated artificial intelligence solution that allows enterprises to manage communication with customers holistically |
| “autonomous driving test license” | a license issued by the relevant governmental authority permitting the conduct of testing of autonomous vehicles either with or without a human in the driver seat in designated areas |
| “AVP” | automated valet parking, a driverless system which finds a free space in the parking garage and parks the car itself by means of autonomous driving technology |
| “Baidu ML” | Baidu machine learning, a full-featured AI development platform for AI algorithm developers based on PaddlePaddle, which offer users a one-stop solution to complete data processing, model training and evaluation, and service deployment |

GLOSSARY OF TECHNICAL TERMS

| | |
|---------------------------------------|---|
| “convolutional neural network” | a class of deep neural networks, most commonly applied to analyzing visual imagery |
| “cost-per-click” or “CPC” | an online advertising pricing model, which is recorded according to the amount of click |
| “CRM” | customer relationship management |
| “DAU” | daily active user, the average number of mobile devices that launched our mobile apps at least once during a day within a specified period |
| “CAGR” | compound annual growth rate, the geometric progression ratio that provides a constant rate of return over the time period |
| “CDN” | content delivery network, geographically distributed network of proxy servers and their data centers |
| “computer vision” | an interdisciplinary scientific field that deals with how computers can gain high-level understanding from digital images or videos, in order to understand and automate tasks that the human visual system can do |
| “deep learning” or “DL” | a class of machine learning algorithms that uses multiple layers to extract higher-level features from the raw inputs |
| “display-based marketing” | graphic advertising on internet websites, apps or social media through banners or other formats made of texts, images, flash, video and audio |
| “DuerOS Skill” | a function developed through DuerOS open platform, which is capable of performing tasks similar to a mobile application |
| “EasyDL” | a no-code toolkit on PaddlePaddle that helps users without programming skills build customized machine learning models with a drag-and-drop interface |
| “EV” | electric vehicle |
| “GPU” | graphics processing unit |
| “IaaS” | infrastructure as a service, a form of cloud computing that provides virtualized computing resources over the internet |
| “IoT” | Internet of Things, the network of physical objects that are embedded with sensors, software, and other technologies for the purpose of connecting and exchanging data with other devices and systems over the Internet |

GLOSSARY OF TECHNICAL TERMS

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|-------------------------------|---|
| “iQIYI’s subscribing members” | individuals who purchased iQIYI’s monthly, quarterly or annual membership packages, including individuals with trial membership, and excluding individuals who pay for video on-demand services, sports paid content, online literature, comics and online games |
| “knowledge graph” | a knowledge base that uses a graph-structured data model to represent and store a collection of interlinked descriptions of entities, such as objects, events, situations and concepts, with free-form semantics |
| “L1” | level 1 of autonomous driving, or driver assistance, such as adaptive cruise control and lane keep assist to assist drivers but still require the driver to be in control |
| “L2” | level 2 of autonomous driving, or partial automation. Level 2 capabilities can assist drivers in controlling speed and steering, such as help with stop-and-go traffic by maintaining the distance between the driver’s vehicle and the vehicle in front, and providing steering assist by centering the vehicle within the lane, while still requiring drivers to have hands on the wheel and be ready to take control at any given moment |
| “L3” | level 3 of autonomous driving, or conditional automation. Level 3 capabilities allow vehicles to drive themselves, but only under ideal conditions and with limitations, such as limited-access divided highways at a certain speed and parking lots. Although hands are off the wheel, drivers are still required behind the wheel |
| “L4” | level 4 of autonomous driving, or high automation. Level 4 capabilities allow vehicles to drive themselves without human interactions but will be restricted to known use cases, or in most environments and road conditions |
| “L5” | level 5 of autonomous driving, or full automation. Level 5 capabilities allow vehicles to monitor and maneuver through all road conditions and require no human interventions whatsoever, eliminating the need for a steering wheel and pedals |
| “LiDAR” | light detection and ranging, a method for measuring distances by illuminating the target with laser light and measuring the reflection with a sensor |
| “MaaS” | mobility-as-a-service, a type of service that offers travelers mobility solutions based on their travel needs through a joint digital channel enables travelers to plan, book, and pay for multiple types of mobility services |

GLOSSARY OF TECHNICAL TERMS

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|---------------------|---|
| “MASS” | masked sequence to sequence, a novel pre-training method for sequence to sequence based language generation tasks, which randomly masks a sentence fragment in the encoder, and then predicts it in the decoder |
| “MAU” | monthly active user, the number of mobile devices that launched our mobile apps during a given month |
| “MCN” | multiple channel network, an organization that works with and assists content creators in areas such as content creation and monetization |
| “neural network” | a series of algorithms that endeavor to recognize underlying relationships in a set of data through a process that mimics the way the human brain operates |
| “NLP” | natural language processing, a branch of artificial intelligence that helps computers understand, interpret and manipulate human language |
| “OCR” | optical character recognition, the electronic or mechanical conversion of images of typed, handwritten or printed text into machine-encoded text |
| “OEM” | original equipment manufacturer, who manufactures products or components that are purchased by another company and retailed under that purchasing company’s brand name |
| “open source” | a source code that is made freely available for possible modification and redistribution |
| “P4P” | pay for performance |
| “PaaS” | platform as a service, a category of cloud computing services that provides a platform and environment to allow developers to build applications over the Internet |
| “PC” | personal computer |
| “POI” | point of interest |
| “PPC” | professionally produced content |
| “pre-trained model” | a model that was trained on a large benchmark data set to solve a problem similar to the one that one want to resolve |
| “Robobus” | a self-driving bus that does not require a driver at the steering wheel |
| “robotaxi” | a self-driving taxi that does not require a driver at the steering wheel |

GLOSSARY OF TECHNICAL TERMS

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|-------------------------------------|--|
| “robotaxi ride” | a complete trip provided to an individual rider of robotaxi services |
| “ROI” | return on investment |
| “SaaS” | software as a service, a cloud-based software licensing and delivery model in which software and associated data are centrally hosted |
| “SME” | small and medium enterprises |
| “Tera operations per second” | a common performance metric used for high-performance system on chips |
| “test mile” | a mile traveled by an autonomous vehicle |
| “TMT” | technology, media and telecommunications |
| “total addressable market” | the revenue opportunity available for a product or service |
| “V2X” | vehicle-to-everything, communication between a vehicle and any object, such as road, traffic lights and roadside signals that may affect, or may be affected by, the vehicle |

FORWARD-LOOKING STATEMENTS

Certain statements in this document are forward looking statements that are, by their nature, subject to significant risks and uncertainties. Any statements that express, or involve discussions as to, expectations, beliefs, plans, objectives, assumptions or future events or performance (often, but not always, through the use of words or phrases such as “will,” “expect,” “anticipate,” “estimate,” “believe,” “going forward,” “ought to,” “may,” “seek,” “should,” “intend,” “plan,” “projection,” “could,” “vision,” “goals,” “aim,” “aspire,” “objective,” “target,” “schedules” and “outlook”) are not historical facts, are forward-looking and may involve estimates and assumptions and are subject to risks (including but not limited to the risk factors detailed in this document), uncertainties and other factors some of which are beyond our Company’s control and which are difficult to predict. Accordingly, these factors could cause actual results or outcomes to differ materially from those expressed in the forward-looking statements.

Our forward-looking statements have been based on assumptions and factors concerning future events that may prove to be inaccurate. Those assumptions and factors are based on information currently available to us about the businesses that we operate. The risks, uncertainties and other factors, many of which are beyond our control, that could influence actual results include, but are not limited to:

- 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;
- competition for, among other things, capital, technology and skilled personnel;
- our ability to control costs;
- our ability to identify and conduct investments and acquisitions, as well as integrate acquired target(s);
- changes to regulatory and operating conditions in the industry and geographical markets in which we operate;
- our dividend policy; and
- all other risks and uncertainties described in “Risk Factors.”

Since actual results or outcomes could differ materially from those expressed in any forward-looking statements, we strongly caution **[REDACTED]** against placing undue reliance on any such forward-looking statements. Any forward-looking statement speaks only as of the date on which such statement is made, and, except as required by the Hong Kong Listing Rules, we undertake no 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. Statements of or references to our intentions or those of any of our Directors are made as of the date of this document. Any such intentions may change in light of future developments.

All forward-looking statements in this document are expressly qualified by reference to this cautionary statement.

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You should carefully consider all of the information set out in this document before making an [REDACTED] in the Shares, including the risks and uncertainties described below in respect of our business and our industry and the [REDACTED]. You should pay particular attention to the fact that we are a company incorporated in the Cayman Islands and that our principal operations are conducted in China and are governed by a legal and regulatory environment that in some respects differs from what prevails in other countries. Our business could be affected materially and adversely by any of these risks.

Risks Related to Our Business and Industry

If we fail to retain existing customers or attract new customers for our online marketing services, our business, results of operations and growth prospects could be seriously harmed.

We generate a substantial majority of our revenues from online marketing services, a substantial majority of which are derived from our pay-for-performance, or P4P, services. Our online marketing customers will not continue to do business with us if their investment does not generate sales leads and ultimately consumers, or if we do not deliver their web pages in an appropriate and effective manner. Our P4P customers may choose to discontinue their business with us, which are not subject to fixed-term contracts. In addition, third parties may develop and use certain technologies to block the display of our customers’ advertisements and other marketing products on our Baidu platform, which may in turn cause us to lose customers and adversely affect our results of operations. Furthermore, as our auction-based P4P services enable our customers to bid for priority placement of their paid sponsored links, we may lose customers if they find the bidding mechanism not cost effective or otherwise not attractive. Additionally, if our users do not increase their engagement on our platform, or our content ecosystem fails to offer rich and quality content that meets users’ tastes and preferences, or our users spend more time with or otherwise satisfy their content consumption demands on competing platforms, or we otherwise experience user traffic decline due to any reason, it would be difficult for us to attract new customers or retain existing customers. If our customers determine that their expenditures on our platform do not generate expected returns, they may allocate a portion or all of their advertising budgets to other advertising channels, such as television, outdoor media and other online marketing platforms, and reduce or discontinue business with us. Failure to retain our existing customers or attract new customers for our online marketing services could seriously harm our business, results of operations and growth prospects. We have recorded substantial customer deposits and deferred revenue, which mainly consist of deposits received from certain customers of our online marketing services. If we are unable to fulfill our obligation in respect of such customer deposits and deferred revenue, we may have to refund the balance to our customers and our cashflow and liquidity position would be materially adversely affected.

Since most of our customers are not bound by long-term contracts, they may amend or terminate advertising arrangements with us easily without incurring liabilities. Failure to retain existing customers or attract new ones to advertise on our platform may materially and adversely affect our business, financial condition, results of operations and prospects.

We have in the past removed, and may in the future again remove, questionable listings or advertisements to ensure the quality and reliability of our search results and/or information feed. Such removal, whether temporary or permanent, may cause affected customers to discontinue their business with us or negatively impact our relationships with affected Baidu Union partners. We also examine the relevant business licenses and bank accounts of prospective customers prior to business engagement, as a quality control measure. In addition, we have taken steps to implement measures

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requested by PRC regulatory authorities, such as modifying paid search practices and limiting the amount of displays. We have also proactively implemented numerous additional measures to deliver a better user experience and build a safer and more trustworthy platform for users. Such measures have had a negative impact on the number of customers and our revenues, although we believe such impact is likely to be temporary. PRC regulations on online marketing services are evolving, and uncertainties remain with respect to the implementation of and compliance with new regulations that may emerge, which in turn may have a material adverse impact on our business, results of operations and growth prospects.

Our business and results of operations could continue to be materially and adversely affected by the challenging macroeconomic environment impacting online marketing demand.

Online marketing services continue to be a primary source of our revenues, although we have seen declines in online marketing revenues during the Track Record Period, mainly due to the weakness in online advertising demand as our customers face challenging macroeconomic environment in their respective industries and in the general economy, including the significant adverse impact of the COVID-19 pandemic in 2020. Our business and results of operations could continue to be materially and adversely affected by the challenging macroeconomic environment and the general growth in online marketing through internet search or feed. While the internet has developed to a more advanced stage in China, customers have many channels to conduct online marketing and promotions. As users may not spend as much time on search-plus-newsfeed as they do on other types of internet platforms, many current and potential customers may not allocate as much of their marketing budgets to online marketing through search-plus-newsfeed, as compared to other methods of online marketing. Our ability to increase revenue and profitability from online marketing may be adversely impacted by a number of factors, many of which are beyond our control, including but not limited to:

- difficulties associated with developing and maintaining a larger user base with demographic characteristics attractive to online marketing customers and maintaining and increasing user engagement;
- increased competition and potential re-allocation of marketing budgets and downward pressure on online marketing prices, for example, resulting from an oversupply of advertising inventory released into the market;
- higher customer acquisition costs due in part to the limited experience of small to medium-sized enterprises, or SMEs, with the internet as a marketing channel or due to competition;
- decreased use of our search and paid click because search queries are increasingly being undertaken via voice-activated smart devices, apps, social media or other online platforms;
- growing reluctance of users to click on search results marked as advertisements;
- ineffectiveness of our online marketing delivery, tracking and reporting systems; and decreased use of internet or online marketing in China.

Our business depends on a strong brand, and if we are unable to maintain and enhance our brand, our business and results of operations may be harmed.

We believe that our brand “Baidu” has contributed significantly to the success of our business. We also believe that maintaining and enhancing the “Baidu” brand is critical to increasing the number of our users, customers, Baidu Union partners and content providers, as well as to expanding our developer communities and to attracting and retaining enterprise and public sector customers and partners. We have conducted various marketing and brand promotion activities, but we cannot assure you that these

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activities will achieve the brand promotion effect expected by us. If we fail to maintain and further promote the “Baidu” brand, or if we incur excessive expenses in this effort, our business and results of operations may be materially and adversely affected.

In addition, any negative publicity about our company, our products and services, our employees, our business practices, our search results or the platform to which our search results link, regardless of its veracity, could harm our brand image and in turn adversely affect our business and results of operations. We cannot assure you that we will be able to defuse negative publicity to the satisfaction of our investors, users, customers and business partners. From time to time, there has been negative publicity about our company and our business practice, which has adversely affected our public image and reputation during certain periods of intense negative publicity. For example, in 2018, Chinese media reported incidents where users had been defrauded by health care and logistics service providers that they found through search listings on Baidu. Also in 2018, an editorial falsely alleged that, unlike Google, Baidu was biased in displaying its feed content in its search results. This editorial attracted the attention of the general public and Chinese media, including state-owned news agencies, and adversely affected our public image. In 2019, Shenzhen Consumer Council received complaints from users who encountered false travel information provided by false travel agencies through search listings on Baidu. The negative publicity surrounding these incidents have resulted in significant adverse impact on our public image and reputation. Intense negative publicity may divert our management’s attention and may adversely impact our business. We cannot assure you that our brand, public image and reputation will not be materially and adversely affected in the future.

We face risks associated with our acquisition of YY Live and its online live streaming business.

Baidu (Hong Kong) Limited, our wholly-owned subsidiary, entered into definitive agreements with JOYY Inc. and certain of its affiliates, which are collectively referred to as JOYY, to acquire YY Live on November 16, 2020, and subsequently amended the share purchase agreement on February 7, 2021. The acquisition has been substantially completed, with certain customary matters remaining to be completed in the near future. On November 18, 2020, Muddy Waters issued a short seller report containing certain allegations against JOYY, including YY Live business. Based on public records, in November 2020, JOYY and certain of its current and former officers and directors were named as defendants in a federal putative securities class action alleging that they made material misstatements and omissions in documents filed with the SEC regarding certain of the allegations contained in the Muddy Waters short seller report. On February 8, 2021, JOYY publicly disclosed that its audit committee conducted an independent review of the allegations raised in the report related to the YY Live business, with the assistance of independent counsel, working with a team of experienced forensic auditors and data analytics experts, and that the review concluded that the allegations raised and conclusions reached in the report about the YY Live business were not substantiated. See “Recent Developments—Business Updates.” We are currently unable to predict the possible or further consequence that may arise from or relate in any way to the allegations contained in the Muddy Waters short seller report. There might be other class actions or regulatory enforcement actions in connection with such allegations. Any adverse outcome as a result of the short seller report, or any class action or regulatory enforcement action in connection thereof, could have a material adverse effect on YY Live’s business, financial condition, results of operation, cash flows, and reputation, and we may record impairment charges or write-offs of intangible assets and goodwill in connection with the acquisition in the future. Even if the allegations against JOYY may ultimately be proven to be groundless, we may have to allocate a portion of our resources to make assessment in relation to the short seller report and various matters provided for in the share purchase agreement. In the event that there is a dispute as to whether indemnification provision is triggered, we may need to utilize a

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significant portion of our resources and divert management’s attention from our day-to-day operations to resolve such disputes, including any litigation or other legal proceedings arising thereof.

There can be no assurance that the acquired YY Live will bring the anticipated benefits to us. We have relatively limited experience with operating the online live streaming business and we may not be able to successfully integrate YY Live into our existing business. We face uncertainties and challenges in navigating the complex regulatory environment, competing effectively in attracting and retaining users and hosts, and developing and/or upgrading products and services as well as technologies to meet everchanging user needs. If implemented ineffectively or if impacted by unforeseen negative economic or market conditions or other factors, we may not realize the full anticipated benefits of the acquisition of YY Live. Our failure to meet the challenges involved in realizing the anticipated benefits of the acquisition of YY Live could cause an interruption of, or a loss of momentum in, our activities and could adversely affect our results of operations. The acquisition and integration of the businesses may result in material unanticipated problems, expenses, liabilities, competitive responses and diversion of management’s attention, and we may record impairment charges or write-offs in connection therewith if the anticipated benefits of the acquisition fail to realize. We would be subject to and may not be able to successfully manage a variety of additional risks associated with respect to combining YY Live with us. These risks include, but are not limited to, the following:

- the online live streaming business is based on a relatively new business model in a relatively new market in which user demand may change or decrease substantially;
- challenges in the integration of operations and systems and in managing the expanded operations of a larger and more complex company;
- challenges in achieving anticipated business opportunities and growth prospects from combining the businesses of YY Live with the rest of our businesses;
- rules and measures governing online live streaming businesses and hosts are complex and evolving, and we may not be able to navigate such complex regulatory environment or to respond to future changes in regulatory environment in an effective and timely manner;
- we may face significant risks related to the content and communications on YY Live, as a majority of the communications on YY Live are conducted in real time, and we are unable to verify the sources of all information posted thereon or examine the content generated by users before it is posted;
- the revenue model for online live streaming may not remain effective, and we may not be able to retain existing users, attract new users, keep users engaged and attract more paying users;
- we may not be able to retain or attract popular talents such as performers, channel managers, professional game players, commentators and hosts for our live streaming platform or these talents may fail to draw fans or participants; and
- unanticipated additional costs and expenses resulting from integrating into our business additional personnel, operations, products, services, technology, internal controls and financial reporting responsibilities.

We face significant competition and may suffer from loss of users and customers as a result.

We face significant competition in almost every aspect of our business. For Baidu Core business, our primary competitors are mainly internet companies, online marketing platforms in China and other search engines. We compete with these entities for both users and customers on the basis of user traffic, cyber security quality (relevance) of search (and other marketing and advertising) results,

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availability and user experience products and services, distribution channels and the number of associated third-party websites. iQIYI competes with Tencent Video and Youku for both users and advertising customers. iQIYI also competes with other internet media and entertainment services, such as internet and social platforms and short-form video platforms, as well as major TV stations. iQIYI competes with these market players primarily on the basis of obtaining IP rights to popular content, conducting brand promotions and other marketing activities, and making investments in and acquisitions of business partners. See “Business—Competition.” Some of our competitors have significant financial resources, long operating histories and are experienced in attracting and retaining their users, accommodating their users’ habits and preferences and managing customers. They may use their experience and resources to compete with us in a variety of ways, including competing for users and their time, customers, third-party agents, content, strategic partners and networks of third-party websites/wapsites, investing more heavily in research and development and making investments and acquisitions. Our business environment is rapidly evolving and competitive. Our business faces changing technologies, shifting user needs, and frequent introductions of rival products and services. Some of our competitors in the search sector may have innovative business models, extensive distribution network or proprietary content or technologies that may provide users with better user experience and customers with better services. They may use their resources in ways that could affect our competitive position, including developing new products, making acquisitions, continuing to invest heavily in research and development and in talent, and continuing to compete aggressively for users, advertisers, customers, and the acquisition of traffic and content. If any of our competitors provides comparable or better Chinese language search and feed experience or internet video services, our user traffic could decline significantly. Additionally, if the channels and properties that we use to distribute services or products to our users and customers are no longer available to us, we may experience a decline in user traffic. Any such decline in traffic could weaken our brand and result in loss of users and customers, which could have a material and adverse effect on our results of operations.

There are vertical service providers in the forms of mobile apps and/or websites that allow users to search within their closed ecosystems. These players often purchase traffic from search engines and try to retain their users by offering comprehensive services on their platforms. As these vertical service providers expand, though they will continue to acquire traffic from search engines, their reliance on search engines may decline, especially if they can consolidate their industry verticals.

We also face competition from other types of advertising media, including traditional advertising media, such as newspapers, magazines, yellow pages, billboards, other forms of outdoor media, television and radio, mobile apps, webcasting and online video. Large companies in China generally allocate, and may continue to allocate, a limited portion of their budgets to online marketing, as opposed to traditional advertising and other forms of advertising media. If these companies do not devote a larger portion of their marketing budgets to online marketing services provided by us, or if our existing customers reduce the amount they spend on online marketing, our results of operations and growth prospects could be adversely affected.

If our expansions into new businesses are not successful, our future results of operation and growth prospects may be materially and adversely affected.

As part of our growth strategy, we enter into new businesses from time to time to generate additional revenue streams and through our development of new business lines or strategic investments in or acquisitions of other businesses. Expansions into new businesses may present operating, marketing and compliance challenges that differ from those that we currently encounter.

We have invested significant resources in the research and development of artificial intelligence (AI) technology and have made significant progress in the commercialization of AI-enabled offerings,

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including in-app services, cloud services and solutions, intelligent driving services and solutions and smart devices and services. We plan to continue to invest capital and other resources into our AI-enabled business operations. However, AI technology is rapidly evolving with significant uncertainties, and we cannot assure you that our investment and exploration in AI technology and AI-enabled products and services will be successful. Our operating results may also suffer if our innovation is not responsive to the needs of our users, customers and partners, inappropriately timed with market opportunities, or marketed ineffectively. For example, we have limited experience with operating and scaling AI-enabled business, including cloud services and solutions, intelligent driving services and solutions and smart devices and services, which could subject us to various challenges and risks, including developing and managing relationships with enterprises and public sector customers and partners, who are likely to have different needs and preferences from our existing customers, users and partners, highly competitive procurement processes, instances of corrupt practices or other illegal gains, longer receivable payment cycles and lower collection rates. We also may not alter our business practices in time to avoid or reduce adverse effects from any of the foregoing risks. In addition, our AI-enabled business requires very different products and services, sales and marketing channels and internal operational systems and processes. These requirements could disrupt our current operations and harm our financial condition and operating results, especially during the initial stage of investment, development and scaling of our new AI-enabled offerings.

We may also enter into other markets and industries/industry verticals that are new to us through organic business initiatives or investment and acquisitions, such as live streaming, e-commerce and healthcare vertical including internet hospital, which may subject us to different and unforeseen risks. However, we cannot assure you that such efforts will be successful. For these new markets and industries/industry verticals, we may not have sufficient experience and may not be able to navigate the rapidly evolving regulatory environment or forecast and meet the continually changing demands and preferences for products and services. Some of these new markets and industries/industry verticals are emerging with relatively novel and untested business models. Any of the foregoing could pose significant challenges to us. We may not realize the anticipated benefits of our investments or acquisitions, due to the uncertainties related to the performance and valuation of the relevant targets, or failure to integrate the targets into our existing business, or difficulty in operating the acquired business with our existing expertise and resources. See also “—Our strategy of investments and acquiring complementary businesses and assets may fail.”

It is uncertain whether our strategies will attract users and customers or generate the revenue required to succeed. If we fail to generate sufficient usage of our new products and services, we may not grow revenue in line with the significant resources we invest in these new businesses. This may negatively impact gross margins and operating income. Commercial success of our expansion into new business areas depends on many factors, including innovativeness, competitiveness, effectiveness of distribution and marketing, and pricing and investments strategies, especially in the early stage of competition for market share. For example, the smart transportation industry is highly competitive and fragmented. Our current and potential competitors in this industry range from large and established technology companies to emerging start-ups. Some competitors have longer operating histories in the sector. They can use their experience, resources and network in ways that could affect our competitive position, including making acquisitions, continuing to invest heavily in research and development and in talents, aggressively initiating intellectual property claims (whether or not meritorious), and continuing to compete aggressively for customers, partners and investees. Our competitors may be able to innovate and provide products and services faster than we can or may foresee product-and-service needs before us. As a result, we may not achieve significant revenue from our new business areas, such as our AI-enabled business operations, for several years, or at all, and may incur significant losses during the process and fail to recoup our investments. On the other hand, market conditions and general

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acceptance of products and services could be adversely impacted if other players in the market fail to adopt appropriate business and operational model, develop and offer successful products and services and develop and adapt appropriate technologies and infrastructure. If the markets of our new businesses, such as intelligent driving and electric vehicle, do not develop and grow as we anticipate, we may incur significant loss from our new businesses and our growth prospects may be materially adversely impacted.

In addition, we may encounter regulatory uncertainties related to new business areas that we enter into. The laws and regulations related to AI technology and products are at an early stage of development and still evolving in China. The effects of such laws and regulations remain unclear and may add uncertainties to the development and operation of our AI-related business. For example, as PRC regulatory framework on autonomous driving evolves, we may be required to comply with approval and other compliance requirements for autonomous driving road test and related data collection and sharing promulgated by PRC authorities from time to time. See “Regulations—Regulations on Artificial Intelligence and Autonomous Driving Vehicles.” We may confront other challenges as we enter new business domains, including the lack of adoption of new products and services, the lack of management talent in the new business, cost management and other factors required for the expansion of new businesses.

We have experienced slowdowns and declines in our revenues, and we may sustain net loss from time to time, and we may experience downward pressure on our operating and profit margins in the future.

Our total revenues grew at a compound annual growth rate of 11.0% from 2016 to 2020. Our growth was driven in part by the growth in China’s internet and online marketing industries, which may not be indicative of future growth or be sustainable. Our revenue growth slowed down in 2019, and declined in 2020 as compared to that of 2019, due to the decline in our online marketing services. We could continue to experience a decline in our revenues, as a result of a number of factors, including changes in the mix of products and services, customer demographics, industry and channel, changes in policy or policy implementation, increase in market competition for marketing and/or new AI offerings, and decrease in pricing arising from an oversupply of advertising inventory in the market, which has been witnessed since 2019. We may also experience a decline in our revenue or revenue growth rate, if there is a decrease in the rate of adoption for our products, services and technologies, or deceleration or decline in demand for platforms used to access our services, among other factors.

Our operating margin increased from 6% in 2019 to 13% in 2020. Net income attributable to us as a percentage of revenue changed from 2% in 2019 to 21% in 2020. We may experience downward pressure on our operating margin from increasing competition, revenue growth slower than expenses, and increased costs from many aspects of our business, including within online marketing where revenue growth does not keep up with traffic growth and related infrastructure costs to support our online properties, such as Baidu App, video-related and other products requiring huge data transmission and computing power. We may also pay increased fees for our distribution channels, as well as increased content acquisition costs to content providers. Additionally, an increase in personnel-related costs, an increase in spending to promote new products and services, the expiration of temporary tax exemptions or reductions, and the impact of the coronavirus (COVID-19), which has negatively affected our revenue growth and delayed certain spending, may dampen our operating margin. We may also experience downward pressure on our operating margin resulting from a variety of factors, such as the expansion of our business into new areas, including AI cloud, intelligent driving, voice assistant & smart device, all of which have margins much lower than that of online marketing. Our operating margin may also be negatively impacted from a greater proportion of revenue contributed by new business areas, which has grown faster than online marketing.

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In addition, we may also sustain net loss from time to time. We experienced significant losses from investment write downs in the third quarter of 2019, and experienced foreign currency fluctuation from time to time. We may experience further investment impairment and currency losses in the future. Declining operating margin and investment impairment have caused us to experience a net loss in 2019 and the first quarter of 2020, and there is no guarantee that we will be profitable in the future.

Due to these factors and the evolving nature of our business, our historical revenue growth rate, historical operating margin and historical profitability may not be indicative of our future performance.

If we fail to continue to innovate and provide products, services and high-quality internet experience that attract and retain users, we may not be able to generate sufficient user traffic to remain competitive; we may expend significant resources in order to remain competitive.

Our success depends on providing products and services to attract users and enable users to have a high-quality internet experience. In order to attract and retain users and compete against our competitors, we must continue to invest significant resources in research and development to enhance our artificial intelligence (AI) or other new technologies, improve our existing products and services, and introduce additional high-quality products and services. If we are unable to anticipate user preferences or industry changes, enhance the quality of our products and services on a timely basis or fail to provide sufficient content, or provide other consumer-facing services and products, including our maps and smart devices, to our users’ satisfaction, we may suffer a decline in the size of our user base. Our results of operations may also suffer if our innovations do not respond to the needs of our users, are not appropriately timed with market opportunities or are not effectively brought to market. As search, marketing and AI technologies and new forms of devices and apps continue to develop, we may expend significant resources in research and development and strategic investments and acquisitions in order to remain competitive.

If our content ecosystem fails to continually offer quality content in a cost effective manner, we may experience declines in user traffic and user engagement, our business and results of operations may be harmed.

Our content ecosystem consists of products developed for our partners, such as Baijiahao, Smart Mini Program, Managed Page and Union network, and internally developed content and services products, such as Baidu Knows, Baidu Wiki, Baidu Healthcare Wiki, Baidu Wenku, Baidu Scholar, Baidu Experience, Baidu Post, Haokan, Quanmin, iQIYI. The success of our content ecosystem depends on our ability to attract content creators and producers to contribute quality content to our platform by leveraging our user traffic and enhance user engagement through the provision of attractive content, so as to create a virtuous cycle. We have relied, and will continue to rely, on third parties for the majority of the content offered in our content ecosystem and some of our products include third party intellectual property. As the competition for quality content becomes increasingly intense in China, we cannot assure you that we will be able to manage our content acquisition costs effectively and generate sufficient revenues to outpace future increase in content spending. We may also be unable to renew some of our content or intellectual property licensing agreements upon their expiration or termination and any renewal of the content or intellectual property licensing agreements may involve higher costs or less favorable terms. If we are not able to license popular premium content on commercially reasonable terms or renew our content or intellectual property licensing agreements, our financial condition and results of operations may be materially and adversely affected. We have undertaken significant commitments of future minimum payments under non-cancellable agreements for produced content and licensed copyrights. If the content does not achieve anticipated popularity and commercial success, such commitments may not be recoverable. In addition, we rely on users to contribute content

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to our various products, including Baijiahao, Baidu Knows, Baidu Wiki, Baidu Healthcare Wiki, Baidu Experience, Baidu Post, Haokan, Quanmin, and iQIYI’s user generated content. If these parties fail to develop and maintain high-quality and engaging content, if our desired premium content becomes exclusive to our competitors, if we are unable to continue to grow our content offerings and stay competitive vis-à-vis other content platforms, or if a large number of our existing relationships are terminated, the attractiveness of our content offerings to users may be severely impaired. If we are unable to offer content that meets users’ tastes and preferences on a continuing basis, including continuously upgrading our content recommendation engines and in a cost effective manner, our user experience may deteriorate, we may suffer from reduced user traffic, our business and results of operations may be harmed.

We have been and may again be subject to legal proceedings, claims and investigations in the ordinary course of business and could be adversely impacted by unfavorable results of legal proceedings and investigations.

We are subject to various legal proceedings, claims and government investigations, penalties or actions that have arisen in the ordinary course of business and have not yet been fully resolved, and new legal proceedings, claims, regulatory investigations, penalties or actions 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. The existence of litigation, claims, governmental investigations and proceedings may harm our reputation, business and adversely affect the trading price of our securities. In 2020, our subsidiary iQIYI was subject to SEC investigation after the publication of a short seller report by Wolfpack Research making certain allegations against iQIYI (the “Wolfpack Report”). In sum and substance, the Wolfpack Report alleges that iQIYI inflated its user numbers, inflated its revenue and deferred revenue in connection with certain parts of iQIYI’s business, inflated its expenses and the purchase prices of certain assets to conceal revenue inflation, and provided misleading financial statements of cash flows by adopting an incorrect accounting method. Following the publication of the Wolfpack Report, the SEC requested iQIYI to produce certain financial, operating, and other documents and records primarily relate to the allegations in the Wolfpack Report. iQIYI has voluntarily and publicly disclosed the SEC’s request for information, and, through its legal counsel, it has been providing the SEC with requested documents and information. We are unable to predict the timing, outcome, or consequences of the SEC investigation of iQIYI, or from the SEC’s review of the documents and records requested from iQIYI. In the same year, iQIYI and certain of its current and former directors and officers were named as defendants in several federal punitive securities litigations. Also in 2020, we and certain of our current and former officers were named as defendants in three federal putative securities class actions, two of which are in regard to certain of the key allegations contained in the Wolfpack Report. In 2021, we and certain of our former officers were named as defendants in a separate federal putative securities class action alleging that our subsidiary, iQIYI, made false and misleading statements in its public disclosure documents in violation of federal securities laws. In the event that a court finds that iQIYI, Baidu and/or other defendants violated any of the applicable securities laws, or in the event that iQIYI, Baidu and/or other defendants choose to reach a settlement with plaintiffs, iQIYI and/or Baidu may be liable for civil monetary damages and the potential financial, operational and reputational impact on iQIYI and/or Baidu may be material. However, we cannot predict the timing, outcome or consequences of these class actions, and there is no basis to conclude at this point whether such actions will be successful or whether the Company will be subject to any damages, let alone how much. For more details, see “Business—Legal Proceedings.” Regardless of the merit of particular claims, legal proceedings, government investigations and proceedings may result in reputational harm, be expensive to respond, time consuming, disruptive to our operations and distracting to management. In the event we or iQIYI does not prevail or we or iQIYI enters into settlement arrangements in any of these proceedings or

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investigations, we or iQIYI may incur significant expenses which may materially adversely affect our results of operations.

The outcome of legal proceedings and investigations is inherently uncertain. If one or more legal matters were resolved against us or an indemnified third party in a reporting period for amounts in excess of management’s expectations, our financial condition and operating results for that reporting period could be materially adversely affected. Further, such an outcome could result in significant compensatory, punitive or trebled monetary damages, disgorgement of revenue or profits, remedial corporate measures or injunctive relief against us that could materially adversely affect our financial condition and operating results.

In addition to the content developed and posted on our platform by ourselves, our users may post information on Baidu Post, Baidu Knows, Baidu Wiki, Baidu Wenku and other sections of our platform, our content providers may provide content through Baijiahao platform and our P4P customers may create text-based descriptions, image descriptions and other phrases to be used as text, images or keywords in our search listings, and users can also use our personal cloud computing service to upload, store and share documents, images, audio and videos on our cloud servers. We have been and may continue to be subject to claims and investigations for intellectual property ownership and infringement, defamation, negligence or other legal theories based on the content found on our platform, the results in our paid search listings or our other products and services, which, with or without merit, may result in diversion of management attention and financial resources and negative publicity for our brand and reputation. In November 2018, an individual, together with his related company, filed a complaint alleging acts of defamation and libel, commercial disparagement, tortious inference with prospective business relations, intentional infliction of emotional distress and civil conspiracy against, among others, us and Robin Yanhong Li in his capacity as our chairman and chief executive officer, in the Supreme Court of New York. The complaint alleged, among other things, that the defendants published articles containing false and defamatory statements concerning the plaintiffs, and sought damages in an aggregate amount of US\$11 billion, including purported punitive damages of US\$10 billion. The defendants moved the complaint to the U.S. District Court for the Eastern District of New York and filed motions to dismiss the complaint. The plaintiff voluntarily dismissed that complaint, and then added us and Mr. Li as defendants to the Second State Court Lawsuit. We filed motions to dismiss that complaint, which were not opposed. The Plaintiff filed a notice of voluntary discontinuance of the complaint in the Second State Court Lawsuit, and subsequently filed a nearly identical complaint in the U.S. District Court for the Eastern District of New York. In January 2020, the U.S. District Court for the Eastern District of New York dismissed that complaint in its entirety with prejudice, and the time for plaintiff to appeal that dismissal has expired. In February 2020, the Supreme Court of New York granted defendants’ motions to discontinue the Second State Court Lawsuit with prejudice. No appeal of that order has been filed as of the date of this disclosure. We believe these claims to be without merit and intend to continue to defend ourselves vigorously. See “Business—Legal Proceedings.” Furthermore, if the content posted on our platform or found, stored or shared through our other products and services contains information that government authorities find objectionable, our platform or relevant products or services may be shut down and we may be subject to other penalties. See “—Risks Related to Doing Business in China—We may be subject to liability for information displayed on or linked to our websites, mobile apps, Smart Mini Program or Managed Page and negative publicity in international media and our business may be adversely affected as a result.”

We have been, and may again in the future be, subject to claims, investigations or negative publicity based on the results in our paid search listings. Claims have been filed against us after we allowed certain customers to register keywords containing trademarks, trade names or brand names owned by

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others and displayed links to such customers’ websites in our paid search listings. While we maintain a database of certain well-known trademarks and continually update our system algorithms and functions to guard against customers keywords containing the well-known trademarks that are owned by others, it is not possible for us to completely prevent our customers from bidding on keywords that contain trademarks, trade names or brand names owned by others. There has been negative publicity about fraudulent information in our paid search listings. Although we have been continually enhancing our technology, control and oversight to prevent fraudulent websites, web pages and information from appearing in our paid search listings, there is no guarantee that the measures we have taken are effective at all times. Claims, investigations and negative publicity based on the results in our paid search listings, regardless of their merit, may divert management attention, severely disrupt our operations, adversely affect our results of operations and harm our reputation.

If we fail to keep up with rapid changes in technologies and user behavior, our future success may be adversely affected.

Our future success will depend on our ability to respond to rapidly changing technologies, adapt our products and services to evolving industry standards and improve the performance and reliability of our products and services. Our failure to adapt to such changes could harm our business. In addition, changes in user behavior resulting from technological developments may also adversely affect us. For example, the number of people accessing the internet through mobile devices and internet of things, or IoTs, such as smartphones, tablets and smart (voice-activated internet) home devices, has increased in recent years, and we expect this trend to continue while 5G and more advanced mobile communications technologies are broadly implemented. If we fail to develop products and technologies that are compatible with all mobile devices, IoTs and operating systems, or if the products and services we develop are not widely accepted and used by users of various mobile devices and IoTs, our position in the mobile internet and AI sectors may be adversely affected. In addition, the widespread adoption of new internet, networking or telecommunications technologies or other technological changes could require substantial expenditures to modify or integrate our products, services or infrastructure. If we fail to keep up with rapid technological changes to remain competitive, or consequently fail to retain users with products and services of exceptional quality, our future success may be materially and adversely affected.

Our increasing focus on cloud-based services presents execution, competitive and compliance risks; Baidu Core’s revenue growth may be materially adversely affected by our ability to develop cloud-based services and generate sufficient usage of such services.

A growing part of our business involves cloud-based services available across a spectrum of computing devices. Our Baidu Core’s cloud services revenue was RMB9.2 billion (US\$1.4 billion) in 2020, increasing by 44% from 2019. We are devoting significant resources to provide AI solutions, cloud infrastructure, and other services to enterprises and individuals. At the same time, our competitors are rapidly developing and deploying their cloud-based solutions and services. Pricing and delivery models are evolving. Devices and form factors influence how users access services in the cloud and sometimes the user’s choice of which suite of cloud-based services to use. Our success in cloud-based services strategy will depend on the level of adoption of our products and services. We may not establish market share sufficient to achieve scale necessary to achieve our business objectives or recoup costs incurred to build and maintain infrastructure to support our cloud-based services. It is uncertain whether our strategies will attract the users or generate the revenue required to succeed. If we fail to generate sufficient usage of our new products and services, we may not grow revenue in line with the costs associated with infrastructure development and research and development investments. This may negatively and materially impact our results of operations and financial performance.

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The development of cloud-based services is accompanied by regulatory compliance risks. For example, regulatory authorities in China are increasing enforcement efforts against non-compliance relating to companies operating content delivery networks, internet data centers, and internet service providers. However, the interpretation and application of relevant laws in China and elsewhere are often uncertain and in flux, and any failure or perceived failure to comply with all applicable laws and regulations may result in legal proceedings or regulatory actions against us, and could have a material adverse effect on our business and results of operations.

In the past, our peers have experienced data security and infrastructure stability issues arising out of their cloud services. Our cloud services may also encounter similar issues, which could have a material and adverse impact on our brand, operations and financial performance.

Potential issues in the adoption and use of artificial intelligence in our product offerings may result in reputational harm or liability.

We are building AI into many of our product offerings and we expect this element of our business to be a driver for our future growth. We envision a future in which AI operates in our services and applications, such as search-plus-feed, cloud services and solutions, intelligent driving services and solutions and Xiaodu smart devices and services, and the cloud helps our customers become more productive. As with many disruptive innovations, AI presents risks and challenges that could affect its adoption, and, therefore, our business. Our products and services based on AI may not be adopted by our users or customers. AI algorithms may be flawed. Datasets may be insufficient or contain biased information. Inappropriate or controversial data practices by us or others could impair the acceptance of our AI solutions. These deficiencies could undermine the decisions, predictions, or analysis AI applications produce, subjecting us to legal liability, and brand or reputational harm. In addition, some AI scenarios present ethical issues. If we enable or offer AI solutions that are controversial because of their impact on human rights, privacy, employment, or other social issues, we may experience reputational harm or be exposed to liability.

We may face challenges in connection with developing, manufacturing and marketing new Xiaodu smart products in response to changing customer requirements, new technologies and market competition.

The market for our Xiaodu smart products is characterized by rapidly changing technology, evolving industry standards, short product life cycles, frequent new product introductions, continual improvement in product price and performance characteristics, and price and feature sensitivity on the part of consumers and businesses. As a result, we must continually introduce new products and technologies and enhance existing products in order to remain competitive.

The success of our Xiaodu smart products depends on several factors, including our ability to:

- anticipate technology and market trends;
- develop innovative new products and enhancements on a timely basis;
- distinguish our products from those of our competitors;
- manufacture and deliver high-quality products in sufficient volumes at competitive cost structure;
- establish strong, efficient online and offline distribution channels;
- price our products competitively;

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- develop a vibrant DuerOS skills store and a large developer community to increase user stickiness and loyalty; and
- innovate post-hardware sales monetization models.

If we are unable to develop, manufacture, market and introduce enhanced or new Xiaodu smart products in a timely manner in response to changing market conditions or customer requirements, including changing fashion trends and styles, it will materially adversely affect our business, revenue growth, financial condition and results of operations. Furthermore, as we develop new generations of products more quickly, we expect that the pace of product obsolescence will increase concurrently. The disposition of inventories of excess or obsolete products may result in reductions to our operating margins and materially and adversely affect our earnings and results of operations.

The success of our Xiaodu smart products depends on the continued growth of the smart device market, our ability to establish and maintain the brand, market share, and competition from other companies, as well as our ability to monetize through services after the initial hardware sale.

We have invested significant resources in the “Xiaodu” brand and the research and development of Xiaodu smart products. If the smart device market does not continue to grow or grow in unpredictable ways, or we fail to maintain and further promote the “Xiaodu” brand, our revenue may fall short of expectations and our operating results may be harmed. Also, we have previously offered, but have recently strategically ceased to offer, sales discounts on Xiaodu smart products. Offering such discounts, which has resulted in a loss on smart device hardware sales, has negatively affected, and will continue to negatively affect, our financial performance in the long term. We cannot assure you that our decision to offer or cease to offer such sales discounts is producing, or will produce, positive outcomes for our results of operations. The market for smart devices may not continue to grow; even if it does, we may not be successful in developing and selling devices that appeal to consumers or gain sufficient market acceptance, which typically takes longer in the smart device market. To succeed in this market, we will need to design, produce and sell innovative and compelling products and partner with other businesses that enable us to capitalize on new technologies, some of which have developed or may develop and sell smart devices of their own. We are currently exploring different business models with Xiaodu smart devices, and exploring different monetization model through services after hardware sales, such as membership, advertising and revenue sharing from distribution of third-party skills. Whether we will be able to achieve profitability in smart devices depends in part on our ability to generate revenue through services after the initial hardware sale at a level sufficient to cover associated operating expenses, but there can be no assurance that we will succeed in formulating and implementing the appropriate business and monetization model. Moreover, competition from other companies that seek to provide smart devices will adversely affect our profitability.

We face a number of manufacturing, supply chain, distribution channel and inventory risks as well as product quality and financing risks that, if not properly managed, could harm our financial condition, operating results, and prospects.

We rely on third parties to manufacture our Xiaodu smart products, to design certain of our components and parts, and to participate in the distribution of our products. Our business could be negatively affected if we are not able to engage these companies with the necessary capabilities or capacity on reasonable terms, or if those we engage fail to meet their obligations (whether due to financial difficulties or other reasons), or make adverse changes in the pricing or other material terms of our arrangements with them.

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We may experience supply shortages and price increases driven by a variety of factors, such as raw material availability, manufacturing capacity, labor shortages, tariffs, trade disputes and barriers, natural disasters, and significant changes in the financial or business condition of our suppliers. We may experience shortages or other supply chain disruptions that could negatively affect our operations. In addition, some of the components we use in our Xiaodu smart products are available only from a single source or limited sources, and we may not be able to find replacement vendors on favorable terms in the event of a supply chain disruption.

Our Xiaodu smart products may have quality issues resulting from design, manufacturing, or operations. Sometimes, these issues may be caused by components we purchase from other manufacturers or suppliers. If the quality of our Xiaodu smart products does not meet expectations or are defective, it could harm our reputation, financial condition, and operating results.

We are exposed to significant inventory risks that may adversely affect our operating results as a result of seasonality, new product launches, rapid changes in product cycles and pricing, defective merchandise, changes in consumer demand and consumer spending patterns, and other factors. We endeavor to accurately predict these trends and avoid overstocking or understocking issues. Demand for our Xiaodu smart products, however, can change significantly between the time inventory or components are ordered and the date of sale. We may misjudge customer demand, resulting in inventory buildup and possible significant 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.

Our Smart Living Group (SLG), which runs the DuerOS and Xiaodu operations, completed its first round of funding in 2020, and has historically experienced an operating loss. If SLG is unable to satisfy its cashflow needs by generating sufficient cash from its operations in the near future, it may need to rely on subsequent round(s) of financing. If SLG’s operating cashflow does not improve and if SLG fails to conduct financing on reasonable terms, it may not be able to continue its business operations, which may adversely impact our results of operations and financial performance.

Our now-divested financial services business may subject us to operational and reputational risks, which may have a material adverse effect on our business, results of operations and financial condition.

We have provided financial services in China in recent years. In August 2018, we completed the divestiture of a majority equity stake in our financial services business unit, which has been rebranded as Du Xiaoman Financial, or Du Xiaoman. After the divestiture, we hold a non-controlling equity interest in Du Xiaoman and have since then deconsolidated the financial results of Du Xiaoman from our consolidated financial statements in accordance with U.S. GAAP. The financial services provided by the now-divested Du Xiaoman mainly include consumer credit, wealth management, financial technology services and payment support, through which Du Xiaoman mainly offers technology solutions to financial institution partners covering loan facilitation and risk management aspects and consumer financing to individual customers to meet their cash expenditure needs or business operation requirements. We are still the largest shareholder of Du Xiaoman and would be exposed to losses from Du Xiaoman.

PRC laws and regulations concerning the internet finance industry, particularly those governing wealth management and credit lending, are evolving. Although to our knowledge Du Xiaoman has taken

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careful measures to comply with the laws and regulations that are applicable to its financial services, the PRC government authorities may promulgate new policies, rules and regulations regulating the internet finance industry. For example, the Supreme Court of the PRC has issued a judicial interpretation in August 2020 which has capped the interest rate of loan contract at four times the one-year Loan Prime Rate then effective when such loan contract is executed. As we hold a non-controlling equity interest in Du Xiaoman and do not control Du Xiaoman’s business conduct and operations, we cannot assure you that the practices of Du Xiaoman would not be deemed to violate any PRC laws or regulations, nor can we ensure that all business cooperators on Du Xiaoman’s platform meet all the regulatory compliance requirements. If Du Xiaoman were deemed to violate any current or future applicable PRC laws or regulations, such as the exposure draft of the Interim Measures for the Administration of Internet Small Loan Business recently released, we may be exposed to negative publicity as a result of the potential misconception that Du Xiaoman is still part of our consolidated group. For example, on December 15, 2020, officials from PBOC publicly named deposit products provided by internet financial platforms as illegal and should be subject to regulatory supervision. Many internet financial platforms, including Du Xiaoman, has removed deposit products from their platforms. Events like this may expose us to negative publicity as well.

Interruption or failure of our own information technology and communications systems or those of third-party service providers we rely upon could impair our ability to provide products and services, which could damage our reputation and harm our results of operations.

Our ability to provide products and services depends on the continuing operation of our information technology and communications systems. Any damage to or failure of our systems could interrupt our services. Service interruptions could reduce our revenue and profit and damage our brand if our systems are perceived to be unreliable. Our systems are vulnerable to damage or interruption as a result of terrorist attacks, wars, earthquakes, floods, fires, power loss, telecommunications failures, health epidemics, undetected errors or “bugs” in our software, computer viruses, interruptions in access to our platform through the use of “denial of service” or similar attacks, hacking or other attempts to harm our systems, and similar events. Some of our systems are not fully redundant, and our disaster recovery planning does not account for all possible scenarios. In November 2018, multiple services including Baidu Search, Baidu Feed, Baidu Wiki, Baidu Post and Baidu Knows were inaccessible to users for seventy-three minutes due to a system failure. Such service disruptions adversely affected our user experience.

Our servers, which are hosted at third-party or our own internet data centers, are vulnerable to break-ins, sabotage and vandalism. The occurrence of natural disasters or closure of an internet data center by a third-party provider without adequate notice could result in lengthy service interruptions. In addition, our domain names are resolved into internet protocol (IP) addresses by systems of third-party domain name registrars and registries. Any interruptions or failures of those service providers’ systems, which are beyond our control, could significantly disrupt our own services. If we experience frequent or persistent system failures on our platform, whether due to interruptions and failures of our own information technology and communications systems or those of third-party service providers that we rely upon, our reputation and brand could be severely harmed. The steps we take to increase the reliability and redundancy of our systems may cause us to incur heavy costs and reduce our operating margin, and may not be successful in reducing the frequency or duration of service interruptions.

We may not be able to manage our expanding operations effectively.

We expect to continue to expand our operations as we grow our user and customer base and explore new opportunities. To manage the further expansion of our business and growth of our operations and

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personnel, we need to continually improve our operational and financial systems, procedures and controls, and expand, train, manage and maintain good relations with our growing employee base. We have experienced labor disputes in the past. Although these disputes were resolved promptly, we cannot assure you that there will not be any new labor disputes in the future.

We expect our AI-enabled business to become a key revenue driver of Baidu Core, and believe our future growth relies on the success of our AI-enabled business. Our systems and processes were designed in the past to support our mobile ecosystem business operations. For our AI-enabled business operations to be successful, we must be able to attract industry expertise and talents, and adapt to systems and processes suitable for the enterprise and public sector business environment. If we are unable to do so, we may not be competitive in these markets and our AI-enabled business offerings will not be successful. In addition, we must maintain and expand our relationships with other websites, internet companies and other third parties. Our current and future personnel, systems, procedures and controls may not be adequate to support our expanding operations, and consequently our financial condition and operating results may be materially and adversely affected.

We may face intellectual property infringement claims and other related claims, which could be time-consuming and costly to defend and may result in an adverse impact over our operations.

Internet, technology and media companies are frequently involved in litigation based on allegations of infringement of intellectual property rights, unfair competition, invasion of privacy, defamation and other violations of other parties' rights. The validity, enforceability and scope of protection of intellectual property in internet-related and AI-related industries, particularly in China, are uncertain and still evolving. As we face increasing competition and as litigation becomes more common in China in resolving commercial disputes, we face a higher risk of being the subject of intellectual property infringement claims. We may be subject to administrative actions brought by relevant PRC competent governmental authorities such as the PRC State Copyright Bureau and in the most severe scenario criminal prosecution for alleged copyright infringement, and as a result may be subject to fines and other penalties and be required to discontinue infringing activities. Furthermore, as we expand our operations outside of China, we may be subject to claims brought against us in jurisdictions outside of China.

Our search products and services link to materials in which third parties may claim ownership of trademarks, copyrights or other rights. As we adopt new technologies and roll out new products and services, we face the risk of being subject to intellectual property infringement claims that may arise from our use of new technologies and provision of new products and services. Our products and services including those based on content storage and sharing, such as Baidu Knows, Baidu Wiki, Baidu Wenku, Baidu Post, Baidu Drive, Baijiahao, Haokan, Quanmin, and iQIYI's user-generated content, allow our users to upload, store and share documents, images, audio and videos on our servers, or share, link to or otherwise provide access to contents from other websites, and we also operate distribution platforms whereby developers can upload, share and sell their apps or games to users. Although we have made commercially reasonable efforts to request users or developers to comply with applicable intellectual property laws, we cannot ensure that all of our users or developers have the rights to upload or share these contents or apps. In addition, we have been and may continue to be subject to copyright or trademark infringement and other related claims from time to time, in China and internationally.

We have been making continuous efforts to keep ourselves informed of and to comply with all applicable laws and regulations affecting our business. However, PRC laws and regulations are evolving, and uncertainties still exist with respect to the legal standards as well as the judicial

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interpretation of the standards for determining liabilities of internet search and other internet service providers for providing links to content on third-party websites that infringe upon others’ copyrights or hosting such content, or providing information storage space, file sharing technology or other internet services that are used by internet users to disseminate such content. The Supreme People’s Court of China promulgated a judicial interpretation on infringement of the right of dissemination through internet in December 2012, which was further amended on December 29, 2020 and came into effect on January 1, 2021. This judicial interpretation, like certain court rulings and certain other judicial interpretations, provide that the courts will place the burden on internet service providers to remove not only links or contents that have been specifically mentioned in the notices of infringement from right holders, but also links or contents they “should have known” to contain infringing content. The interpretation further provides that where an internet service provider has directly obtained economic benefits from any content made available by an internet user, it has a higher duty of care with respect to internet users’ infringement of third-party copyrights. A guidance on the trial of audio/video sharing copyright disputes promulgated by the Higher People’s Court of Beijing in December 2012 provides that where an internet service provider has directly obtained economic benefits from any audio/video content made available by an internet user who has no authorization for sharing such content, the internet service provider shall be presumed to be at fault. The Civil Code promulgated in 2020 has further elaborated the circumstances where internet service providers may be found liable for the infringement of third parties. See “Regulations—Regulations on Tort Liability”. The Copyright Law which will become effective in June 2021 further provides that the competent copyright authority may require compliance from the relevant parties in the process of investigating the infringing activities.

These interpretations could subject us and other internet service providers to significant administrative burdens and litigation risks.

We conduct our business operations primarily in China. There might be claims that we are subject to U.S. copyright laws, including the legal standards for determining indirect liability for copyright infringement, although we believe such claims are without merit. We cannot assure you that we will not be subject to copyright infringement lawsuits or other proceedings in the U.S. or elsewhere in the future.

Intellectual property litigation is expensive, time-consuming and could divert resources and management attention from the operations of our business. We are currently named as defendant in certain copyright infringement suits in connection with Baidu Feed, P4P, Baidu Post, Baidu Search, iQIYI, Baidu Wenku, Baidu Drive, Baijiahao, Haokan and certain other products or services. See “Business—Legal Proceedings.” There is no guarantee that the courts will accept our defenses and rule in our favor. If there is a successful claim of infringement, we may be required to discontinue the infringing activities, pay substantial fines and damages and/or enter into royalty or license agreements that may not be available on commercially acceptable terms, if at all. Our failure to obtain a license of the rights on a timely basis could harm our business. Any intellectual property litigation by third parties and/or negative publicity alleging our intellectual property infringement could have an adverse effect on our business, reputation, financial condition or results of operations. To address the risks relating to intellectual property infringement, we may have to substantially modify, limit or terminate some of our search services. Any such change could materially affect user experience and in turn have an adverse impact on our business.

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Liability claims against, or any unauthorized control or manipulation of our autonomous driving systems, could result in the loss of confidence in us, our brands and our products, and harm our business.

Our Intelligent Driving platform contains complex information technology systems. We have designed, implemented and tested security measures intended to prevent unauthorized access to our Intelligent Driving platform, but there can be no assurance that vulnerabilities will not be identified in the future, or that our remediation efforts are or will be successful. Hackers have reportedly attempted, and may attempt in the future, to gain unauthorized access to modify, alter and use our Intelligent Driving platform to gain control of, or to change, functionality, user interface and performance characteristics of vehicles utilizing our Intelligent Driving platform, or to gain access to data stored in or generated by the vehicles. Any unauthorized access to or control of autonomous driving vehicles or their systems or any loss of data could result in death and personal injury, and legal claims or proceedings against us.

Our Intelligent Driving platform may be involved in crashes resulting in property damage, death or personal injury in the future, and such crashes may be the subject of significant public attention. We may face claims related to any misuse or failure of new technologies that we are pioneering, including our Intelligent Driving platform and related solutions, such as smart transportation. A successful product liability claim against us could require us to pay substantial monetary damages.

Moreover, product liability claims or reports of unauthorized access to our Intelligent Driving platform or data, regardless of their veracity, could generate substantial negative publicity about our products and business and could have material adverse impact on our brand, business, prospects and operating results.

Our strategy of investments and acquiring complementary businesses and assets may fail.

As part of our business strategy, we have pursued, and intend to continue to pursue, selective strategic investments and acquisitions of businesses and assets that complement our existing business and help us execute our growth strategies. For example, we invested in Trip.com Group Limited (Trip.com) (formerly known as Ctrip). In November 2020, we entered into definitive agreements with JOYY Inc. and certain of its affiliates to acquire its domestic video-based entertainment live streaming business in China, or YY Live, which includes YY mobile app, YY.com website and PC YY, among others. For more details, see “—We face risks associated with our acquisition of YY Live and its online live streaming business.”

We intend to make other strategic investments and acquisitions in the future if suitable opportunities arise. Investments and acquisitions involve uncertainties and risks, including, but not limited to:

- potential ongoing financial obligations and unforeseen or hidden liabilities, including liability for infringement of third-party copyrights or other intellectual property;
- failure to achieve the intended objectives, benefits or revenue-enhancing opportunities,
- non-occurrence of anticipated or speculative transactions and any resulting negative impact;
- costs and difficulties of integrating acquired businesses and managing a larger business;
- in the case of investments where we do not obtain management and operational control, lack of influence over the controlling partner or shareholder, which may prevent us from achieving our strategic goals in the investments;
- possible unsatisfactory operational or financial performance, including financial loss, or fraudulent activities of a target business;

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- possible loss of key employees of a target business;
- potential claims or litigation regarding our board’s exercise of its duty of care and other duties required under applicable law in connection with any of our significant acquisitions or investments approved by the board;
- diversion of resources and management attention;
- regulatory hurdles and compliance risks, including the anti-monopoly and competition laws, rules and regulations of China and other jurisdictions and the enhanced compliance requirement for outbound acquisitions and investment under the laws and regulations of China; and
- in the case of acquisitions of businesses or assets outside of China, the need to integrate operations across different business cultures and languages and to address the particular economic, currency, political, and regulatory risks associated with specific countries.

Any failure to address these risks successfully may have a material and adverse effect on our financial condition and results of operations. Investments and acquisitions may require a significant amount of capital, which would decrease the amount of cash available for working capital or capital expenditures. In addition, if we use our equity securities to pay for investments and acquisitions, we may dilute the value of our listed securities and the ordinary shares underlying our ADSs. If we borrow funds to finance investments and acquisitions, such debt instruments may contain restrictive covenants that could, among other things, restrict us from distributing dividends. Moreover, acquisitions may also generate significant amortization expenses related to intangible assets. We are required to test our intangible assets and goodwill for impairment annually or more frequently if events or changes in circumstances indicate that they may be impaired. We may also incur impairment charges to earnings for investments and acquired businesses and assets.

There can be no assurance that the acquired YY Live will bring the anticipated strategic benefits to us. We have relatively limited experience with operating the online live streaming business and we may not be able to successfully integrate YY Live into our existing business. We face uncertainties and challenges in navigating the complex regulatory environment, competing effectively in attracting and retaining users and hosts, and developing and/or upgrading products and services as well as technologies to meet everchanging user needs.

We would be subject to and may not be able to successfully manage a variety of additional risks associated with the online streaming business. These risks include, but are not limited to, the following:

- the online live streaming business is based on a relatively new business model in a relatively new market in which user demand may change or decrease substantially;
- rules and measures governing online live streaming businesses and hosts are complex and evolving, and we may not be able to navigate such complex regulatory environment;
- we may face significant risks related to the content and communications on YY Live, as a majority of the communications on YY Live are conducted in real time, and we are unable to verify the sources of all information posted thereon or examine the content generated by users before it is posted;
- the revenue model for online live streaming may not remain effective, and we may not be able to retain existing users, attract new users, keep users engaged and attract more paying users; and
- we may not be able to retain or attract popular talents such as performers, channel managers, professional game players, commentators and hosts for our live streaming platform or these talents may fail to draw fans or participants.

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Our business is subject to complex and evolving Chinese and international laws and regulations regarding privacy and data protection. Many of these laws and regulations are subject to change and uncertain interpretation, and could result in claims, changes to our business practices, increased cost of operations, or declines in user growth or engagement, or otherwise harm our business.

We are required by privacy and data protection laws in China and other jurisdictions, including, without limitation, the PRC Cyber Security Law, to ensure the confidentiality, integrity and availability of the information of our users, customers, third-party agents, content providers and Baidu Union partners, which is also essential to maintaining their confidence in our online products and services. However, the interpretation and application of such laws in China and elsewhere are often uncertain and in flux.

In December 2012, the Standing Committee of the PRC National People’s Congress promulgated the Decision on Strengthening Network Information Protection, or the Network Information Protection Decision, to enhance the legal protection of information security and privacy on the internet. The Network Information Protection Decision also requires internet operators to take measures to ensure confidentiality of information of users. 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 service and internet information service in China. In August 2015, the Standing Committee of the National People’s Congress promulgated the Ninth Amendment to the Criminal Law, which became effective in November 2015 and amended the standards of crime of infringing citizens’ personal information and reinforced the criminal culpability of unlawful collection, transaction, and provision of personal information. It further provides that any ICP provider that fails to fulfill the obligations related to internet information security administration as required by applicable laws and refuses to rectify upon orders will be subject to criminal liability. In November 2016, the Standing Committee of the National People’s Congress promulgated the PRC Cyber Security Law, which requires, among others, that network operators take security measures to protect the network from unauthorized interference, damage and unauthorized access and prevent data from being divulged, stolen or tampered with. Network operators are also required to collect and use personal information in compliance with the principles of legitimacy, properness and necessity, and strictly within the scope of authorization by the subject of personal information unless otherwise prescribed by laws or regulations. Significant capital, managerial and human resources are required to comply with legal requirements, enhance information security and to address any issues caused by security failures. The Civil Code promulgated in 2020 also provides specific provisions regarding the protection of personal information. See “Regulations—Regulations on Information Security” and “Regulations—Regulations on Internet Privacy”

The PRC Cyber Security Law and Civil Code are relatively new and subject to interpretation by the regulators. Although we only gain access to user information that is necessary for, and relevant to, the services provided, the data we obtain and use may include information that is deemed as “personal information” under the PRC Cyber Security Law, the Civil Code and related data privacy and protection laws and regulations. As such, we have adopted a series of measures to ensure that we comply with relevant laws and regulations in the collection, use, disclosure, sharing, storage, and security of user information.

While we take all these measures to comply with all applicable data privacy and protection laws and regulations, we cannot guarantee the effectiveness of the measures undertaken by us and business partners, and such measures may still be determined as insufficient, improper, or even as user-privacy invasive, by the relevant authorities, which may result in penalties against us. The activities of third

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parties such as our customers and business partners are beyond our control. If our business partners violate the PRC Cyber Security Law and other laws and regulations relating to the protection of personal information, or fail to fully comply with the service agreements with us, or if any of our employees fail to comply with our internal control measures and misuse the information, we may be subject to penalties and other legal liabilities. Any failure or perceived failure to comply with all applicable data privacy and protection laws and regulations, or any failure or perceived failure of our business partners to do so, or any failure or perceived failure of our employees to comply with our internal control measures, may result in negative publicity and legal proceedings or regulatory actions against us, and could damage our reputation, discourage current and potential users and customers from using our products or services and subject us to fines and damages, which could have a material adverse effect on our business and results of operations.

The PRC laws and regulations concerning data protection are subject to changes and updates from time to time. For example, the Draft Personal Information Protection Law promulgated by the Standing Committee of the National People’s Congress in October 2020 sets forth more specific requirements on and introduces notable changes to the current obligations of personal information protection under applicable PRC laws and regulations. There are also a number of legislative proposals in the European Union and the United States, at both the federal and state level, as well as other jurisdictions that could impose new obligations in areas affecting our business. New laws or regulations concerning data protection, or the interpretation and application of existing consumer and data protection laws or regulations, which are often uncertain and in flux, may be inconsistent with our practices. The introduction of new products or other actions that we may take may subject us to additional laws, regulations, or other government scrutiny. Complying with new laws and regulations could cause us to incur substantial costs or require us to change our business practices in a manner materially adverse to our business. For example, if privacy concerns or regulatory restrictions prevent us from selling demographically targeted advertising, we may become less attractive to online advertising customers. In addition, some countries are considering or have passed legislation implementing data protection requirements or requiring local storage and processing of data or similar requirements that could increase the cost and complexity of delivering our services.

Any failure or perceived failure by us to prevent information security breaches or to comply with privacy policies or privacy-related legal obligations, or any compromise of security that results in the unauthorized use, release or transfer of personally identifiable information or other user data, could cause our users to lose trust in us and could expose us to legal claims or penalties. Any perception by the public that privacy of user information are becoming increasingly unsafe or vulnerable to attacks could inhibit the growth of our products and services generally. We expect that these areas will be subject to greater public scrutiny and attention from regulators and more frequent and rigid investigation or review by regulators, which will increase our compliance costs and subject us to heightened risks and challenges. We may have to spend much more personnel cost and time evaluating and managing these risks and challenges in connection with our products and services in the ordinary course of our business operations, and cooperated and will keep cooperating in the future with the competent regulators in these respects. If we are unable to manage these risks, we could become subject to penalties, including fines, suspension of business and revocation of required licenses, and our reputation and results of operations could be materially and adversely affected.

Our business may be adversely affected if we were found to have failed to fulfill the additional obligations under the online advertising rules.

Although the PRC Advertising Law has not specified “paid search results” as a form of advertising, the Interim Administration Measures of Internet Advertising, or the Internet Advertising Measures, which

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was promulgated by the SAIC (currently known as SAMR) and became effective on September 1, 2016, characterizes “paid search results” as a form of internet advertising from the perspective of regulating the online advertising business. Pursuant to the Internet Advertising Measures, we are subject to additional legal obligations to monitor our P4P customers’ listings on our website during the course of our provision of P4P services. For example, we must examine, verify and record identity information of our P4P customers, such as the customer’s name, address and contact information, and maintain an updated verification of such information on a regular basis. Moreover, we must examine supporting documentation provided by our P4P customers. Where a special government review is required for specific categories of advertisements before posting, we must confirm that the review has been performed and approval has been obtained. If the content of the advertisement is inconsistent with the supporting documentation, or the supporting documentation is incomplete, the advertisement cannot be published. The Chinese government may, from time to time, promulgate new advertising laws and regulations in the future to impose further requirements on online advertising services relating to medical, pharmaceutical, health care and other similar businesses. We cannot assure that we will be in compliance with the requirements under these new laws and regulations. Failure to comply with these obligations may subject us to fines and other administrative penalties. If advertisements shown on our platform are in violation of relevant PRC advertising laws and regulations, or if the supporting documentation and government approvals provided to us by our P4P customers in connection with the advertising content are not complete or accurate, we may be subject to legal liabilities and our reputation could be harmed. See “Regulations—Regulations on Advertisements and Online Advertising.”

We may be subject to patent infringement claims with respect to our P4P platform.

Our technologies and business methods, including those relating to our P4P platform, may be subject to third-party claims or rights that limit or prevent their use. We applied for a patent in China for our P4P platform, but our application was rejected on the ground that it is not patentable. Certain U.S.-based companies, including Overture Services Inc., have been granted patents in the United States relating to P4P platforms and similar business methods and related technologies. While we believe that we are not subject to U.S. patent laws since we conduct our business operations primarily in China, we cannot assure you that U.S. patent laws would not be applicable to our business operations, or that holders of patents relating to a P4P platform would not seek to enforce such patents against us in the United States or China.

Many parties are actively developing and seeking protection for internet-related technologies, including patent protection. They may hold patents issued or pending that relate to certain aspects of our technologies, products, business methods or services. Any patent infringement claims, regardless of their merits, could be time-consuming and costly to us. If we were sued for patent infringement claims with respect to our P4P platform and were found to infringe upon the patents and were not able to adopt non-infringing technologies, we may be severely limited in our ability to operate our P4P platform, which would have a material and adverse effect on our results of operations and prospects.

Our business may be adversely affected by third-party software apps or practices that interfere with our receipt of information from, or provision of information to, our users, which may impair our users’ experience.

Our business may be adversely affected by third-party malicious or unintentional software apps that make changes to our users’ computers and interfere with our products and services. These software apps may change our users’ internet experience by hijacking queries to our platform, altering or replacing our search results, or otherwise interfering with our ability to connect with our users. The

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interference often occurs without disclosure to or consent from users, resulting in a negative experience, which users may associate with our platform. These software apps may be difficult to remove or disable, may reinstall themselves and may circumvent other apps’ efforts to block or remove them.

In addition, our business may be adversely affected by the practices of third-party website owners, content providers and developers which interfere with our ability to crawl and index their web pages and contents including apps. The ability to provide a superior user experience is critical to our success. If we are unable to successfully combat malicious third-party software apps that interfere with our products and services, our reputation may be harmed. If a significant number of website owners, content providers and developers prevent us from indexing and including their high-quality web pages and content including apps in our search results, or if we cannot effectively combat web spam from low-quality and irrelevant content websites, the quality of our search results may be impaired, which may damage our reputation and deter our current and potential users from using our products and services.

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

We rely on a combination of copyright, trademark and trade secret laws, as well as nondisclosure agreements and other methods to protect our intellectual property rights. The protection of intellectual property rights in China may not be as effective as those in the United States or other countries. The steps we have taken may be inadequate to prevent the misappropriation of our technology. Reverse engineering, unauthorized copying or other misappropriation of our technologies could enable third parties to benefit from our technologies without paying us. Moreover, unauthorized use of our technology could enable our competitors to offer products and services that compete with ours, which could harm our business and competitive position. We have in the past resorted to litigation to enforce our intellectual property rights, and may have to do so from time to time in the future. There is no guarantee that the competent courts will accept our claims and rule in our favor. Such litigation may result in substantial costs and diversion of resources and management attention.

Our success depends on the continuing and collaborative efforts of our management team and other key personnel, and our business may be disrupted if we lose their services and are not able to find their successors in a timely manner.

Our success depends heavily upon the continuing services of our management team, in particular our chairman and chief executive officer, Robin Yanhong Li. If one or more of our executives or other key personnel are unable or unwilling to continue in their present positions and we are not able to find their successors in a timely manner, our business may be disrupted and our financial condition and results of operations may be adversely affected. Competition for management and key personnel is intense, the pool of qualified candidates is limited, and we may not be able to retain the services of our executives or key personnel, or attract and retain experienced executives or key personnel in the future.

If any of our executives or other key personnel joins a competitor or forms a competing company, we may not be able to successfully retain customers, key agents, know-how and key personnel. Each of our executive officers and key employees has entered into an employment agreement with us, containing confidentiality and non-competition provisions. If any disputes arise between any of our executives or key personnel and us, we cannot assure you the extent to which any of these agreements may be enforced.

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We rely on highly skilled personnel. If we are unable to retain or motivate them or hire additional qualified personnel, we may not be able to grow effectively.

Our performance and future success depend on the talents and efforts of highly skilled individuals. We will need to continue to identify, hire, develop, motivate and retain highly skilled personnel for all areas of our organization and business operations. Competitions for qualified employees in the industries we operate in is intense. Our continued ability to compete effectively depends on our ability to attract new employees and to retain and motivate our existing employees. As competitions in our industries intensify, it may be more difficult for us to hire, motivate and retain highly skilled personnel. In general, if we do not succeed in attracting additional highly skilled personnel or retaining or motivating our existing personnel, we may be unable to grow effectively. In certain emerging industry, such as autonomous driving, many players with sufficient funds would heavily devote their resources to compete for talents with us. To keep our competitiveness and market position, we would need to, among others, recruit, train and retain our key talents and employees, in particular research and development personnel. If we fail to do so, we may lag behind with respect to the ever-emerging and cutting-edge technologies in the emerging industry, and our prospects in such industry would be ultimately harmed.

We are exposed to significant downward adjustments or impairments in the market values of our investments, which will be material to financial statements.

As part of our business strategy, we have investments in both private and public companies. Fair values of these investments can be negatively impacted by fluctuations in the share prices of public companies we own, the fair value of private companies we own, liquidity, credit deterioration or losses, financial results, foreign exchange rates, changes in interest rates, or other factors. In addition, after adopting ASC Topic 321, *Investments—Equity Securities* (“ASC 321”), on January 1, 2018, for investments previously accounted for using the cost method, we elected to use the measurement alternative to measure these investments at cost, less any impairment, plus or minus changes resulting from observable price changes in orderly transactions for identical or similar investments of the same issuer, if any. Equity securities with readily determinable fair values are measured at fair value, and any changes in fair value are recognized in earnings, instead of through other comprehensive income if they were previously designated as available for sale equity securities under legacy GAAP. The change of these equity securities’ fair value could result in significant fluctuation of our financial condition and operating results.

For example, in 2019, the market value of Trip.com declined, and the continuing low market price of its ADSs caused us to recognize a non-cash impairment loss of RMB8.9 billion in the third quarter of 2019. We have also recognized impairment charges on our long-term investments in 2020, due to the impact of COVID-19 and other factors. We may still suffer significant impairment loss or downward adjustments of our investments in the future. The carrying amounts of short-term investments and long-term investments as of December 31, 2020 were RMB126.4 billion (US\$19.4 billion) and RMB76.2 billion (US\$11.7 billion), respectively. The value or liquidity of our investments could decline and result in a material impairment, which could materially adversely affect our financial condition and operating results.

We are subject to risks and uncertainties faced by companies in a rapidly evolving industry.

We operate in the rapidly evolving internet industry, which makes it difficult to predict our future results of operations. Accordingly, you should consider our future prospects in light of the risks and

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uncertainties experienced by companies in evolving industries. Some of these risks and uncertainties relate to our ability to:

- maintain our leading position in the Chinese-language internet search market;
- offer attractive, useful and innovative products and services to attract and retain a larger user base;
- procure content from studios and other content providers, as well as distribution channels and other licensors of content;
- attract users’ continuing use of internet search services;
- retain existing customers and attract additional customers and increase spending per customer;
- evaluate the credit worthiness and collectability of accounts receivables from an evolving variety of customers, whose failure to pay us in a timely manner may adversely affect our liquidity position;
- retain members and attract new members of iQIYI’s membership services;
- upgrade our technology to support increased traffic and expanded product-and-service offerings;
- further enhance our brand;
- respond to competitive market conditions;
- respond to evolving user preferences or industry changes;
- respond to changes in the regulatory environment and manage legal risks, including those associated with intellectual property rights;
- maintain effective control of our costs and expenses;
- execute our strategic investments and acquisitions and post-acquisition integrations effectively;
- attract, retain and motivate qualified personnel and maintain good relations with a young and growing work force; and
- build profitable operations in new markets and other overseas internet markets we have entered into.

If we are unsuccessful in addressing any of these risks and uncertainties, our business may be materially and adversely affected.

Our indebtedness could adversely affect our financial condition and our ability to obtain additional capital on reasonable terms when necessary.

As of December 31, 2020, we had an aggregate of RMB75.5 billion (US\$11.6 billion) of outstanding indebtedness (including loans, convertible senior notes and notes payable), which will mature between 2021 and 2030, which include RMB20.6 billion (US\$3.2 billion) of outstanding indebtedness of iQIYI. In February 2021, we entered into a non-binding term sheet for a term and revolving facility with a group of five mandated lead arrangers, bookrunners and underwriters, pursuant to which we plan to borrow a total of US\$3 billion. See “Financial Information—Liquidity and Capital Resources”. We may incur additional indebtedness in the future. Our current and future debt requires us to dedicate a portion of our cash flow to service interest and principal payments and may limit our ability to engage in other transactions. Our ability to pay interest and repay the principal for our indebtedness is dependent upon our ability to manage our business operations, generate sufficient cash flows, raise additional capital and the other factors discussed in this section. There can be no assurance that we will be able to manage any of these risks successfully.

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Certain of our outstanding indebtedness include financial and other covenants. For example, certain of these covenants require iQIYI to maintain minimum liquidity. If we fail to comply with these covenants and are unable to remedy or obtain a waiver or amendment, an event of default would result. If an event of default were to occur, the lenders could, among other things, declare outstanding amounts due and payable. In addition, because certain outstanding notes of Baidu, Inc. contain customary cross default and cross acceleration provisions, an event of default or declaration of acceleration under a subsidiary’s outstanding loan could also result in an event of default under these notes of Baidu, Inc., which would permit the notes holders to accelerate the repayment of the notes. If any of these notes is accelerated, we may be required to renegotiate, repay or refinance these obligations and may not have sufficient funds available to repay it, and our liquidity and financial position would be materially and adversely affected.

We may require additional capital to support our business growth or to respond to business opportunities, challenges or unforeseen circumstances. Our ability to obtain additional capital, if and when required, will depend on our business plans, investor demand, our operating performance, the condition of the capital markets, and other factors, and our indebtedness may limit our ability to borrow additional funds. We may have difficulty incurring new debt on terms that we would consider to be commercially reasonable. In addition, we may also need to refinance a portion of our outstanding debt as it matures. There is a risk that we may not be able to refinance existing debt or that the terms of any refinancing may not be as favorable as the terms of our existing debt.

iQIYI has significant working capital requirements, and our controlling interest in iQIYI may be diluted if iQIYI raises additional capital by issuing and selling additional equity in the future.

iQIYI, our controlled subsidiary listed on the Nasdaq Global Select Market, has experienced working capital deficits. iQIYI had achieved a working capital surplus as of December 31, 2018 and December 31, 2019, but experienced a working capital deficit as of December 31, 2020. There is no assurance that iQIYI will be able to improve its working capital position and achieve working capital surplus again, although iQIYI will take actions to manage its working capital. iQIYI raised a concurrent equity and convertible bond offering in December 2020. There can be no assurance that iQIYI will be able to raise additional equity or debt financing on terms that are acceptable to iQIYI in the future. Any failure to do so as and when necessary could materially adversely affect iQIYI’s liquidity, results of operations, financial condition and ability to operate. In addition, when iQIYI obtains additional financing by issuing and selling additional equity or equity-linked securities, such as convertible bonds, our interest in iQIYI will be diluted.

iQIYI operates in a capital intensive industry and requires a significant amount of cash to fund its operations, content acquisitions and technology investments. If iQIYI cannot obtain sufficient capital, its business, financial condition and prospects may be materially and adversely affected.

The operation of an internet video streaming platform requires significant and continuous investment in content and technology. Producing high-quality original content is costly and time-consuming and it will typically take a long period of time to realize returns on investment, if at all. To date, iQIYI has financed its operations primarily with net cash generated from operating activities, as well as financing activities such as placements of preferred shares, convertible notes and asset-based securities, and the proceeds from its initial public offering. In order to implement its growth strategies, iQIYI will incur additional capital in the future to cover, among others, costs to produce and license content. iQIYI may need to obtain additional financing, including equity offering or debt financing, to fund the operation

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and expansion of business. iQIYI’s ability to obtain additional financing in the future, however, is subject to a number of uncertainties, including those relating to:

- iQIYI’s business development, financial condition and results of operations;
- general market conditions for financing activities by companies in iQIYI’s industry; and
- macro-economic and other conditions in China and elsewhere.

As a public company with a growing business, iQIYI expects to increasingly rely on net cash provided by operating activities, financing through capital markets and commercial banks for its liquidity needs. However, iQIYI cannot assure you that it will be successful in its efforts to further diversify its sources of liquidity and obtain financing. In addition, certain financing may pose additional capital needs on iQIYI, for example, the potential redemption by holders of iQIYI’s convertible notes. See “Financial Information—Liquidity and Capital Resources.” If iQIYI cannot obtain sufficient capital to meet its capital needs, iQIYI may not be able to execute its growth strategies and its business, financial condition and prospects may be materially and adversely affected.

Our results of operations may fluctuate, which makes our results difficult to predict and could cause our results to fall short of expectations.

Our results of operations may fluctuate as a result of a number of factors, many of which are beyond our control. For these reasons, comparing our results of operations on a period-to-period basis may not be meaningful, and you should not rely on our past results as an indication of our future performance. Our quarterly and annual revenues and costs and expenses as a percentage of our revenues may be significantly different from our historical or projected figures. Our results of operations in future quarters may fall below expectations. Any of these events could cause the price of our securities to fall. Any of the risk factors listed in this “Risk Factors” section, and in particular the following factors, could cause our results of operations to fluctuate from quarter to quarter:

- general economic conditions in China and economic conditions specific to the internet, internet search and feed, and online marketing industries;
- our ability to continue to attract users to our platform despite the emergence of mobile apps and other services;
- our ability to attract additional customers and increase spending per customer;
- the announcement or introduction of new or enhanced products and services by us or our competitors;
- the amount and timing of operating costs and capital expenditures related to the maintenance and expansion of our businesses, operations and infrastructure;
- the results of our acquisitions of, or investments in, other businesses or assets;
- PRC regulations or government actions pertaining to activities on the internet, including various forms of entertainment, online payment and activities otherwise affecting our online marketing customers, and those relating to the products and services we provide;
- unforeseen events, such as negative publicity arising from widespread media coverage and other sources and labor disputes; and
- geopolitical events, natural disasters or epidemics.

Because of the rapid growth of our business, our historical results of operations may not be useful to you in predicting our future results of operations. Our user traffic tends to be seasonal. For example, we generally experience less user traffic during public holidays and other special event periods in China. In addition, advertising and other marketing spending in China has historically been cyclical,

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reflecting overall economic conditions as well as budgeting and buying patterns. As we continue to grow, we expect that the cyclical and seasonality in our business may cause our results of operations to fluctuate.

A severe and prolonged downturn in the Chinese or global economy could materially and adversely affect our business, results of operations and financial condition.

COVID-19 has had a severe and negative impact on the Chinese and global economy since early 2020. Whether this will lead to a prolonged downturn in the economy is still unknown, especially considering the multiple recent outbreaks in various countries and regions as well as the uncertainties brought by the newly launched vaccination programs. Even before the outbreak of COVID-19, the global macroeconomic environment had been facing challenges. The growth of the Chinese economy has gradually slowed down in recent years and the trend may continue. There is considerable uncertainty over the long-term effects of the monetary and fiscal policies adopted by the central banks and financial authorities of some of the world’s leading economies, including the United States and China. There have been concerns over unrest and terrorist threats in the Middle East, Europe and Africa. There have also been concerns on the relationship between China and other countries, including surrounding Asian countries, which may potentially lead to foreign investors closing down their businesses or withdrawing their investments in China and, thus, exiting the China market, and other economic effects. In particular, there is significant uncertainty about the future relationship between the United States and China with respect to trade policies, treaties, government regulations and tariffs. Economic conditions in China are sensitive to global economic conditions, as well as changes in domestic economic and political policies and the expected or perceived overall economic growth rate in China. Any severe or prolonged slowdown in the global or Chinese economy may have a negative impact on our business, results of operations and financial condition, and continued turbulence in the international markets may adversely affect our ability to access the capital markets to meet liquidity needs. Our customers may reduce or delay spending with us, while we may have difficulty expanding our customer base fast enough, or at all, to offset the impact of decreased spending by our existing customers. In addition, to the extent we offer credit to any customer and the customer experiences financial difficulties due to the economic slowdown, we could have difficulty collecting payment from the customer.

Rising international political tensions, including changes in U.S. and international trade policies, particularly with regard to China, may adversely impact our business and operating results.

The U.S. government has made statements and taken certain actions that may lead to changes in U.S. and international trade policies towards China. In January 2020, the “Phase One” agreement was signed between the United States and China on trade matters. However, it remains unclear what additional actions, if any, will be taken by the U.S. or other governments with respect to international trade agreements, the imposition of tariffs on goods imported into the United States, tax policy related to international commerce, or other trade matters. While cross-border business may not be an area of focus for us, any unfavorable government policies on international trade, such as capital controls or tariffs, may affect the demand for our products and services, impact the competitive position of our products or prevent us from selling products in certain countries. If any new tariffs, legislation and/or regulations are implemented, or if existing trade agreements are renegotiated or, in particular, if the U.S. government takes retaliatory trade actions due to recent U.S.-China trade tensions, such changes could have an adverse effect on our business, financial condition and results of operations.

In addition, we have been closely monitoring domestic policies in the United States designed to restrict certain Chinese companies from supplying or operating in the U.S. market. These policies include the Clean Network project initiated by the U.S. Department of State in August 2020 and new authorities

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granted to the Department of Commerce to prohibit or restrict the use of information and communications technology and services (“ICTS”). While a substantial majority of our business is conducted in China, policies like these may deter U.S. users from accessing and/or using our search engine, apps and other products in the United States, which could adversely impact our user experience and reputation. Similarly, India has banned a large number of apps in 2020 out of national security concerns, many of which are China-based apps (including our apps), escalating regional political and trade tensions.

Likewise, we are monitoring policies in the United States that are aimed at restricting U.S. persons from investing in or supplying certain Chinese companies. The United States and various foreign governments have imposed controls, license requirements and restrictions on the import or export of technologies and products (or voiced the intention to do so). For instance, the United States is in the process of developing new export controls with respect to “emerging and foundational” technologies, which may include certain AI and semiconductor technologies. In addition, the U.S. government may potentially impose a ban prohibiting U.S. persons from making investments in or engaging in transactions with certain Chinese companies. Measures such as these could deter suppliers in the United States and/or other countries that impose export controls and other restrictions from providing technologies and products to, making investments in, or otherwise engaging in transactions with Chinese companies. As a result, Chinese companies would have to identify and secure alternative supplies or sources of financing, while they may not be able to do so in a timely manner and at commercially acceptable terms, or at all. In addition, Chinese companies may have to limit and reduce their research and development and other business activities, or cease conducting transactions with parties, in the United States and other countries that impose export controls or other restrictions. Like other Chinese companies, our business, financial condition and results of operations could be adversely affected as a result.

Failure to retain key third-party agents or attract additional third-party agents, or termination of our relationship with third-party agents could materially and adversely affect our business. Moreover, there is no assurance that our direct sales model in some key geographic markets will continue to be successful.

We rely, to a large extent, on a nationwide distribution network of third-party agents for our sales to, and collection of payment from, our customers. The operations and conduct of such third-party agents are beyond our control. They may fail to provide quality services to our customers or otherwise breach their contracts with our customers, or experience operational or financial difficulties or run out of business, or engage in misconduct with respect to our sales and our customers. If any of the foregoing issues arise, we may terminate our relationship with third-party agents, lose customers and our results of operations may be materially and adversely affected. In the past, there had been alleged incidents of certain of our employees and consultants colluding with third-party agents in illegal activities. Although we have zero tolerance towards any illegal activities and have internal policies and procedures against employee misconduct, we cannot assure you that our employees would always comply with such policies and procedures, nor can we control third-party agents’ conduct or guarantee that such incidents would not happen again. In addition, since most of third-party agents are not bound by long-term contracts, we cannot assure you that we will continue to maintain favorable relationships with them. If we fail to retain key third-party agents or attract additional ones on terms that are commercially reasonable, our business and results of operations could be materially and adversely affected. We may decide to terminate existing third-party agents and transition to new ones or to our own distribution channel. If we decide and fail to smoothly transition our business to new third-party agents or to our own distribution channel, our business and results of operations could be materially and adversely affected.

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We have transitioned to using our direct sales force to serve customers in some key geographic markets, such as Beijing, Shanghai and other cities. There is no assurance that our direct sales model in those markets will continue to be successful. If we fail to maintain an adequate direct sales force, retain existing customers and continue to attract new customers in those markets, our business, results of operations and prospects could be materially and adversely affected.

We may not be able to detect or prevent misconduct committed by our employees or third parties.

Misconduct by our employees, such as unauthorized business transactions, bribery, corruption and breach of our internal policies and procedures, or by consultants or other third parties, such as breach of law, may be difficult to detect or prevent. It could subject us to financial loss and sanctions imposed by governmental authorities while seriously damaging our reputation. This may also impair our ability to effectively attract prospective users, develop customer loyalty, obtain financing on favorable terms and conduct other business activities. Our risk management systems, information technology systems and internal control procedures are designed to monitor our operations and overall compliance. Historically we have identified certain incidents of employee and third-party misconduct. However, there can be no assurance we will be able to identify non-compliance or illegal activities promptly, or at all. Furthermore, it is not always possible to detect and prevent misconduct committed by our employees or third parties, and the precautions we take to prevent and detect such activities may not be effective. This may materially and adversely affect our business, brand, financial condition and results of operations.

We rely on Baidu Union partners for a significant portion of our revenues. If we fail to retain existing Baidu Union partners or attract additional members, our revenue growth and profitability may be adversely affected.

We pay Baidu Union partners a portion of our revenues as we leverage traffic of the Baidu Union partners' internet properties. Some of Baidu Union partners, however, may compete with us in one or more areas of our business. Therefore, they may decide in the future to terminate their relationships with us. If Baidu Union partners decide to use a competitor's or their own internet search services, or if our competitors offer more attractive prices to bid for union traffic, our user traffic may decline, which may adversely affect our revenues. If we fail to attract additional Baidu Union partners, our revenue growth may be adversely affected. In addition, if we have to share a larger portion of our revenues to retain existing Baidu Union partners or attract additional partners, our profitability may be adversely affected.

Our overseas operations may not be successful.

We have launched products and services in local languages to internet users in several countries. It is uncertain when the operation will become profitable, if at all. In particular, we rely on local telecommunication operators and service providers to provide us with network services and data center hosting services, and our systems for these international products and services are not redundant across different regions and data centers. Any interruption to the internet infrastructure or any data center may render our products and services in the region unavailable.

We face certain risks inherent in doing business internationally, including:

- difficulties in developing, staffing and simultaneously managing a foreign operation as a result of distance, language and cultural differences;
- challenges in formulating effective local sales and marketing strategies targeting users from various jurisdictions and cultures, who have a diverse range of preferences and demands;

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- challenges in identifying appropriate local business partners and establishing and maintaining good working relationships with them;
- dependence on local platforms in marketing our international products and services overseas;
- challenges in selecting suitable geographical regions for international business;
- longer customer payment cycles;
- currency exchange rate fluctuations;
- political or social unrest or economic instability;
- compliance with applicable foreign laws and regulations and unexpected changes in laws or regulations;
- exposure to different tax jurisdictions that may subject us to greater fluctuations in our effective tax rate and potentially adverse tax consequences; and
- increased costs associated with doing business in foreign jurisdictions.

One or more of these factors could harm our overseas operations and consequently, could harm our overall results of operations.

If we are unable to adapt or expand our existing technology infrastructure to accommodate greater traffic, content or additional customer requirements, our business may be harmed.

Our Baidu platform regularly serves a large number of users and customers and delivers a large number of daily page views. Our technology infrastructure is highly complex and may not provide satisfactory service in the future, especially as the number of users and customers increases. We may be required to upgrade our technology infrastructure to keep up with the increasing traffic on our Baidu platform, such as increasing the capacity of our servers and the sophistication of our software. If we fail to adapt our technology infrastructure to accommodate greater traffic or customer requirements, our users and customers may become dissatisfied with our services and switch to our competitors' websites, which could harm our business.

If we fail to detect fraudulent click-throughs, our customers' confidence in us could be damaged and our revenues could decline.

We are exposed to the risk of click-through fraud on our paid search results. Click-through fraud occurs when a person clicks paid search results for a reason other than to view the underlying content of search results. Although our anti-spam algorithms and tools can identify and respond to spam web pages quickly and effectively and thus capture and prevent some fraudulent click-throughs, there is no assurance that our anti-spam technology is able to detect and stop all fraudulent click-throughs. If we fail to detect fraudulent clicks or otherwise are unable to prevent this fraudulent activity, the affected customers may experience a reduced return on investments, or ROI, in our online marketing services and lose confidence in the integrity of our systems, and we may have to issue refunds to our customers. If this happens, we may be unable to retain existing customers or attract new customers for our online marketing services, and our online marketing revenues could decline. In addition, affected customers may also file legal actions against us claiming that we have over-charged or failed to refund them. Any such claims or similar claims, regardless of their merits, could be time-consuming and costly for us to defend against and could also adversely affect our brand and our customers' confidence in the integrity of our systems. We experienced a number of incidents involving fraudulent click-throughs in recent years. Although the amount of revenue involved in these incidents was immaterial, such cases of fraudulent click-throughs, if occurring on a large-scale and widespread manner, may damage the reputation of our search ecosystem.

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The successful operation of our business depends upon the performance and reliability of the internet infrastructure and fixed telecommunications networks in China.

Our business depends on the performance and reliability of the internet infrastructure in China. Almost all access to the internet is maintained through state-owned telecommunication operators under the administrative control and regulatory supervision of the Ministry of Industry and Information Technology, or the MIIT. In addition, the national networks in China are connected to the internet through international gateways controlled by the PRC government. These international gateways are the only channels through which a domestic user can connect to the internet. It is unpredictable whether a more sophisticated internet infrastructure will be developed in China. We may not have access to alternative networks in the event of disruptions, failures or other problems with China’s internet infrastructure. In addition, the internet infrastructure in China may not support the demands associated with continued growth in internet usage.

We rely heavily on China Telecommunications Corporation, or China Telecom, China United Network Communications Group Company Limited, or China Unicom, and China Mobile Communications Corporation, or China Mobile, to provide us with network services and data center hosting services. We have entered into contracts with various local branches or subsidiaries of China Telecom, China Unicom and China Mobile to obtain data communications capacity. We have limited access to alternative services in the event of disruptions, failures or other problems with the fixed telecommunications networks of these companies, or if these companies otherwise fail to provide the services. Any unscheduled service interruption could damage our reputation and result in a decrease in our revenues. Furthermore, we have no control over the costs of the services provided by these telecommunication companies. If the prices that we pay for telecommunications and internet services rise significantly, our gross margins could be adversely affected. In addition, if internet access fees or other charges to internet users increase, our user traffic may decrease, which in turn may harm our revenues.

Security breaches and improper access to or disclosure of our data or user data, or any system failure or compromise of our security, could harm our reputation and adversely affect our business.

Our business is prone to cyber-attacks seeking unauthorized access to our data or user data or to disrupt our ability to provide services. Any failure to prevent or mitigate security breaches and improper access to or disclosure of our data or user data, such as personal information, including names, accounts, user IDs and passwords, and payment or transaction related information, could result in the loss or misuse of such data, which could cause a loss or give rise to liabilities to the owners of confidential information, such as our users, customers, third-party agents, content providers and Baidu Union partners, subject us to penalties imposed by administrative authorities, and disrupt our operations. For example, Baidu Drive provides services to many individual users who may upload sensitive personal information and documents of significance to Baidu Drive. In the event of an unauthorized access, such information and documents might be leaked or even further sold through illegal means. In addition, computer malware, viruses, social engineering (predominantly spear phishing attacks), and general hacking have become more prevalent in our industry, have occurred on our systems in the past, and may occur again on our systems in the future. We also regularly encounter attempts to create false or undesirable user accounts, purchase ads, or take other actions on our platform for purposes such as spamming, spreading misinformation, or other objectionable ends. As a result of our prominence, the size of our user base, and the types and volume of personal data on our systems, we believe that we are a particularly attractive target for such breaches and attacks. Such attacks may cause interruptions to the services we provide, degrade the user experience, cause users or

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customers to lose confidence and trust in our products and services, impair our internal systems, or result in financial harm to us.

We have adopted strict information security policies and deployed advanced measures to implement the policies, including, among others, advanced encryption technologies. However, we may not be able to implement adequate preventative measures or prevent compromises or breaches of our preventative measures due to the evolution of the sophistication of cyber-attacks, advances in technology, an increased level of sophistication and diversity of our products and services, an increased level of expertise of hackers, new discoveries in the field of cryptography or others, software bugs or other technical malfunctions, employee, contractor, or vendor error or malfeasance, government surveillance, or other evolving threats. As a result, we may incur significant costs in protecting against or remediating cyber-attacks.

In addition, some of our developers or other partners, such as those that help us measure the effectiveness of advertisements, may receive or store information provided by us or by our users through mobile or web applications integrated with our products. We provide limited information to such third parties based on the scope of services provided to us. However, if these third parties fail to adopt or adhere to adequate data security practices, or in the event of a breach of their networks, our data or our users' data may be improperly accessed, used, or disclosed.

Affected users or government authorities could initiate legal or regulatory actions against us in connection with any actual or perceived security breaches or improper disclosure of data, which could cause us to incur significant expense and liabilities or result in orders or consent decrees forcing us to modify our business practices. Such incidents or our efforts to remediate such incidents may also result in a decline in our user base or engagement levels. Any of these events could have a material and adverse effect on our business, reputation, or results of operations.

Defects or errors in our products or services could diminish demand for our products or services, harm our business and results of operations and subject us to liability.

Our customers use our products for important aspects of their personal lives or businesses. Any errors, defects or disruptions to our products and any other performance problems with our products could damage our customers' personal lives or businesses and, in turn, hurt our brand and reputation. We provide regular updates to our products, which have in the past contained, and may in the future contain, undetected errors, failures, vulnerabilities and bugs when first introduced or released. Real or perceived errors, failures or bugs in our products could result in negative publicity, loss of or delay in market acceptance of our platform, loss of competitive position, lower customer retention or claims by customers for losses sustained by them. In such an event, we may be required, or may choose, for customer relations or other reasons, to expend additional resources in order to help correct the problem. In addition, we may not carry insurance to compensate us for any losses that may result from claims arising from defects or disruptions in our products. As a result, our reputation and our brand could be harmed, and our business, results of operations and financial condition may be adversely affected.

Concerns and unfavorable media coverage relating to our privacy practices could damage our reputation, deter current and potential users and customers from using our products and services and negatively impact our business.

The internet industry is facing significant challenges with respect to information security and privacy, including the storage, transmission and sharing of confidential information. The general public, our users, customers, third-party agents, content providers and Baidu Union partners are increasingly

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aware of the vulnerability of confidential and private information. We will continue to experience media or regulatory scrutiny of our actions or decisions regarding user privacy, content or advertising. Furthermore, concerns have been expressed from time to time about whether our products, services or processes could compromise the privacy of users and others.

We transmit and store confidential and private information of our users, customers, third-party agents, content providers and Baidu Union partners, such as personal information, including names, accounts, user IDs and passwords, and payment or transaction related information. Historically there has been negative publicity or media reports making allegations about our practice, and we cannot rule out similar possibilities of such in the future. Although we strive to comply with all privacy related requirements, we cannot guarantee that our products or services are at all times without defect due to the complexity and rapid evolution of technology, etc. Concerns about our practices with regard to the collection, use, disclosure, or security of personal information or other privacy related matters, and any negative publicity on our information safety or privacy protection mechanism and policy, even if unfounded, has in the past, and could adversely affect our business and results of operations and financial condition. Such concerns and negative publicity could damage our reputation and brand, and have an adverse effect on the size, engagement and loyalty of our user base, which could adversely affect our business and results.

If we fail to maintain an effective system of internal control over financial reporting, we may lose investor confidence in the reliability of our financial statements.

We are subject to reporting obligations under the U.S. securities laws. The SEC, as required by Section 404 of the Sarbanes-Oxley Act of 2002, adopted rules requiring every public company to include a management report on the company’s internal control over financial reporting in its annual report, which contains management’s assessment of the effectiveness of its internal control over financial reporting. In addition, an independent registered public accounting firm must attest to and report on the effectiveness of the company’s internal control over financial reporting. We have been subject to these requirements since the fiscal year ended December 31, 2006.

Our management has concluded that our internal control over financial reporting was effective as of December 31, 2019. See “Item 15. Controls and Procedures” of our annual report on Form 20-F for our fiscal year ended December 31, 2019, originally filed with the SEC on March 13, 2020. Our independent registered public accounting firm has issued an attestation report, which has concluded that our internal control over financial reporting was effective in all material aspects as of December 31, 2019. However, if we fail to maintain an effective system of internal control over financial reporting in the future, our management and our independent registered public accounting firm may not be able to conclude that we have effective internal control over financial reporting at a reasonable assurance level. This could in turn result in loss of investor confidence in the reliability of our financial statements and negatively impact the trading price of our securities. Furthermore, we have incurred and anticipate that we will continue to incur considerable costs, management time and other resources in an effort to comply with Section 404 of the Sarbanes-Oxley Act and other requirements.

We are subject to changing laws and regulations regarding regulatory matters, corporate governance and public disclosures that have increased both our costs and the risk of non-compliance.

We are subject to rules and regulations by various governing bodies, including, for example, the SEC, which is charged with the protection of investors and the oversight of companies whose securities are publicly traded, and the various regulatory authorities in China and the Cayman Islands, and to new

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and evolving regulatory measures under applicable law. Our efforts to comply with new and changing laws and regulations have resulted in and are likely to continue to result in, increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities.

Moreover, because these laws, regulations and standards are subject to varying interpretations, their application in practice may evolve over time as new guidance becomes available. This evolution may result in continuing uncertainty regarding compliance matters and additional costs necessitated by ongoing revisions to our disclosure and governance practices. If we fail to address and comply with these regulations and any subsequent changes, we may be subject to penalty and our business may be harmed.

We have limited business insurance coverage.

We have purchased insurance to cover certain liabilities, properties and employees in connection with our intelligent driving business. We only have limited business liability or disruption insurance coverage for our operations in China. Any business disruption may result in our incurring substantial costs and the diversion of our resources.

We face risks related to health epidemics, severe weather conditions and other outbreaks.

In recent years, there have been outbreaks of epidemics in China and globally, including the outbreak of COVID-19. In March 2020, the World Health Organization declared the COVID-19 a pandemic. COVID-19 has resulted in quarantines, travel restrictions, and the temporary closure of businesses and facilities in China and worldwide.

Our results of operations have been, and could continue to be adversely, and may be materially, affected, to the extent that the COVID-19 or any other epidemic harms the Chinese and global economy in general. Any potential impact to our results will depend on, to a large extent, future developments and new information that may emerge regarding the duration and severity of the COVID-19 and the actions taken by government authorities and other entities to contain the COVID-19 or treat its impact, including the effectiveness of the vaccine programs, almost all of which are beyond our control. Potential impacts include, but are not limited to, the following:

- temporary closure of offices, travel restrictions or suspension of services of our customers and suppliers have negatively affected, and could continue to negatively affect, the demand for our services;
- our customers in industries that are negatively impacted by COVID-19, including healthcare, travel, offline education, franchising, auto/transportation and real estate/home furnishing sectors, may reduce their budgets on online advertising and marketing, which may materially adversely impact our revenue from online marketing services;
- our customers may require additional time to pay us or fail to pay us at all, which could significantly increase the amount of accounts receivable and require us to record additional allowances for doubtful accounts. We have provided and may continue to provide significant sales incentives to our customers and third-party agents during the pandemic, which may in turn materially adversely affect our financial condition and operating results;
- the business operations of our third-party agents have been and could continue to be negatively impacted by the pandemic, which may negatively impact our distribution channel, or result in loss of customers or disruption of our services, which may in turn materially adversely affect our financial condition and operating results;

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- any disruption of our supply chain, logistics providers or customers could adversely impact our business and results of operations, including causing us or our suppliers to cease manufacturing Xiaodu smart devices for a period of time or materially delay delivery to customers, which may also lead to loss of customers, as well as reputational, competitive and business harm to us;
- many of our customers, third-party agents, suppliers and other partners are small and medium-sized enterprises (SMEs), which may not have strong cash flows or be well capitalized, and may be vulnerable to a pandemic and slowing macroeconomic conditions. If the SMEs that we work with cannot weather COVID-19 and the resulting economic impact, or cannot resume business as usual after a prolonged pandemic, our revenues and business operations may be materially and adversely impacted;
- the global stock markets have experienced, and may continue to experience, significant decline from the COVID-19 pandemic and the private and public companies that we have invested in could be materially adversely affected, which may lead to significant impairment in the fair values of our investments and in turn materially adversely affect our financial condition and operating results; and
- corporate social responsibility initiatives we put forth in response to COVID-19, such as the RMB300 million charitable initiative with the goal of providing awareness education and improving public health in China, and many other efforts to leverage our technology, products and services to help contain the pandemic, may negatively affect our financial condition and operating results.

The potential downturn brought by and the duration of the COVID-19 pandemic may be difficult to assess or predict where actual effects will depend on many factors beyond our control. The extent to which the COVID-19 pandemic impacts our long-term results remains uncertain, and we are closely monitoring its impact on us. During the year ended December 31, 2020, our operations have been significantly affected by the COVID-19 pandemic. Our online marketing revenues declined compared to the prior period mainly due to weakness in online advertising demand as our customers in certain industries are negatively impacted by COVID-19. We have also provided additional allowance for credit losses for accounts receivable and contract assets, recognized impairment charges on our long-term investments and content assets, and recorded loss from equity method investments in 2020, due to the impact of COVID-19 and other factors. In addition, increased market volatility has contributed to larger fluctuations in the valuation of our equity investments. There are still significant uncertainties of COVID-19’s future impact, and the extent of the impact will depend on a number of factors, including the duration and severity of COVID-19, possibility of a second wave in China and other countries, the development of the vaccine and other medical treatment, the actions taken by government authorities to contain the outbreak, and government stimulus measures, almost all of which are beyond our control. As a result, certain of our estimates and assumptions, including the allowance for credit losses, the valuation of certain debt and equity investments, long-term investments, content assets and long-lived assets subject to impairment assessments, require significant judgments and carry a higher degree of variabilities and volatilities that could result in material changes to our current estimates in future periods.

In general, our business could be adversely affected by the effects of epidemics, including, but not limited to, the COVID-19, avian influenza, severe acute respiratory syndrome (SARS), the influenza A virus, Ebola virus, severe weather conditions such as a snowstorm, flood or hazardous air pollution, or other outbreaks. In response to an epidemic, severe weather conditions, or other outbreaks, government and other organizations may adopt regulations and policies that could lead to severe disruption to our daily operations, including temporary closure of our offices and other facilities. These severe conditions may cause us and/or our partners to make internal adjustments, including but not limited to,

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temporarily closing down business, limiting business hours, and setting restrictions on travel and/or visits with clients and partners for a prolonged period of time. Various impact arising from a severe condition may cause business disruption, resulting in material, adverse impact to our financial condition and results of operations.

Risks Related to Our Corporate Structure

PRC laws and regulations governing our businesses and the validity of certain of our contractual arrangements are uncertain. If we are found to be in violation, we could be subject to sanctions. In addition, changes in PRC laws and regulations or changes in interpretations thereof may materially and adversely affect our business.

The PRC government restricts or imposes conditions on foreign investment in various industries such as internet content, value-added telecommunication-based online marketing, audio and video services and mobile application distribution businesses. We and our PRC subsidiaries are still considered foreign persons or foreign-invested enterprises under PRC foreign investment related laws. As a result, we and our PRC subsidiaries are subject to PRC legal restrictions on or conditions for foreign ownership of internet content, value-added telecommunication-based online marketing, audio and video services and mobile application distribution businesses. Due to these restrictions and conditions, we operate our platform and conduct business in certain restricted or prohibited industries such as value-added telecommunication-based online marketing, audio and video services and mobile application distribution businesses in China through our consolidated affiliated entities. As all the nominee shareholders of our consolidated affiliated entities are either PRC citizens or PRC domestic enterprises, these entities are therefore considered as PRC domestic enterprises under PRC law. The “nominee shareholders” refer to those shareholders who have entered into exclusive equity purchase and transfer option agreements and equity pledge agreements with us as part of the contractual arrangements. Our contractual arrangements with our consolidated affiliated entities and the nominee shareholders allow us to have the power to direct the activities of these entities that most significantly impact their economic performance. These contractual arrangements demonstrate our ability and intention to continue to exercise the ability to absorb losses or receive economic benefits that could potentially be significant to the consolidated affiliated entities. In 2018, 2019 and 2020, we derived 33%, 40% and 43% of our external revenues from our consolidated affiliated entities, respectively.

There are substantial uncertainties regarding the interpretation and application of PRC laws and regulations, including, but not limited to, the laws and regulations governing our business, or the enforcement and performance of our contractual arrangements with our consolidated affiliated entities, including but not limited to Baidu Netcom and the nominee shareholders. These laws and regulations may be subject to change, and their official interpretation and enforcement may involve substantial uncertainty. New laws and regulations that affect existing and proposed future businesses may also be applied retroactively. Due to the uncertainty and complexity of the regulatory environment, we cannot assure you that we would always be in full compliance with applicable laws and regulations, the violation of which may have adverse effect on our business and our reputation.

Although we believe we comply with current PRC laws and regulations, we cannot assure you that the PRC government would agree that our contractual arrangements comply with PRC licensing, registration or other regulatory requirements, with existing policies or with requirements or policies that may be adopted in the future. The PRC government has broad discretion in determining rectifiable or punitive measures for non-compliance with or violations of PRC laws and regulations. If the PRC government determines that we do not comply with applicable law, it could revoke our business and operating licenses, require us to discontinue or restrict our operations, restrict our right to collect

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revenues, block our websites, require us to restructure our operations, impose additional conditions or requirements with which we may not be able to comply, impose restrictions on our business operations or on our customers, or take other regulatory or enforcement actions against us that could be harmful to our business. Any of these or similar occurrences could significantly disrupt our business operations or restrict us from conducting a substantial portion of our business operations, which could materially and adversely affect our business, financial condition and results of operations. If any of these occurrences results in our inability to direct the activities of any of our consolidated affiliated entities that most significantly impact its economic performance, and/or our failure to receive the economic benefits from any of our consolidated affiliated entities, we may not be able to consolidate these entities in our consolidated financial statements in accordance with U.S. GAAP.

Our contractual arrangements with our consolidated affiliated entities in China and the individual nominee shareholders may not be as effective in providing control over these entities as direct ownership.

Since PRC law restricts or imposes conditions on foreign equity ownership in the internet sector, value-added telecommunication-based online marketing, online audio and video services and mobile application distribution companies in China, we operate our platform and conduct our value-added telecommunication-based online marketing, online audio and video services and mobile app distribution businesses through our consolidated affiliated entities in China. We have no equity interest in any of these entities and must rely on contractual arrangements to control and operate the businesses and assets held by our consolidated affiliated entities, including the domain names and trademarks that have been transferred from our subsidiaries to our consolidated affiliated entities in accordance with requirements of PRC law. These contractual arrangements may not be as effective in providing control over these entities as direct ownership. For example, our consolidated affiliated entities and the individual nominee shareholders could breach their contractual arrangements with us by, among other things, failing to operate our business, such as using the domain names and trademarks our subsidiaries have transferred to them or maintaining our platform, in an acceptable manner or taking other actions that are detrimental to our interests. If our consolidated affiliated entities or the individual nominee shareholders fail to perform their obligations under these contractual arrangements, we may have to incur substantial costs to enforce such arrangements, and rely on legal remedies under PRC law, including contract remedies, which may not be sufficient or effective. If we are unable to enforce these contractual arrangements, or if we suffer significant delay or other obstacles in the process of enforcing these contractual arrangements, we may not be able to have the power to direct the activities that most significantly affect the economic performance of our consolidated affiliated entities, and we may lose control over the assets owned by our consolidated affiliated entities, including our *Baidu.com* domain name and website, and any other domain names and websites we have access to may not attract a large number of users and customers at the same level as *Baidu.com*. As a result, our ability to conduct our business may be materially and adversely affected, and we may not be able to consolidate the financial results of the relevant affiliated entities into our consolidated financial statements in accordance with U.S. GAAP, which may materially and adversely affect our results of operations and damage our reputation.

Our contractual arrangements with our consolidated affiliated entities in China may result in adverse tax consequences to us.

As a result of our corporate structure and the contractual arrangements between our subsidiaries and each of our consolidated affiliated entities in China, we would be subject to adverse tax consequences if the PRC tax authorities were to determine that the contracts between our subsidiaries and these consolidated affiliated entities were not on an arm’s-length basis and therefore constituted a favorable

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transfer pricing. Under the PRC Enterprise Income Tax Law, or the EIT Law, an enterprise must submit its annual tax return together with information on related-party transactions to the PRC tax authorities. The PRC tax authorities may impose reasonable adjustments on taxation if they have identified any related party transactions that are inconsistent with arm’s-length principles. For example, the PRC tax authorities could request that our consolidated affiliated entities adjust their taxable income upward for PRC tax purposes. Such adjustment could adversely affect us by increasing our consolidated affiliated entities’ tax expenses without reducing our subsidiaries’ tax expenses, which could subject our consolidated affiliated entities to interest due on late payments and other penalties for under-payment of taxes.

We may have exposure to greater than anticipated tax liabilities.

We are subject to enterprise income tax, or EIT, VAT, and other taxes in many provinces and cities in China and our tax structure is subject to review by various local tax authorities. The determination of our provision for income tax and other tax liabilities requires significant judgment. In the ordinary course of our business, there are many transactions and calculations where the ultimate tax determination is uncertain. For example, if our P4P service is classified as a form of advertisement distribution service, we may be required to pay a cultural business construction fee. See “Financial Information—Taxation—PRC VAT in Lieu of Business Tax.” In addition, if this classification of P4P services were to be retroactively applied, we might be subject to sanctions, including payment of delinquent fees and fines for the revenues generated from our P4P services prior to the classification. Moreover, under the EIT Law, the PRC tax authorities may impose reasonable adjustments on taxation if they have identified any related party transactions that are inconsistent with arm’s-length principles. Particularly, pursuant to the Administrative Measures for Special Tax Adjustment and Investigation and Mutual Consultation Procedures issued by the State Administration of Tax in March 2017, if a PRC enterprise makes an outbound payment to its overseas related party which undertakes no functions, bears no risks or has no substantial operation or activities and such payment is inconsistent with arm’s-length principles, the tax authorities may carry out a special tax adjustment based on the full amount deducted prior to tax. Although we believe all our related party transactions, including all payments by our PRC subsidiaries and consolidated affiliated entities to our non-PRC entities, are made on an arm’s-length basis and our estimates are reasonable, the ultimate decisions by the relevant tax authorities may differ from the amounts recorded in our financial statements and may materially affect our financial results in the period or periods for which such determination is made.

The individual nominee shareholders of our consolidated affiliated entities may have potential conflicts of interest with us, which may adversely affect our business. We do not have any arrangements in place to address such potential conflicts.

We have designated individuals who are PRC nationals to be the nominee shareholders of our consolidated affiliated entities in China. For example, Robin Yanhong Li, our chairman, chief executive officer and co-founder, is also the principal nominee shareholder of Baidu Netcom, which is our principal consolidated affiliated entity.

Although the individual nominee shareholders are contractually obligated to act in good faith and in our best interest, they may still have potential conflicts of interest with us. For example, some individual nominee shareholders of our consolidated affiliated entities do not have a significant equity stake in our company other than the share options granted to them. We cannot assure you that when conflicts of interest arise, any or all of these individuals will act in the best interests of our company or such conflicts will be resolved in our favor. In addition, these individuals may breach, cause our consolidated affiliated entities to breach or refuse to renew, the existing contractual arrangements with

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us. Currently, we do not have any arrangements to address potential conflicts of interest between these individuals and our company, except that we could exercise our transfer option under the exclusive equity purchase and transfer option agreement with the relevant individual nominee shareholder to request him/her to transfer all of his/her equity ownership in the relevant consolidated affiliated entity to a PRC entity or individual designated by us. We rely on Mr. Robin Yanhong Li, who is also a director of our company, to abide by the Cayman Islands law, which provides that directors owe a fiduciary duty to the company, and those who are also directors or officers of our PRC subsidiaries to abide by PRC law, which provides that directors and officers owe a fiduciary duty to the company. Such fiduciary duty requires directors and/or officers to act in good faith and in the best interests of the company and not to use their positions for personal gains. There are, however, no specific provisions under the Cayman Islands or PRC law on how to address potential conflicts of interest. If we cannot resolve any conflict of interest or dispute between us and the individual nominee shareholders of our consolidated affiliated entities, we would have to rely on legal proceedings, which could disrupt our business, distract management and subject us to substantial uncertainty as to the outcome of any such legal proceedings.

We may be unable to collect long-term loans to the nominee shareholders of our consolidated affiliated entities in China.

As of the December 31, 2020, we have made long-term loans in an aggregate principal amount of RMB19.1 billion (US\$2.9 billion) to the nominee shareholders of our consolidated affiliated entities. We extended these loans to enable the nominee shareholders to fund the capitalization of these entities. We may in the future provide additional loans to the nominee shareholders of our consolidated affiliated entities in China in connection with any increase in their capitalization to the extent necessary and permissible under applicable law. Our ability to ultimately collect these loans will depend on the profitability of these consolidated affiliated entities and their operational needs, which are uncertain.

We are in the process of registering the pledges of equity interests by nominee shareholders of some of our consolidated affiliated entities, and we may not be able to enforce the equity pledges against any third parties who acquire the equity interests in good faith in the relevant consolidated affiliated entities before the pledges are registered.

Pursuant to equity pledge agreements under the contractual arrangements, the nominee shareholders of each of our consolidated affiliated entities should pledge all of their equity interests in the relevant consolidated affiliated entities to our subsidiaries. An equity pledge agreement becomes effective among the parties upon execution. However, according to the Civil Code which became effective from January 1, 2021, an equity pledge is not perfected as a security property right unless it is registered with the relevant local administration for market regulation. We are still in the process of registering the pledge relating to certain consolidated affiliated entitie(s), relating to recent equity interest transfers and capital increase. Prior to the completion of the registration, we may not be able to successfully enforce the equity pledge against any third parties who have acquired property right interests in good faith in the equity interests in the relevant consolidated affiliated entitie(s).

If the chops of our PRC subsidiaries and our VIEs are not kept safely, are stolen or are used by unauthorized persons or for unauthorized purposes, the corporate governance of these entities could be severely and adversely compromised.

In China, a company chop or seal serves as the legal representation of the company towards third parties even when unaccompanied by a signature. Each legally registered company in China is required to maintain a company chop, which must be registered with the local Public Security Bureau. In

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addition to this mandatory company chop, companies may have several other chops which can be used for specific purposes. The chops of our PRC subsidiaries and VIEs are generally held securely by personnel designated or approved by us in accordance with our internal control procedures. To the extent those chops are not kept safely, are stolen or are used by unauthorized persons or for unauthorized purposes, the corporate governance of these entities could be severely and adversely compromised and those corporate entities may be bound to abide by the terms of any documents so chopped, even if they were chopped by an individual who lacked the requisite power and authority to do so. In addition, if the chops are misused by unauthorized persons, we could experience disruption to our normal business operations. We may have to take corporate or legal action, which could involve significant time and resources to resolve while distracting management from our operations.

Risks Related to Doing Business in China

Changes in China’s economic, political or social conditions or government policies could have a material and adverse effect on our business and operations.

Most of our business operations are conducted in China. Accordingly, our business, results of operations, financial condition and prospects are affected by economic, political and social conditions in China generally and by continued economic growth in China as a whole.

China’s economy differs from the economies of most developed countries in many respects, including the extent of government involvement, level of development, growth rate, control of foreign exchange and allocation of resources. Although the Chinese government has implemented measures emphasizing the utilization of market forces for economic reform, the reduction of state ownership of productive assets, and the establishment of improved corporate governance in business enterprises, a substantial portion of productive assets in China is still owned by the government. In addition, the Chinese government continues to play a significant role in regulating industry development. The Chinese government also exercises significant control over China’s economic growth through allocating resources, controlling payment of foreign currency-denominated obligations, setting monetary policy, and providing preferential treatment to particular industries or companies.

Growth of China’s economy has been uneven, both geographically and among various sectors of the economy, and the growth of the Chinese economy has slowed down in recent years. Some of the government measures may benefit the overall Chinese economy, but may have a negative effect on us. For example, our financial condition and results of operations may be adversely affected by government control over capital investments or changes in tax regulations. Any stimulus measures designed to boost the Chinese economy may contribute to higher inflation, which could adversely affect our results of operations and financial condition. For example, certain operating costs and expenses, such as employee compensation and office operating expenses, may increase as a result of higher inflation. Additionally, because a substantial portion of our assets consists of cash and cash equivalents and short-term investments, high inflation could significantly reduce the value and purchasing power of these assets.

Uncertainties with respect to the PRC legal system could adversely affect us.

We conduct our business primarily through our subsidiaries and consolidated affiliated entities in China. Our operations in China are governed by PRC laws and regulations. Our subsidiaries are generally subject to laws and regulations applicable to foreign investments in China. The PRC legal system is based on written statutes. Prior court decisions may be cited for reference but have limited precedential value.

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PRC laws and regulations have significantly enhanced the protections afforded to various forms of foreign investments in China for the past decades. However, China has not developed a fully integrated legal system and recently enacted laws and regulations may not sufficiently cover all aspects of economic activities in China. In particular, because these laws and regulations are relatively new, and because of the limited volume of published decisions and their nonbinding nature, the interpretation and enforcement of these laws and regulations involve uncertainties.

Furthermore, the PRC legal system is based in part on government policies and internal rules, some of which are not published on a timely basis or at all. As a result, we may not be aware of our potential violation of these policies and rules. In addition, any administrative and court proceedings in China may be protracted and result in substantial costs and diversion of resources and management attention.

We may be adversely affected by the complexity, uncertainties and changes in PRC regulations of internet and related business and companies.

The PRC government regulates the internet and related industry extensively, including foreign ownership of, and the licensing and permit requirements pertaining to, companies in the internet industry. These internet-related laws and regulations are relatively new and evolving, and their interpretation and enforcement involve significant uncertainty. As a result, under certain circumstances it may be difficult to determine what actions or omissions may be deemed to be violations of applicable laws and regulations. Issues, risks and uncertainties relating to PRC government regulation of the internet industry include, but are not limited to, the following:

- We only have contractual control over our websites. We do not own the websites due to the restriction of foreign investment in businesses providing value-added telecommunications services in China, including online information services.
- The licensing requirements relating to the internet business in China are uncertain and evolving. This means that permits, licenses or operations at some of our PRC subsidiaries and consolidated affiliated entities may be subject to challenge, or we may not be able to obtain or renew certain permits or licenses, including without limitation, a Value-Added Telecommunication Business Operating License, which is issued by the MIIT, an Internet News License, which is issued by the Cyberspace Administration of China, or the CAC, a Short Messaging Service Access Code Certificate, which is issued by the MIIT, an Online Audio/Video Program Transmission License, which is issued by the State Administration of Press Publication, Radio, Film and Television, or the SAPPRFT (the corresponding regulatory body currently known as National Radio and Television Administration, or the NRTA), a Radio and Television Program Production License, which is issued by the local bureau of the NRTA, a Surveying and Mapping Qualification Certificate for internet map services, which is issued by the National Administration of Surveying, Mapping and Geo-information, an Internet Culture Business Permit with or without the permitted scope of business covering online game operation and online game virtual currency issuance or trading, which is issued by the local bureau of the then Ministry of Culture, or the Ministry of Culture and Tourism which has replaced the Ministry of Culture, an Internet Publication Service License, which is issued by the SAPPRFT (the corresponding regulatory body currently known as the National Press and Publication Administration, or the NPPA), a Publication Business Operating License, which is issued by the local bureau of the SAPPRFT or NPPA, a Qualification Certificate for Internet Drug Information Services, which is issued by provincial branch of the State Food and Drug Administration (the corresponding regulatory body currently known as the National Medical Products Administration), a Human Resource Services License, which is issued by the local bureau of the Ministry of Human Resources and Social Security, and a Commercial Performances License, which is issued by the Municipal Bureau of Culture and Tourism. Failure

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to obtain or renew these permits and licenses may significantly disrupt our business, or subject us to sanctions, requirements to increase capital or other conditions or enforcement, or compromise enforceability of related contractual arrangements, or have other harmful effects on us.

- New laws and regulations may be promulgated to regulate internet activities, including online advertising and internet cultural activities. Other aspects of our online operations may be further regulated in the future. If these new laws and regulations are promulgated, additional licenses may be required for our online operations. If our operations do not comply with these new regulations at the time they become effective, or if we fail to obtain any licenses required under these new laws and regulations, we could be subject to penalties.

We provide value-added telecommunications services through our consolidated affiliated entities, which hold the required licenses. In July 2006, the MIIT issued the Notice of the Ministry of Industry and Information Technology on Intensifying the Administration of Foreign Investment in Value-Added Telecommunications Services. This notice prohibits domestic telecommunication service providers from leasing, transferring or selling telecommunication business operating licenses to any foreign investor in any form, or providing any resources, sites or facilities to any foreign investor for their illegal operation of a telecommunication business in China. According to this notice, either the holder of a Value-Added Telecommunication Business Operating License or its shareholders must directly own the domain names and trademarks used by the license holder in its provision of value-added telecommunications services. Our major consolidated affiliated entities hold the necessary assets that are material to the operation of our business, including domain names, personnel, facilities and most of our intellectual property rights.

As we enter into new businesses, we may encounter additional regulatory uncertainties. For example, the current PRC legal framework on autonomous cars or autonomous driving is still new and evolving. Pursuant to the local rules and regulations in various cities including Beijing, Shanghai, Chongqing, and other cities, any entity intending to conduct a road testing of autonomous driving vehicles in these cities must file an application for road testing with a designated local agency supervising road testing of autonomous vehicles in these cities. It also remains uncertain what additional compliance requirements we need to meet in order to undertake a road testing of our autonomous driving cars in other locations in China. Baidu has obtained permits to conduct road testing in certain cities such as Beijing, Guangzhou, Yangquan, Shanghai, Yinchuan, Nanjing and Hefei. There is no guarantee that the road testing of our autonomous driving cars in other locations fully complies with local laws and regulations. If our road testing is deemed by local enforcement authority as a violation of the applicable traffic and transportation laws, we may have to suspend the testing, and the progress of our research and development of autonomous cars may be adversely affected.

The interpretation and application of existing PRC laws, regulations and policies and possible new laws, regulations or policies relating to the internet industry have created substantial uncertainties regarding the legality of existing and future foreign investments in, and the businesses and activities of, internet businesses in China, including our business.

Any failure or perceived failure by us to comply with the enacted Anti-Monopoly Guidelines for Internet Platforms and other anti-monopoly laws and regulations may result in governmental investigations or enforcement actions, litigation or claims against us and could have an adverse effect on our business, financial condition and results of operations.

The PRC anti-monopoly enforcement agencies have in recent years strengthened enforcement under the PRC Anti-monopoly Law. In March 2018, the SAMR was formed as a new governmental agency

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to take over, among other things, the anti-monopoly enforcement functions from the relevant departments under the MOFCOM, the NDRC and the SAIC, respectively. Since its inception, the SAMR has continued to strengthen anti-monopoly enforcement. On December 28, 2018, the SAMR issued the Notice on Anti-monopoly Enforcement Authorization, which grants authorities to its province-level branches to conduct anti-monopoly enforcement within their respective jurisdictions. On September 11, 2020, the SAMR issued Anti-monopoly Compliance Guideline for Operators, which requires, under the PRC Anti-monopoly Law, operators to establish anti-monopoly compliance management systems to prevent anti-monopoly compliance risks. On February 7, 2021, the Anti-monopoly Commission of the State Council officially promulgated the Anti-Monopoly Guidelines for Internet Platforms. Pursuant to an official interpretation from the Anti-monopoly Commission of the State Council, the Anti-Monopoly Guidelines for Internet Platforms mainly covers five aspects, including general provisions, monopoly agreements, abusing market dominance, concentration of undertakings, and abusing of administrative powers eliminating or restricting competition. The Anti-Monopoly Guidelines for Internet Platforms prohibits certain monopolistic acts of internet platforms so as to protect market competition and safeguard interests of users and undertakings participating in internet platform economy, including without limitation, prohibiting platforms with dominant position from abusing their market dominance (such as discriminating customers in terms of pricing and other transactional conditions using big data and analytics, coercing counterparties into exclusivity arrangements, using technology means to block competitors' interface, favorable positioning in search results of goods displays, using bundle services to sell services or products, compulsory collection of unnecessary user data). In addition, the Anti-Monopoly Guidelines for Internet Platforms also reinforces antitrust merger review for internet platform related transactions to safeguard market competition. As the Anti-Monopoly Guidelines for Internet Platforms was newly promulgated, we are uncertain to estimate its specific impact on our business, financial condition, results of operations and prospects. We cannot assure you that our business operations comply with such regulations and authorities' requirements in all respects. If any non-compliance is raised by relevant authorities and determined against us, we may be subject to fines and other penalties.

To our knowledge, a certain number of PRC Internet companies adopt VIE structure, but there have been few precedents where Internet companies with a VIE structure were investigated for being involved in the concentrations of undertaking until recently. It has been long debated whether transactions involving Internet companies with a VIE structure are subject to prior filing of notification requirements, since filing of notification of concentration of undertaking made by couples of Internet companies were not accepted in the past. Due to such regulatory history in the industry and as a matter of common industry practice in the past, we did not file prior notification of concentrations of undertaking. In April 2020, the SAMR published a case of concentration of undertaking where a VIE structure was involved (such case was closed in July 2020 and unconditional approval was granted). In November 2020, the draft Guidelines to Anti-Monopoly in the Field of Internet Platforms also, for the first time, expressly include concentrations involving a VIE structure within the ambit of SAMR's merger control review if the reporting thresholds are triggered. Furthermore, in December 2020, SAMR has, for the first time, formally penalized three Internet companies with a VIE structure for failure to file prior notifications of implementing concentrations. Hence, starting from 2020, SAMR has been reviewing historical cases of concentrations of undertaking of Internet companies with a VIE structure, and past failure to file prior notification of concentrations of undertaking may be investigated and penalized.

We have received enquiry from the SAMR related to failure to file prior notification of concentrations of undertaking and the possibility of penalty. Relevant cases are still under investigation. We have been cooperating with SAMR and we keep written and oral correspondence with SAMR. In January

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2021, we received one official case-filing notification in connection with one case, which required us to provide relevant materials and statements on whether the non-filing constitutes a failure to file prior notification of concentrations of undertaking. We have been cooperating with SAMR and providing the requested documents and information. Recently we received a notification from the SAMR contemplating the imposition of a fine of RMB500,000 in connection with this case. The SAMR will issue an official notice imposing the penalty if no objection was raised within three business days. We did not object to the penalty. We do not expect further penalty from the SAMR in connection with this case after we make full payment of the penalty. There can be no assurance that such enquiry can be resolved in a timely manner to the SAMR’s satisfaction, or that we will not be subject to more enquiries in the future. We may be subject to penalty in connection with any such enquiry, including certain fines up to RMB500,000 per case, and in extreme case being order to terminate the contemplated concentration, to dispose of our equity or asset within a prescribed period, to transfer our business within a prescribed time or to take any other necessary measures to return to the pre-concentration status. We may receive greater scrutiny and attention from regulators and more frequent and rigid investigation or review by regulators, which will increase our compliance costs and subject us to heightened risks and challenges. We may have to spend much more personnel cost and time evaluating and managing these risks and challenges in connection with our products and services as well as our investments in our ordinary business course to avoid any failure to comply with these regulations. Any failure or perceived failure by us to comply with the enacted Anti-Monopoly Guidelines for Internet Platforms and other anti-monopoly laws and regulations may result in governmental investigations or enforcement actions, litigations or claims against us and could have an adverse effect on our business, financial condition and results of operations.

We are subject to governmental economic sanctions or export control laws.

We are subject to 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 U.S. sanctions. United Kingdom financial sanctions and European Union sanctions also have similar regime to prohibit the provision of products and services to countries, governments and persons on their respective target list.

In August 2020, MOFCOM and the Ministry of Technology jointly promulgated a notice to adjust and pronounce the Catalog of Technologies Prohibited or Restricted from Export of the PRC, which has provided that certain technologies on interactive interface of AI (including voice recognition, microphone array, voice wake-up and interactive understanding) could be restricted for export from the PRC without approval. According to the Administrative Measures on the Import and Export of Technologies of the PRC, which was recently revised by the State Council in November 2020, if we would like to conduct any type of cross-border technology service or cooperation involving certain AI technologies which are or may be (subject to determination by the relevant governmental authority) restricted from export, we would be required to apply for approval from the provincial competent commercial department before entering into any substantial stage of negotiation or execution of any technology export contract. If and after such contract is executed, we shall apply for an export certificate and such contract would only come into effect after the competent commercial department has granted us the permit. Such process may be time consuming and there is no guarantee that such permit would always be granted, which could negatively affect our potential cross-border technology service or cooperation.

While we believe that we have been, and that we continue to be, in compliance with applicable governmental economic sanctions or export control laws, our failure to employ appropriate safeguards with respect to users located in countries that are targets of governmental economic sanctions or export

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control may result in a violation of such laws and regulations. Non-compliance with applicable governmental economic sanctions or export control laws could subject us to adverse media coverage, investigations, severe administrative, civil and possibly criminal sanctions, and expenses related to remedial measures and legal expenses, which could materially and adversely affect our reputation, business, financial condition, results of operations and prospects.

There are uncertainties associated with PRC laws and regulations on virtual assets, and therefore it is not clear what liabilities, if any, we may have relating to the loss of virtual assets by our users.

While participating on our platform, our users may acquire, purchase and accumulate certain virtual assets, such as gifts or certain statuses and privileges. Such virtual assets can be important to users and have monetary value and, in some cases, can be cashed to actual money. However, virtual assets may become lost for various reasons, often through unauthorized use of the account of one user by other users and occasionally through data loss caused by delays in network service, network crashes or hacking activities. Currently, there are uncertainties associated with PRC laws and regulations on virtual assets. As a result, uncertainties still exist as to who the legal owner of virtual assets is, whether and how the ownership of virtual assets is protected by law, and whether an operator of a platform would have any liability, whether in contract, tort or otherwise, to users or other interested parties, for loss of such virtual assets. Some recent PRC court judgments ordered certain online platform operators liable for losses of virtual assets by platform users, and have ordered online platform operators to restore the lost virtual items to users or pay damages and losses. In case of a loss of virtual assets, we may be sued by our users and held liable for losses, which may negatively affect our reputation, business, financial condition, results of operations and prospects. We have been involved in virtual items related lawsuits in the past, and we cannot assure you that such lawsuits will not be brought against us again in the future.

Uncertainties exist with respect to the interpretation and implementation of the new PRC Foreign Investment Law and its Implementation Regulations and how it may impact the viability of our current corporate structure, corporate governance and business operations.

On January 1, 2020, the Foreign Investment Law and the Regulations for Implementation of the Foreign Investment Law of the People’s Republic of China, or the Implementation Regulations, came into effect and replaced the trio of prior laws regulating foreign investment in 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 and the Implementation Regulations embody an expected PRC 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 they are relatively new, uncertainties still exist in relation to their 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 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

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requirements for foreign investment under the PRC 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.

If any of our VIEs would be deemed as foreign invested enterprise under any such future laws, administrative regulations or provisions and any of our business would be included in any negative list or other form of restrictions on foreign investment, we may need to take further actions to comply with such future laws, administrative regulations or provisions. Such actions may have a material and adverse impact on our business, financial condition, result of operations and prospects. If we or any of our VIEs is found to be in violation of any existing or future PRC laws, administrative regulations or provisions, or fail to obtain or maintain any of the required permits or approvals, the relevant PRC regulatory authorities would have broad discretion to take corresponding action regarding such violations or failures to such entities, such as:

- order to immediately terminate prohibited investment activities and to take certain measures to return to the pre-investment status;
- order to rectify within prescribed period and to take necessary measures to comply with such laws, administrative regulations or provisions;
- revocation of such entities’ business licenses and/or operating licenses;
- shutting down of our website, or discontinuance or restriction on any transactions between certain of our PRC subsidiaries with them;
- fines, confiscation of the income from our PRC subsidiaries or VIEs, or other requirements with which we or our VIEs may not be able to comply;
- order to restructure our ownership structure, corporate governance and business operations, including terminating the contractual arrangements with our VIEs and deregistering the equity pledges of our VIEs, which in turn would affect our ability to consolidate, derive economic interests from, or impose effective control over our VIEs; or
- restriction or prohibition on our use of the proceeds of any financing outside PRC to finance our business operations in PRC, and other regulatory or enforcement actions that could be harmful to our business.

Any of the above penalties may result in a material and adverse effect on our business operation. In addition, if the PRC regulatory authorities were to find our legal structure and contractual arrangements to be in violation of any PRC laws, administrative regulations or provisions, we are uncertain what impact of above PRC regulatory authorities’ actions would have on us and our ability to consolidate our VIEs in the consolidated financial statement. If any of these regulatory actions result in us losing our right to direct the activities of our VIEs or to receive substantially all the economic benefits and residual returns from our VIEs and we are not able to restructure our ownership structure and operations in a satisfactory manner, we would no longer be able to consolidate the financial results of our VIEs in the consolidated financial statements. Any of the above results, or any other significant unfavorable actions that might be imposed on us in this event, would have an adverse effect on our business, financial condition, results of operations and prospects. 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.

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It may be difficult for overseas regulators to conduct investigation or collect evidence within China.

Shareholder claims or regulatory investigation that are common in the United States generally are difficult to pursue as a matter of law or practicality in China. For example, in China, there are significant legal and other obstacles to providing information needed for regulatory investigations or litigation initiated outside China. Although the authorities in China may establish a regulatory cooperation mechanism with the securities regulatory authorities of another country or region to implement cross-border supervision and administration, such cooperation with the securities regulatory authorities in the United States may not be efficient in the absence of mutual and practical cooperation mechanism. Furthermore, according to Article 177 of the PRC Securities Law, or Article 177, which became effective in March 2020, no overseas securities regulator is allowed to directly conduct investigation or evidence collection activities within the territory of the PRC. While detailed interpretation of or implementation rules under Article 177 have yet to be promulgated, the inability for an overseas securities regulator to directly conduct investigation or evidence collection activities within China may further increase difficulties faced by you in protecting your interests. See also “—Risks Related to Our Shares, ADSs and the Listing—Certain judgments obtained against us by our shareholders may not be enforceable.” for risks associated with [REDACTED] in us as a Cayman Islands company.

We may be subject to liability for information displayed on or linked to our websites, mobile apps, Smart Mini Program or Managed Page and negative publicity in international media and our business may be adversely affected as a result.

The PRC government has adopted regulations governing internet access and distribution of news and other information over the internet. Under these regulations, internet content providers and internet publishers are prohibited from posting or displaying over the internet content that, among other things, violates PRC laws and regulations, impairs the national dignity of China, contains terrorism or extremism content, or is reactionary, obscene, superstitious, fraudulent or defamatory. Failure to comply with these requirements may result in the revocation of licenses to provide internet content and other licenses and the closure of the concerned websites. In the past, failure to comply with these requirements has resulted in the closure of certain websites. The website operator may also be held liable for the information displayed on or linked to the website or the mobile apps.

In particular, the MIIT has published regulations that subject website operators to potential liability for content displayed on their websites or mobile apps and the actions of users and others using their systems, including liability for violations of PRC laws and regulations prohibiting the dissemination of content deemed to be socially destabilizing. The Ministry of Public Security has the authority to order any local internet service provider to block any internet website at its sole discretion. From time to time, the Ministry of Public Security has stopped the dissemination over the internet of information which it believes to be socially destabilizing. The State Secrecy Bureau is also authorized to block any website it deems to be leaking state secrets or failing to meet the relevant regulations relating to the protection of state secrets in the dissemination of online information. Furthermore, we are required to report any suspicious content to relevant governmental authorities, and to undergo computer security inspections. If we fail to implement the relevant safeguards against security breaches, our websites may be shut down and our business and ICP licenses may be revoked. In addition, the CAC has, from time to time, also issued rules enhancing the internet service provider’s obligations to monitor information displayed on its information platform and prevent dissemination of illegal contents. See “Regulations—Regulations on Value-Added Telecommunications Services and Internet Content Services—Regulations on Content.”

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The Anti-Terrorism Law, which took effect on January 1, 2016 and was amended on April 27, 2018, further requires internet service providers to verify the identity of their users, and to not provide services to anyone whose identity is unclear or who declines verification. Although the identity verification requirements are already embodied in some internet related regulations, the Anti-Terrorism Law extends these requirements to all types of internet services. The internet service providers are also required to provide technical interfaces, decryption and other technical support and assistance for the competent departments to prevent and investigate terrorist activities. See “Regulations—Regulations on Information Security” for more details.

Although we attempt to monitor the content in our search results, mobile apps, online communities such as Baidu Post, Smart Mini Programs and Managed Page, we are not able to control or restrict the content of other internet content providers linked to or accessible through our websites, mobile apps, or content generated or placed on our Baidu Post message boards, mini programs, Managed Page, or our other online communities by our users. To the extent that PRC regulatory authorities find any content displayed on our websites or mobile apps illegal, they may require us to limit or eliminate the dissemination of such information on our websites or mobile apps. To the extent that PRC regulatory authorities find any content displayed on our websites or mobile apps objectionable, they may suggest that we limit or eliminate the dissemination of such information on our websites or mobile apps. If third-party websites linked to or accessible through our websites or mini programs accessible through our mobile apps conduct unlawful activities such as online gambling, PRC regulatory authorities may require us to report such unlawful activities to relevant authorities and to remove the links to such websites or mobile apps, or they may suspend or shut down the operation of these third-party websites. PRC regulatory authorities may also temporarily block access to certain websites or mobile apps for a period of time for reasons beyond our control. Any of these actions may reduce our user traffic and adversely affect our business. In addition, we have been and may be subject to penalties in the future for violations of those regulations arising from information displayed on or linked to our websites or mobile apps, including a suspension or shutdown of our online operations. For example, in April 2020, we were approached and inquired by the CAC with respect to the display and dissemination of vulgar contents and insufficient content monitoring on the public accounts on Baidu App. As a consequence, our Baidu App was ordered to suspend any updates for over two weeks before updates resumed to normal. Although we will make our best efforts to closely monitor and filter the contents displayed and disseminated on our Baidu App and other products, we cannot assure you that incidents of similar type would not take place in the future.

Moreover, our compliance with PRC regulations governing internet access and distribution of news and other information over the internet may subject us to negative publicity or even legal actions outside of China. In May 2011, eight New York residents filed a lawsuit against us before the U.S. District Court for the Southern District of New York accusing us of aiding Chinese censorship in violation of the U.S. Constitution. In March 2014, the U.S. District Court for the Southern District of New York granted our motion for judgment on the pleadings based upon the First Amendment to the U.S. Constitution and dismissed with prejudice the plaintiffs’ complaint in its entirety, barring the plaintiffs from bringing an appeal or action based on the same claim. Even though we have won the case, our reputation may continually be adversely affected among users and investors outside of China.

The discontinuation of any of the preferential income tax treatments currently available to us in the PRC could have a material and adverse effect on our result of operations and financial condition.

Pursuant to the EIT Law, as further clarified by subsequent tax regulations implementing the EIT Law, foreign-invested enterprises and domestic enterprises are subject to EIT at a uniform rate of 25%. Certain enterprises may benefit from a preferential tax rate of 15% under the EIT Law if they qualify

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as “High and New Technology Enterprises strongly supported by the state,” subject to certain general factors described in the EIT Law and the related regulations.

A number of our PRC subsidiaries and consolidated affiliated entities, such as Baidu Online Network Technology (Beijing) Co., Ltd., or Baidu Online, and Baidu Netcom are entitled to enjoy a preferential tax rate of 15% due to their qualification as “High and New Technology Enterprise,” which has a term of three years. If any or some of these PRC subsidiaries and consolidated affiliated entities fail to maintain the “High and New Technology Enterprise” qualification, their applicable EIT rate will increase to 25%. Furthermore, Baidu Online was entitled to a preferential income tax rate of 10% from 2010 to 2019 due to its “Key Software Enterprise” status, so was Baidu China for 2015 to 2019, and Baidu International Technology (Shenzhen) Co., Ltd., or Baidu International, for 2016 to 2019. Baidu Online, Baidu China and Baidu International will file with the local tax authority for the preferential tax rate of 10% for a “Key Software Enterprise” for 2020 before the end of May 2021, and will be subject to relevant governmental authorities’ assessment. However, there is no assurance that any of these entities will continue to enjoy the preferential tax rate as a “Key Software Enterprise.” See “Financial Information—Taxation—PRC Enterprise Income Tax.”

The discontinuation of any of the above-mentioned preferential income tax treatments currently available to us in the PRC could have a material and adverse effect on our result of operations and financial condition. We cannot assure you that we will be able to maintain our current effective tax rate in the future.

If our PRC subsidiaries declare and distribute dividends to their respective offshore parent companies, we will be required to pay more taxes, which could have a material and adverse effect on our result of operations.

Under the EIT Law and related regulations, dividends, interests, rent or royalties payable by a foreign-invested enterprise, such as our PRC subsidiaries, to any of its foreign non-resident enterprise investors, and proceeds from any such foreign enterprise investor’s disposition of assets (after deducting the net value of such assets) are subject to a 10% withholding tax, unless the foreign enterprise investor’s jurisdiction of incorporation has a tax treaty with China that provides for a reduced rate of withholding tax. Undistributed profits earned by foreign-invested enterprises prior to January 1, 2008 are exempted from any withholding tax. The British Virgin Islands, where Baidu Holdings Limited, the direct parent company of our PRC subsidiaries Baidu Online and Baidu International, is incorporated, does not have such a tax treaty with China. Hong Kong has a tax arrangement with China that provides for a 5% withholding tax on dividends subject to certain conditions and requirements, such as the requirement that the Hong Kong resident enterprise own at least 25% of the PRC enterprise distributing the dividend at all times within the 12-month period immediately preceding the distribution of dividends and be a “beneficial owner” of the dividends. For example, Baidu (Hong Kong) Limited, which directly owns our PRC subsidiaries Baidu China and Baidu Times, is incorporated in Hong Kong. However, if Baidu (Hong Kong) Limited is not considered to be a Hong Kong tax resident enterprise or the beneficial owner of dividends paid or to be paid to it by Baidu China and Baidu Times under the tax circulars promulgated in February 2009 and 2018, such dividends would be subject to withholding tax at a rate of 10%. See “Financial Information—Taxation—PRC Enterprise Income Tax.” If our PRC subsidiaries further declare and distribute profits earned after January 1, 2008 to us in the future, such payments will be subject to withholding tax, which will further increase our tax liability and reduce the amount of cash available to our company.

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We may be deemed a PRC resident enterprise under the EIT Law, which could subject us to PRC taxation on our global income, and which may have a material and adverse effect on our results of operations.

Under the EIT Law and related regulations, an enterprise established outside of the PRC with “de facto management body” within the PRC is considered a PRC resident enterprise and is subject to the EIT at the rate of 25% on its worldwide income as well as PRC EIT reporting obligations. The related regulations define the term “de facto management body” as “the establishment that exercises substantial and overall management and control over the production, business, personnel, accounts and properties of an enterprise.” The State Administration of Taxation issued SAT Circular 82 in April 2009, which provides certain specific criteria for determining whether the “de facto management body” of a Chinese-controlled overseas-incorporated enterprise is located in China. The State Administration of Taxation issued additional rules to provide more guidance on the implementation of SAT Circular 82 in July 2011, and issued an amendment to SAT Circular 82 delegating the authority to its provincial branches to determine whether a Chinese-controlled overseas-incorporated enterprise should be considered a PRC resident enterprise, in January 2014. See “Financial Information—Taxation—PRC Enterprise Income Tax.” Although the SAT Circular 82, the additional guidance and amendment apply only to overseas registered enterprises controlled by PRC enterprises, not to those controlled by PRC individuals or foreigners, the criteria set forth in SAT Circular 82 may reflect the State Administration of Taxation’s general position on how the “de facto management body” test should be applied in determining the tax resident status of offshore enterprises, regardless of whether they are controlled by PRC enterprises or individuals. If we are deemed a PRC resident enterprise, we may be subject to the EIT at 25% on our global income, except that the dividends we receive from our PRC subsidiaries may be exempt from the EIT to the extent such dividends are deemed as “dividends among qualified PRC resident enterprises.” If we are deemed a PRC resident enterprise and earn income other than dividends from our PRC subsidiaries, a 25% EIT on our global income could significantly increase our tax burden and materially and adversely affect our cash flow and profitability.

Under PRC tax laws, dividends payable by us and gains on the disposition of our shares or ADSs may be subject to PRC taxation.

If we are considered a PRC resident enterprise under the EIT Law, our shareholders and ADS holders who are deemed non-resident enterprises may be subject to the EIT at the rate of 10% upon the dividends payable by us or upon any gains realized from the transfer of our shares or ADSs, if such income is deemed derived from China, provided that (i) such foreign enterprise investor has no establishment or premises in China, or (ii) it has establishment or premises in China but its income derived from China has no real connection with such establishment or premises. If we are required under the EIT Law to withhold PRC income tax on our dividends payable to our non-PRC resident enterprise shareholders and ADS holders, or if any gains realized from the transfer of our shares or ADSs by our non-PRC resident enterprise shareholders and ADS holders are subject to the EIT, your [REDACTED] in our shares or ADSs could be materially and adversely affected.

Furthermore, if we are considered a PRC resident enterprise and relevant PRC tax authorities consider dividends we pay with respect to our shares or ADSs and the gains realized from the transfer of our shares or ADSs to be income derived from sources within the PRC, it is possible that such dividends and gains earned by non-resident individuals may be subject to PRC individual income tax at a rate of 20%. If we are required under PRC tax laws to withhold PRC income tax on dividends payable to our non-PRC investors that are non-resident individuals or if you are required to pay PRC income tax on the transfer of our shares or ADSs, the value of your [REDACTED] in our shares or ADSs may be materially and adversely affected.

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Our subsidiaries and consolidated affiliated entities in China are subject to restrictions on paying dividends and making other payments to our holding company.

Baidu, Inc. is our holding company incorporated in the Cayman Islands. As a result of the holding company structure, it currently relies on dividend payments from our subsidiaries in China. However, PRC regulations currently permit payment of dividends only out of accumulated profits, as determined in accordance with PRC accounting standards and regulations. Our subsidiaries and consolidated affiliated entities in China are also required to set aside a portion of their after-tax profits according to PRC accounting standards and regulations to fund certain reserve funds. The PRC government also imposes controls on the conversion of RMB into foreign currencies and the remittance of foreign currencies out of China. We may experience difficulties in completing the administrative procedures necessary to obtain and remit foreign currency. See “—Governmental control of currency conversion may affect the value of your [REDACTED].” Furthermore, if our subsidiaries or consolidated affiliated entities in China incur debt on their own in the future, the instruments governing the debt may restrict their ability to pay dividends or make other payments. If our subsidiaries and consolidated affiliated entities in China are unable to pay dividends or make other payments to us, we may be unable to pay dividends on our ordinary shares and ADSs.

Governmental control of currency conversion may affect the value of your [REDACTED].

The PRC government imposes controls on the convertibility of RMB into foreign currencies and, in certain cases, the remittance of foreign currency out of China. We receive most of our revenues in RMB. Under our current structure, our income at the Cayman Islands holding company level will primarily be derived from dividend payments from our PRC subsidiaries. Shortages in the availability of foreign currency may restrict the ability of our PRC subsidiaries and consolidated affiliated entities to remit sufficient foreign currency to pay dividends or other payments to us, or otherwise satisfy their foreign currency denominated obligations. Under existing PRC foreign exchange regulations, payments of current account items, including profit distributions, interest payments and expenditures from trade-related transactions, can be made in foreign currencies without prior approval from the State Administration of Foreign Exchange, or SAFE, by complying with certain procedural requirements. However, approval from appropriate government authorities is required where RMB 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 also at its discretion restrict access in the future to foreign currencies for current account transactions. If the foreign exchange control system prevents us from obtaining sufficient foreign currency to satisfy our currency demands, we may not be able to pay dividends in foreign currencies to our shareholders or ADS holders.

PRC regulation of loans to and direct investment in PRC entities by offshore holding companies and governmental control of currency conversion may delay or prevent us from making loans to our PRC subsidiaries, consolidated affiliated entities and certain related parties, or making additional capital contributions to our PRC subsidiaries, which could adversely affect our ability to fund and expand our business.

Baidu, Inc. is our offshore holding company conducting operations in China through our PRC subsidiaries and consolidated affiliated entities. We may make loans to our PRC subsidiaries and consolidated affiliated entities, or we may make additional capital contributions to our PRC subsidiaries. Loans by Baidu, Inc. or any of our offshore subsidiaries to our PRC subsidiaries, which are treated as foreign-invested enterprises under PRC law, or to our consolidated affiliated entities are subject to PRC regulations and foreign exchange loan registrations. Such loans to any of our PRC

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subsidiaries and consolidated affiliated entities to finance their activities cannot exceed a statutory upper limit and must be filed with SAFE through the online filing system of SAFE pursuant to the applicable PRC regulations. We may also decide to finance our PRC subsidiaries by means of capital contributions, in which case the PRC subsidiary is required to register the details of the capital contribution with the local branch of SAMR and submit a report on the capital contribution via the online enterprise registration system to the Ministry of Commerce. Meanwhile, we are not likely to finance the activities of our consolidated affiliated entities by means of capital contributions given the PRC legal restrictions on foreign ownership of internet, value-added telecommunication-based online marketing, online audio and video services and mobile app distribution businesses. We have also entered into several loan agreements with Du Xiaoman, our related party. Please refer to “Related Party Transactions—Transactions with Related Parties—Du Xiaoman”.

In May 2014, SAFE promulgated the Provisions on the Foreign Exchange Administration Rules on Cross-border Guarantee (《跨境擔保外匯管理規定》), which, along with the PRC Foreign Currency Administration Rules, provides that failure to register a cross-border guarantee may subject the violator to order to rectify, warning and a fine no more than RMB300,000. In June 2016, SAFE promulgated SAFE Circular No. 16, which removed certain restrictions previously provided under several SAFE circulars, including SAFE Circular No. 19, in respect of conversion by a foreign-invested enterprise of foreign currency registered capital into RMB and use of such RMB capital. However, SAFE Circular No. 16 continues to prohibit foreign-invested enterprises from, among other things, using RMB fund converted from its foreign exchange capitals for expenditure beyond its business scope, and providing loans to non-affiliated enterprises except as permitted in the business scope. On October 23, 2019, the SAFE issued the Circular on Further Promoting Cross-border Trade and Investment Facilitation, or SAFE Circular 28. Among others, SAFE Circular 28 relaxes prior restrictions and allows foreign-invested enterprises that do not have equity investments in their approved business scope to use their capital obtained from foreign exchange settlement to make domestic equity investments as long as the investments are real and in compliance with the foreign investment-related laws and regulations.

In light of the various requirements imposed by PRC regulations on loans to and direct investment in PRC entities by offshore holding companies, including SAFE Rules and Circulars referred to above, we cannot assure you that we will be able to complete the necessary government registrations or filings on a timely basis, if at all, with respect to existing and future loans by us to our PRC subsidiaries, consolidated affiliated entities and certain related parties or additional capital contributions by us to our PRC subsidiaries, and conversion of such loans or capital contributions into RMB. If we fail to complete such registrations or filings, our ability to capitalize or otherwise fund our PRC operations may be negatively affected, which could adversely affect our ability to fund and expand our business.

PRC regulations relating to the establishment of offshore special purpose companies by PRC residents may limit our ability to inject capital into our PRC subsidiaries, limit our subsidiaries’ ability to increase their registered capital or distribute profits to us, or may otherwise adversely affect us.

The Notice on Relevant Issues Concerning Foreign Exchange Administration for PRC Residents to Engage in Financing and Inbound Investment via Overseas Special Purpose Vehicles, or SAFE Circular No. 75, and a series of implementation rules and guidance issued by SAFE, including the circular relating to operating procedures that came into effect in July 2011, require PRC residents and PRC corporate entities to register with local branches of SAFE in connection with their direct or indirect offshore investment in an overseas special purpose vehicle, or SPV, for the purposes of overseas equity financing activities, and to update such registration in the event of any significant changes with respect to that offshore company. SAFE promulgated the Circular on Relevant Issues

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Concerning Foreign Exchange Control on Domestic Residents’ Offshore Investment and Financing and Roundtrip Investment through Special Purpose Vehicles, or SAFE Circular No. 37, on July 4, 2014, which replaced the SAFE Circular No. 75. SAFE Circular No. 37 requires PRC residents to register with local branches of SAFE in connection with their direct establishment or indirect control of an offshore entity, for the purpose of overseas investment and financing, with such PRC residents’ legally owned assets or equity interests in domestic enterprises or offshore assets or interests, referred to in SAFE Circular No. 37 as a “special purpose vehicle.” The term “control” under SAFE Circular No. 37 is broadly defined as the operation rights, beneficiary rights or decision-making rights acquired by the PRC residents in the offshore special purpose vehicles or PRC companies by such means as acquisition, trust, proxy, voting rights, repurchase, convertible bonds or other arrangements. SAFE Circular No. 37 further requires amendment to the registration in the event of any changes with respect to the basic information of the special purpose vehicle, such as changes in a PRC resident individual shareholder, name or operation period; or any significant changes with respect to the special purpose vehicle, such as increase or decrease of capital contributed by PRC individuals, share transfer or exchange, merger, division or other material event. If the shareholders of the offshore holding company who are PRC residents do not complete their registration with the local SAFE branches, the PRC subsidiaries may be prohibited from distributing their profits and proceeds from any reduction in capital, share transfer or liquidation to the offshore company, and the offshore company may be restricted in its ability to contribute additional capital to its PRC subsidiaries. Moreover, failure to comply with SAFE registration and amendment requirements described above could result in liability under PRC law for evasion of applicable foreign exchange restrictions. On February 28, 2015, SAFE promulgated a Notice on Further Simplifying and Improving Foreign Exchange Administration Policy on Direct Investment, or SAFE Notice 13, which became effective on June 1, 2015. In accordance with SAFE Notice 13, entities and individuals are required to apply for foreign exchange registration of foreign direct investment and overseas direct investment, including those required under the SAFE Circular No. 37, with qualified banks, instead of SAFE. The qualified banks, under the supervision of SAFE, directly examine the applications and conduct the registration.

In addition, our shareholders who are PRC entities shall complete their overseas direct investment filings according to applicable laws and regulations regarding the overseas direct investment by PRC entities, including certificates, filings or registrations with the MOFCOM and NDRC or the local branch of the MOFCOM and NDRC based on the investment amount, invested industry or other factors thereof, and shall also update or apply for amendment in respect to the certificates, filings or registrations in the event of any significant changes with respect to the offshore investment.

We have notified holders of ordinary shares of our company whom we know are PRC residents to register with the local SAFE branch and update their registrations as required under the SAFE regulations described above. We are aware that Mr. Robin Yanhong Li, our chairman, chief executive officer and principal shareholder, who is a PRC resident, has registered, and updated registration when required, with the relevant local SAFE branch. We, however, cannot provide any assurances that all of our shareholders or ADS holders who are PRC residents will file all applicable registrations or update previously filed registrations as required by these SAFE regulations. The failure or inability of our PRC resident shareholders to comply with the registration procedures or other applicable PRC regulations may subject the PRC resident shareholders to fines and legal sanctions, restrict our cross-border investment activities, or limit our PRC subsidiaries’ ability to distribute dividends to or obtain foreign exchange-dominated loans from our company.

As it is uncertain how the SAFE regulations described above will be interpreted or implemented, we cannot predict how these regulations will affect our business operations or future strategy. For example, we may be subject to more stringent review and approval process with respect to our foreign

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exchange activities, such as remittance of dividends and foreign currency-denominated borrowings, which may adversely affect our results of operations and financial condition. In addition, if we decide to acquire a PRC domestic company, we cannot assure you that we or the owners of such company will be able to obtain the necessary approvals or complete the necessary filings and registrations required by the SAFE regulations. This may restrict our ability to implement our acquisition strategy and could adversely affect our business and prospects.

Failure to comply with PRC regulations regarding the registration requirements for employee stock ownership plans or share option plans may subject the PRC plan participants or us to fines and other legal or administrative sanctions.

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 Rule, replacing the earlier rules promulgated in March 2007. Under the Stock Option Rule, PRC residents who are granted stock options by an overseas publicly listed company are required, through a PRC agent or PRC subsidiary of such overseas publicly listed company, to register with SAFE and complete certain other procedures. We and our PRC resident employees who have been granted stock options are subject to these regulations. We have designated our PRC subsidiary Baidu Online to handle the registration and other procedures required by the Stock Option Rule. However, if we or our PRC optionees fail to comply with these regulations on a timely basis, we or our PRC optionees and their local employers may be subject to fines and legal sanctions.

PRC regulations establish complex procedures for some acquisitions conducted by foreign investors, which could make it more difficult for us to pursue growth through acquisitions in China.

The Regulations on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors, adopted by six PRC regulatory agencies in August 2006 and amended in June 2009, among other things, established additional procedures and requirements that could make merger and acquisition activities by foreign investors more time-consuming and complex. In addition, the Implementing Rules Concerning Security Review on the Mergers and Acquisitions by Foreign Investors of Domestic Enterprises, or the Rules Concerning Security Review on M&A, issued by the Ministry of Commerce in August 2011, specify that mergers and acquisitions by foreign investors involved in “an industry related to national security” are subject to strict review by the Ministry of Commerce, and prohibit any activities attempting to bypass such security review, including by structuring the transaction through a proxy or contractual control arrangement. We believe that our business is not in an industry related to national security, but we cannot preclude the possibility that the competent PRC government authorities may publish explanations contrary to our understanding or broaden the scope of such security reviews in the future, in which case our future acquisitions and investment in the PRC, including those by way of entering into contractual control arrangements with target entities, may be closely scrutinized or prohibited. Moreover, according to the Anti-Monopoly Law, the SMAR shall be notified in advance of any concentration of undertaking if certain filing thresholds are triggered. We may grow our business in part by directly acquiring complementary businesses in China. Complying with the requirements of the laws and regulations mentioned above and other PRC regulations to complete such transactions could be time-consuming, and any required approval processes, including obtaining approval from the SMAR, may delay or inhibit our ability to complete such transactions, which could affect our ability to expand our business or maintain our market share. Our ability to expand our business or maintain or expand our market share through future acquisitions would as such be materially and adversely affected.

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In December 2020, the National Development and Reform Commission and the Ministry of Commerce promulgated the Measures for the Security Review of Foreign Investment, which came into effect on January 18, 2021. See “Regulations—Regulations on Foreign Investment.” for more details. As these measures are recently promulgated, official guidance has not been issued by the designated office in charge of such security review yet. At this stage, the interpretation of those measures remains unclear in many aspects such as what would constitute “important information technology and internet services and products” and whether these measures may apply to foreign investment that is implemented or completed before the enactment of these new measures. As our business may be deemed to constitute the foregoing circumstances, we cannot assure you that our current business operations will remain fully compliant, or we can adapt our business operations to new regulatory requirements on a timely basis, or at all.

The auditor of our consolidated financial statements included in this document and our annual reports on Form 20-F filed with the SEC, like other independent registered public accounting firms operating in China, is not permitted to be subject to inspection by the Public Company Accounting Oversight Board, or PCAOB, and consequently, you are deprived of the benefits of such inspection. In addition, various legislative and regulatory developments related to U.S.-listed China-based companies due to lack of PCAOB inspection and other developments due to political tensions between the United States and China may have a material adverse impact on our listing and trading in the U.S. and the trading prices of our securities.

The auditor of our consolidated financial statements included in this document and our annual reports on Form 20-F filed with the SEC, is registered with the Public Company Accounting Oversight Board (United States), or the PCAOB. Pursuant to laws in the United States, the PCAOB has authority to conduct regular inspections over independent registered public accounting firms registered with the PCAOB to assess their compliance with the applicable professional standards. The auditor is located in China, a jurisdiction which does not allow the PCAOB to conduct inspections without the approval of the Chinese authorities. As a result, we understand that our auditor is not currently inspected by the PCAOB.

In May 2013, the PCAOB announced that it had entered into a Memorandum of Understanding on Enforcement Cooperation with the China Securities Regulation Commission, or the CSRC, and the Ministry of Finance, which establishes a cooperative framework between the parties for the production and exchange of audit documents relevant to investigations undertaken by PCAOB, the CSRC or the Ministry of Finance in the United States and the PRC, respectively. The PCAOB continues to discuss with the CSRC and the Ministry of Finance on joint inspections in the PRC of PCAOB-registered audit firms that provide auditing services to Chinese companies that trade on U.S. stock exchanges. On December 7, 2018, the SEC and the PCAOB issued a joint statement highlighting continued challenges faced by the U.S. regulators in their oversight of financial statement audits of U.S.-listed companies with significant operations in China. However, it remains unclear what further actions the SEC and the PCAOB will take to address the problem. On April 21, 2020, the SEC and the PCAOB issued another joint statement reiterating the greater risk of insufficient disclosures from companies in many emerging markets, including China, compared to those from U.S. domestic companies. In discussing the specific issues related to these greater risk, the statement again highlighted the PCAOB’s inability to inspect audit work and practices of accounting firms in China with respect to U.S. reporting companies.

On June 4, 2020, the then U.S. President issued a memorandum ordering the President’s Working Group on Financial Markets, or the PWG, to submit a report to the President within 60 days of the memorandum that includes recommendations for actions that can be taken by the executive branch and by the SEC or PCAOB on Chinese companies listed on U.S. stock exchanges and their audit firms.

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On August 6, 2020, the PWG released the report. In particular, with respect to jurisdictions that do not grant the PCAOB sufficient access to fulfill its statutory mandate, or NCJs, the PWG recommends that enhanced listing standards be applied to companies from NCJs for seeking initial listing and remaining listed on U.S. stock exchanges. Under the enhanced listing standards, if the PCAOB does not have access to work papers of the principal audit firm located in a NCJ for the audit of a U.S.-listed company as a result of governmental restrictions, the U.S.-listed company may satisfy this standard by providing a co-audit from an audit firm with comparable resources and experience where the PCAOB determines that it has sufficient access to the firm’s audit work papers and practices to inspect the co-audit. The report permits the new listing standards to provide for a transition period until January 1, 2022 for listed companies, but would apply immediately to new listings once the necessary rulemakings and/or standard-setting are effective. After this transition period, if currently listed companies were unable to meet the enhanced listing standards, then they would become subject to securities exchange rules and processes that could lead to possible de-listing if not cured, deregistration from the SEC and/or other risks, which may materially and adversely affect the market price and liquidity of such companies’ securities, or effectively terminate their trading in the United States. The measures in the PWG Report are presumably subject to the standard SEC rulemaking process before becoming effective. These were recent media reports about the SEC’s proposed rulemaking in this regard. It is uncertain whether the PWG recommendations will be adopted, in whole or in part, and the impact of any new rule on us cannot be estimated at this time.

Inspections of other firms that PCAOB has conducted outside of China have identified deficiencies in those firms’ audit procedures and quality control procedures, which may be addressed as part of the inspection process to improve future audit quality. The lack of the PCAOB inspections in China prevents the PCAOB from fully evaluating audits and quality control procedures of the auditor of our consolidated financial statements included in this document and our annual reports on Form 20-F filed with the SEC. As a result, we and investors in our ordinary shares are deprived of the benefits of such PCAOB inspections, which could cause investors and potential **[REDACTED]** in our stock to lose confidence in our audit procedures and reported financial information and the quality of our financial statements.

As part of a continued regulatory focus in the United States on access to audit and other information currently protected by national law, in particular China’s, the Holding Foreign Companies Accountable Act, or the Act, has been enacted in December 2020. In essence, the Act requires the SEC to prohibit foreign companies from having its securities traded on U.S. securities exchanges or “over-the-counter” if a company retains a foreign accounting firm that cannot be inspected by the PCAOB for three consecutive years, beginning in 2021. The enactment of Act and any additional rulemaking efforts to increase U.S. regulatory access to audit information in China could cause investor uncertainty for affected SEC registrants, including us, the market price of our ADSs could be materially adversely affected, and our ADSs could be delisted if we are unable to meet the PCAOB inspection requirement in time.

In addition, political tensions between the United States and China have escalated due to, among other things, trade disputes, the COVID-19 outbreak, sanctions imposed by the U.S. Department of Treasury on certain officials of the Hong Kong Special Administrative Region and the central government of the PRC and the executive orders issued by then U.S. President Donald J. Trump in August 2020 that prohibit certain transactions with certain Chinese companies and their applications. Rising political tensions could reduce levels of trades, investments, technological exchanges and other economic activities between the two major economies, which would have a material adverse effect on global

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economic conditions and the stability of global financial markets. Any of these factors could have a material adverse effect on our business, prospects, financial condition and results of operations.

Proceedings instituted by the SEC against certain PRC-based accounting firms, including the auditor of our consolidated financial statements included in this document and our annual reports on Form 20-F filed with the SEC, could result in financial statements being determined to not be in compliance with the requirements of the Securities Exchange Act of 1934, as amended, or the Exchange Act.

In December 2012, the SEC brought administrative proceedings against five accounting firms in China, including the auditor of our consolidated financial statements included in this document and our annual reports on Form 20-F filed with the SEC, alleging that they had refused to produce audit work papers and other documents related to certain other China-based companies under investigation by the SEC. On January 22, 2014, an initial administrative law decision was issued, censuring these accounting firms and suspending four of these firms from practicing before the SEC for a period of six months. The decision is neither final nor legally effective unless and until reviewed and approved by the SEC. On February 12, 2014, four of these PRC-based accounting firms appealed to the SEC against this decision. In February 2015, each of the four PRC-based accounting firms agreed to a censure and to pay a fine to the SEC to settle the dispute and avoid suspension of their ability to practice before the SEC. The settlement requires the firms to follow detailed procedures to seek to provide the SEC with access to Chinese firms’ audit documents via the CSRC. If the firms fail to meet specified criteria, during a period of four years starting from the settlement date, the SEC retains authority to impose a variety of additional remedial measures on the firms depending on the nature of the failure. Additional remedies for any future noncompliance could include, as appropriate, an automatic six-month bar on a single firm’s performance of certain audit work, commencement of additional proceedings against a firm, or in extreme cases the resumption of the current proceeding against all four firms.

The audit committee is aware of the policy restriction and regularly communicated with our independent auditor to ensure compliance. If additional remedial measures are imposed on the China-based “big four” accounting firms, including our independent registered public accounting firm, in administrative proceedings brought by the SEC alleging the firms’ failure to meet specific criteria set by the SEC with respect to requests for the production of documents, we could be unable to timely file future financial statements in compliance with the requirements of the Exchange Act. The settlement did not require the firms to admit to any violation of law and preserves the firms’ legal defenses in the event the administrative proceeding is restarted.

In the event that the SEC restarts the administrative proceedings, depending upon the final outcome, listed companies in the United States with major PRC operations may find it difficult or impossible to retain auditors in respect of their operations in the PRC, which could result in financial statements being determined to not be in compliance with the requirements of the Exchange Act, including possible delisting. Moreover, any negative news about the proceedings against these audit firms may cause investor uncertainty regarding China-based, United States-listed companies and the market price of our securities may be adversely affected.

If the auditor of our consolidated financial statements included in this document and our annual reports on Form 20-F filed with the SEC were denied, even temporarily, the ability to practice before the SEC and we were unable to timely find another registered public accounting firm to audit and issue an opinion on our financial statements, our financial statements could be determined not to be in compliance with the requirements of the Exchange Act. Such a determination could ultimately lead to

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our delisting from the Nasdaq Global Select Market or deregistration from the SEC, or both, which would substantially reduce or effectively terminate the trading of our ADSs in the United States.

Fluctuation in exchange rates could have a material and adverse effect on our results of operations and the value of your [REDACTED].

The conversion of Renminbi into foreign currencies, including U.S. dollars, is based on rates set by the People’s Bank of China. The value of Renminbi against the U.S. dollar and other currencies is affected by changes in China’s political and economic conditions and by China’s foreign exchange policies, among other things. We cannot assure you that Renminbi will not appreciate or depreciate significantly in value against the U.S. dollar in the future. It is difficult to predict how market forces or PRC or U.S. government policy may impact the exchange rate between Renminbi and the U.S. dollar in the future.

Our revenues and costs are mostly denominated in RMB. Any significant revaluation of RMB may materially and adversely affect our cash flows, revenues, earnings and financial position, and the value of, and any dividends payable on, our ordinary shares and/or ADSs in U.S. dollars. For example, to the extent that we need to convert U.S. dollars into RMB for our operations, appreciation of the RMB against the U.S. dollar would have an adverse effect on the RMB amount we would receive from the conversion. Conversely, if we decide to convert our RMB into U.S. dollars for the purpose of making payments for dividends on our ordinary shares or ADSs, repaying our U.S. dollar denominated notes or other payment obligations or for other business purposes, appreciation of the U.S. dollar against the RMB would have a negative effect on the U.S. dollar amount available to us. In addition, appreciation or depreciation in the value of the RMB relative to U.S. dollars would affect our financial results reported, regardless of any underlying change in our business or results of operations, as RMB is our reporting currency. For example, an appreciation of RMB against the U.S. dollar would result in foreign currency translation losses for financial reporting purposes when we translate our U.S. dollar denominated financial assets into RMB, our reporting currency, and foreign exchange losses reported in earnings for certain RMB denominated loans that overseas entities borrowed from our PRC entities. Conversely, a depreciation of RMB against the U.S. dollar would result in foreign currency translation losses for financial reporting purposes when we translate our U.S. dollar denominated notes and other indebtedness into RMB. Moreover, a significant depreciation of the RMB against the U.S. dollar may significantly reduce our earnings translated in the U.S. dollars, which in turn could adversely affect the price of our securities.

Very limited hedging options are available in China to reduce our exposure to exchange rate fluctuations. To date, we have not entered into any hedging transactions in an effort to reduce our exposure to foreign currency exchange risk. While we may decide to enter into hedging transactions in the future, the availability and effectiveness of these hedges may be limited and we may not be able to adequately hedge our exposure or at all. In addition, our currency exchange losses may be magnified by PRC exchange control regulations that restrict our ability to convert RMB into foreign currency. As a result, fluctuations in exchange rates may have a material adverse effect on your [REDACTED].

We face uncertainties with respect to indirect transfers of equity interests in PRC resident enterprises by their non-PRC holding companies. Enhanced scrutiny over acquisition transactions by the PRC tax authorities may have a negative impact on potential acquisitions we may pursue in the future.

In February 2015, the State Administration of Tax issued a Public Notice Regarding Certain Corporate Income Tax Matters on Indirect Transfer of Properties by Non-Tax Resident Enterprises, or Public Notice 7. Public Notice 7 extends its tax jurisdiction to not only indirect transfers but also transactions

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involving transfer of other taxable assets, through the offshore transfer of a foreign intermediate holding company. Public Notice 7 also brings challenges to both the foreign transferor and transferee (or other person who is obligated to pay for the transfer) of the taxable assets. Where a non-resident enterprise conducts an “indirect transfer” by transferring the taxable assets indirectly by disposing of the equity interests of an overseas holding company, the non-resident enterprise being the transferor, or the transferee, or the PRC entity which directly owned the taxable assets may report to the relevant tax authority such indirect transfer. Using a “substance over form” principle, the PRC tax authority may re-characterize such indirect transfer as a direct transfer of the equity interests in the PRC tax resident enterprise and other properties in China. As a result, gains derived from such indirect transfer may be subject to PRC enterprise income tax, and the transferee or other person who is obligated to pay for the transfer is obligated to withhold the applicable taxes, currently at a rate of up to 10% for the transfer of equity interests in a PRC resident enterprise. However, Public Notice 7 provides safe harbors for internal group restructurings and the purchase and sale of equity through a public securities market. On October 17, 2017, the State Administration of Taxation, or the SAT issued the Announcement of the State Administration of Taxation on Issues Concerning the Withholding of Non-resident Enterprise Income Tax at Source, or SAT Bulletin 37, which came into effect on December 1, 2017. SAT Bulletin 37 further clarifies the practice and procedure of the withholding of non-resident enterprise income tax. Pursuant to Public Notice 7 and SAT Bulletin 37, both the transferor and the transferee may be subject to penalties under PRC tax laws if the transferee fails to withhold the taxes and the transferor fails to pay the taxes.

We face uncertainties with respect to the reporting and consequences of private equity financing transactions, share exchange or other transactions involving the transfer of shares in our company by investors that are non-PRC resident enterprises, or sale or purchase of shares in other non-PRC resident companies or other taxable assets by us. Our company and other non-resident enterprises in our group may be subject to filing obligations or being taxed if our company and other non-resident enterprises in our group are transferors in such transactions, and may be subject to withholding obligations if our company and other non-resident enterprises in our group are transferees in such transactions, under Public Notice 7 and SAT Bulletin 37. For the transfer of shares in our company by investors that are non-PRC resident enterprises, our PRC subsidiaries may be requested to assist in the filing under Public Notice 7 and SAT Bulletin 37. As a result, we may be required to expend valuable resources to comply with Public Notice 7 and SAT Bulletin 37 or to request the relevant transferors from whom we purchase taxable assets to comply with these circulars, or to establish that our company and other non-resident enterprises in our group should not be taxed under these circulars. The PRC tax authorities have the discretion under Public Notice 7 and SAT Bulletin 37 to make adjustments to the taxable capital gains based on the difference between the fair value of the taxable assets transferred and the cost of investment. If the PRC tax authorities make adjustments to the taxable income of the transactions under Public Notice 7 and SAT Bulletin 37, our income tax costs associated with such transactions will be increased, which may have an adverse effect on our financial condition and results of operations. We have made acquisitions in the past and may conduct additional acquisitions in the future. We cannot assure you that the PRC 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 to them for the investigation of any transactions we were involved in. Heightened scrutiny over acquisition transactions by the PRC tax authorities may have a negative impact on potential acquisitions we may pursue in the future.

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Risks Related to Our Shares, ADSs and the Listing

As a company applying for listing under Chapter 19C, we adopt different practices as to certain matters as compared with many other companies listed on the Hong Kong Stock Exchange.

As we are applying for listing under Chapter 19C of the Hong Kong Listing Rules, we will not be subject to certain provisions of the Hong Kong Listing Rules pursuant to Rule 19C.11, including, among others, rules on notifiable transactions, connected transactions, share option schemes, content of financial statements as well as certain other continuing obligations. In addition, in connection with the Listing, we have applied for a number of waivers and/or exemptions from strict compliance with the Hong Kong Listing Rules, the Companies (Winding Up and Miscellaneous Provisions) Ordinance, the Takeovers Codes and the SFO. As a result, we will adopt different practices as to those matters as compared with other companies listed on the Hong Kong Stock Exchange that do not enjoy those exemptions or waivers. For additional information, see “Waivers from Strict Compliance with the Hong Kong Listing Rules and Exemptions from the Companies (Winding Up and Miscellaneous Provisions) Ordinance.”

Our Articles of Association are specific to us and include certain provisions that may be different from the requirements under the Hong Kong Listing Rules and common practices in Hong Kong. For example, Rule 19C.07(7) of the Hong Kong Listing Rules provides that the minimum stake required to convene an extraordinary general meeting and add resolutions to a meeting agenda must not be higher than 10% of the voting rights, on a one vote per share basis, in the share capital of a Qualifying Issuer, but our Articles of Association provide that not less than a majority of the aggregate voting power of our Company is required to convene an extraordinary general meeting. We will convene an extraordinary general meeting by December 31, 2021, and put forth a resolution to revise our Articles of Association to comply with Rule 19C.07(7) of the Hong Kong Listing Rules. Prior to the amendment to our Articles, we undertake to convene general meetings at the request of shareholders holding in aggregate not less than 10% of the Company’s voting rights, on a one vote per share basis.

Furthermore, if 55% or more of the total worldwide trading volume, by dollar value, of our Class A ordinary shares and ADSs over our most recent fiscal year takes place on the Hong Kong Stock Exchange, the Hong Kong Stock Exchange will regard us as having a dual primary listing in Hong Kong and we will no longer enjoy certain exemptions or waivers from strict compliance with the requirements under the Hong Kong Listing Rules, the Companies (Winding Up and Miscellaneous Provisions) Ordinance, the Takeovers Codes and the SFO, which could result in us having to amend our corporate structure and Articles of Association and our incurring of incremental compliance costs.

The trading price of our ADSs has been and is likely to continue to be, and the trading price of our Class A ordinary shares can be, volatile regardless of our operating performance.

The trading price of our ADSs has been and is likely to continue to be volatile, and could fluctuate widely in response to a variety of factors, many of which are beyond our control. Likewise, the trading price of our Class A ordinary shares can be volatile for similar or different reasons.

Factors impacting the price and trading volume of our listed securities include, but are not limited to, the following:

- actual or anticipated fluctuations in our quarterly results of operations and changes or revisions of our expected results, as well as our margins and profitability;
- changes in financial estimates by securities research analysts;
- conditions in internet search and online marketing markets;

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- changes in the operating performance or market valuations of other internet search or internet companies;
- announcements by us or our competitors or other internet companies of new product-and-service offerings, acquisitions, strategic partnerships, joint ventures, capital raisings or capital commitments;
- success or failure of our new business initiatives or the development or growth of the new markets we enter into;
- addition to or departure of key personnel;
- public perception or negative news about our products or services or potential investments or acquisitions;
- our share repurchase program;
- fluctuations of exchange rates between RMB and the U.S. dollar;
- litigation, government investigation or other legal or regulatory proceeding; and
- general economic or political conditions in China or elsewhere in the world.

In addition, the stock market in general, and the performance and fluctuation of the market prices for internet-related companies and other companies with operations mainly in China in particular, may affect the volatility in the prices of and trading volumes for our securities. The securities of some China-based companies that have listed their securities in the United States and/or Hong Kong have experienced significant volatility that often has been unrelated to the operating performance of such companies, including, in some cases, substantial declines in the trading prices of their securities. The trading performances of these companies' securities may affect the attitudes of investors towards Chinese companies listed in the United States and/or Hong Kong in general, which consequently may impact the trading performance of our securities, regardless of our actual operating performance. In addition, any negative news or perceptions about inadequate corporate governance practices or fraudulent accounting, corporate structure or other matters of other Chinese companies may also negatively affect the attitudes of investors towards Chinese companies in general, including us, regardless of whether we have engaged in any inappropriate activities. In particular, the global financial crisis, the ensuing economic recessions and deterioration in the credit market in many countries have contributed and may continue to contribute to extreme volatility in the global stock markets. These broad market and industry fluctuations may adversely affect the market price of our securities. Volatility or a lack of positive performance in the price of our listed securities may also adversely affect our ability to retain key employees, most of whom have been granted options or other equity incentives.

Substantial future sales or perceived potential sales of our Class A ordinary shares and/or ADSs in the public market could cause the price of our Class A ordinary shares and/or ADSs to decline.

Sales of our Class A ordinary shares and/or ADSs in the public market, or the perception that these sales could occur, could cause the market price of our Class A ordinary shares and/or ADSs to decline. Such sales also might make it more difficult for us to sell equity or equity-related securities in the future at a time and price that we deem appropriate. If any existing shareholder or shareholders sell a substantial amount of our Class A ordinary shares and/or ADSs, the prevailing market price for our Class A ordinary shares and/or ADSs could be adversely affected. In addition, if we pay for our future acquisitions in whole or in part with additionally issued ordinary shares, your ownership interests in our company would be diluted and this, in turn, could have a material and adverse effect on the price of our Class A ordinary shares and/or ADSs.

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If securities or industry analysts do not publish research or publish inaccurate or unfavorable research about our business, the market price for our Class A ordinary shares and/or ADSs and trading volume could decline.

The trading market for our Class A ordinary shares and/or ADSs will depend in part on the research and reports that securities or industry analysts publish about us or our business. If research analysts do not maintain adequate research coverage or if one or more of the analysts who covers us downgrades our Class A ordinary shares and/or ADSs or publishes inaccurate or unfavorable research about our business, the market price for our Class A ordinary shares and/or ADSs would likely decline. If one or more of these analysts cease coverage of our company or fail to publish reports on us regularly, we could lose visibility in the financial markets, which, in turn, could cause the market price of or trading volume for our Class A ordinary shares and/or ADSs to decline.

Techniques employed by short sellers may drive down the market price of our listed securities.

Short selling is the practice of selling securities that a seller does not own but rather has borrowed from a third party with the intention of buying identical securities back at a later date to return to the lender. Short sellers hope to profit from a decline in the value of the securities between the sale of the borrowed securities and the purchase of the replacement shares, as short sellers expect to pay less in that purchase than they received in the sale. As it is in short sellers’ interest for the price of the security to decline, many short sellers publish, or arrange for the publication of, negative opinions and allegations regarding the relevant issuer and its business prospects in order to create negative market momentum and generate profits for themselves after selling a security short. These short attacks have, in the past, led to selling of shares in the market.

Public companies listed in the United States that have substantially all of their operations in China have been the subject of short selling. Much of the scrutiny and negative publicity has centered on allegations of a lack of effective internal control over financial reporting resulting in financial and accounting irregularities and mistakes, inadequate corporate governance policies or a lack of adherence thereto and, in many cases, allegations of fraud. As a result, many of these companies are now conducting internal and external investigations into the allegations and, in the interim, are subject to shareholder lawsuits and/or SEC enforcement actions.

iQIYI was subject to allegations made in the short seller report published by Wolfpack Research. See “Business—Legal Proceedings.” In November 2020, we entered into definitive agreements with JOYY Inc. and certain of its affiliates to acquire YY Live. Muddy Waters published a short selling report on November 18, 2020 against JOYY Inc. Based on public records, JOYY Inc. and certain of its current and former officers and directors were named as defendants in a federal putative securities class action filed in November 2020 alleging that they made material misstatements and omissions in documents filed with the SEC regarding certain of the allegations contained in the Muddy Waters short seller report. See “—We face risks associated with our acquisition of YY Live and its online live streaming business.” We may also become the subject of other short seller attacks from time to time in the future and class actions or regulatory enforcement actions derivative of such short seller attacks or actions of a similar nature. Any such allegations may be followed by periods of instability in the market price of our ordinary shares and ADSs and negative publicity. If and when we become the subject of any unfavorable allegations, whether such allegations are proven to be true or untrue, we may have to expend a significant amount of resources to investigate such allegations and/or defend ourselves, including in connection with class actions or regulatory enforcement actions derivative of such allegations. While we would strongly defend against any such short seller attacks, we may be constrained in the manner in which we can proceed against the relevant short sellers by principles of

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freedom of speech, applicable state law or issues of commercial confidentiality. Such a situation could be costly and time-consuming, and could divert management’s attention from the day-to-day operations of our company. Even if such allegations are ultimately proven to be groundless, allegations against us could severely impact the market price of our securities and our business operations.

We cannot guarantee that any share repurchase program will be fully consummated or that any share repurchase program will enhance long-term shareholder value, and share repurchases could increase the volatility of the price of our Class A ordinary shares and/or ADSs and could diminish our cash reserves.

Our board of director have authorized a few share repurchase programs in recent years, some of which had not been fully consummated:

- On June 26, 2018, our board of directors authorized a share repurchase program, under which we may repurchase up to US\$1.0 billion of our ADSs or ordinary shares over 12 months from June 27, 2018 through June 26, 2019.
- On May 16, 2019, our board of directors authorized a new share repurchase program, under which we may repurchase up to US\$1.0 billion of our ADSs or ordinary shares, effective until July 1, 2020.
- On May 13, 2020, our board of directors authorized a share repurchase program, under which we may repurchase up to US\$1.0 billion of our ADSs or shares, effective until July 1, 2021. On August 6, 2020, our board of directors approved a change to the 2020 share repurchase program, increasing the repurchase authorization from US\$1 billion to US\$3 billion and extending the effective time through December 31, 2022. On December 8, 2020, our board of directors approved a further increase in the repurchase authorization from US\$3 billion to US\$4.5 billion.

Our board of directors also has the discretion to authorize additional share repurchase programs in the future. The share repurchase programs do not obligate us to repurchase any specific dollar amount or to acquire any specific number of ADSs and/or shares. We cannot guarantee that any share repurchase program will enhance long-term shareholder value. The share repurchase programs could affect the price of our securities and increase volatility, and may be suspended or terminated at any time, which may result in a decrease in the trading price of our securities. Furthermore, share repurchases could increase the volatility of the price of our Class A ordinary shares and/or ADSs and could diminish our cash reserves.

Because we do not expect to pay dividends in the foreseeable future, you must rely on price appreciation of our Class A ordinary shares and/or ADSs for return on your [REDACTED].

We currently do not expect to pay any cash dividends in the foreseeable future. Therefore, you should not rely on an [REDACTED] in our Class A ordinary shares and/or ADSs as a source for any future dividend income.

Our board of directors has complete discretion as to whether to distribute dividends. In addition, our shareholders may by ordinary resolution declare a dividend, but no dividend may exceed the amount recommended by our board of directors. In either case, the declaration of dividend will be subject to our Memorandum and Articles and certain restrictions under Cayman Islands law. Even if our board of directors decides to declare and pay dividends, the timing, amount and form of future dividends, if any, will depend on, among other things, our future results of operations and cash flow, our capital requirements and surplus, the amount of distributions, if any, received by us from our subsidiaries, our

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financial condition, contractual restrictions and other factors deemed relevant by our board of directors. Accordingly, the return on your [REDACTED] in our Class A ordinary shares and/or ADSs will likely depend entirely upon any future price appreciation of our Class A ordinary shares and/or ADSs. There is no guarantee that our Class A ordinary shares and/or ADSs will appreciate in value or even maintain the price at which you purchased the Class A ordinary shares and/or ADSs. You may not realize a return on your [REDACTED] in our Class A ordinary shares and/or ADSs and you may even lose your entire [REDACTED] in our Class A ordinary shares and/or ADSs.

Holders of our ADSs may not have the same voting rights as the holders of our ordinary shares and may not receive voting materials in time to be able to exercise their right to vote.

Holders of our ADSs will not be able to exercise directly voting rights attached to the shares evidenced by our ADSs on an individual basis. Holders of our ADSs will appoint the depositary or its nominee as their representative to exercise the voting rights attached to the shares represented by the ADSs. Holders of our ADSs may not receive voting materials in time to instruct the depositary to vote, and it is possible that such holders, or persons who hold their ADSs through brokers, dealers or other third parties, will not have the opportunity to exercise a right to vote. Upon our written request, the depositary will mail to holders of our ADSs a shareholder meeting notice which contains, among other things, a statement as to the manner in which such holders' voting instructions may be given, including an express indication that such instructions may be given or deemed given to the depositary to give a discretionary proxy to a person designated by us if no instructions are received by the depositary from the holders on or before the response date established by the depositary. However, no voting instruction will be deemed given and no such discretionary proxy will be given with respect to any matter as to which we inform the depositary that (i) we do not wish such proxy given, (ii) substantial opposition exists, or (iii) such matter materially and adversely affects the rights of shareholders.

Holders of our ADSs, and holders of ordinary shares located in the United States, may not be able to participate in rights offerings and may experience dilution of their holdings as a result.

We may from time to time distribute rights to our shareholders, including rights to acquire our securities. Under the deposit agreement for the ADSs, the depositary will not offer those rights to ADS holders unless both the rights and the underlying securities to be distributed to ADS holders are either registered under the Securities Act of 1933, or exempt from registration under the Securities Act with respect to all holders of ADSs. Holders of ordinary shares located in the United States also cannot exercise rights unless the rights and the underlying shares are so regulated. We are under no obligation to file a registration statement with respect to any such rights or underlying securities or to endeavor to cause such a registration statement to be declared effective. In addition, we may not be able to take advantage of any exemptions from registration under the Securities Act. Accordingly, holders of our ADSs, and holders of ordinary shares located in the United States, may be unable to participate in our rights offerings and may experience dilution in their holdings as a result.

Holders of our ADSs may not receive cash dividends if the depositary decides it is impractical to make them available to them.

The depositary will pay cash dividends on the ADSs only to the extent that we decide to distribute dividends on our Class A ordinary shares or other deposited securities, and we do not have any present plan to pay any cash dividends on our ordinary shares in the foreseeable future. To the extent that there is a distribution, the depositary of our ADSs has agreed to pay to holders of our ADSs the cash dividends or other distributions it or the custodian receives on our Class A ordinary shares or other deposited securities after deducting its fees and expenses. ADS holders will receive these distributions

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in proportion to the number of Class A ordinary shares their ADSs represent. However, the depository may, at its discretion, decide that it is inequitable or impractical to make a distribution available to any holders of ADSs. In these cases, the depository may decide not to distribute such property to holders of our ADSs.

Holders of our ADSs may be subject to limitations on transfer of their ADSs.

The ADSs are transferable on the books of the depository. However, the depository may close its transfer books at any time or from time to time when it deems expedient in connection with the performance of its duties. In addition, the depository may refuse to deliver, transfer or register transfers of ADSs generally when our books or the books of the depository are closed, or at any time if we or the depository deems it advisable to do so because of any requirement of law or of any government or governmental body, or under any provision of the deposit agreement, or for any other reason.

Certain judgments obtained against us by our shareholders may not be enforceable.

We are incorporated in the Cayman Islands, and conduct most of our operations in China through our subsidiaries and consolidated affiliated entities in China. All of our executive officers and a majority of our directors do not reside in the United States or Hong Kong and some or all of the assets of these persons are not located in the United States or Hong Kong. As a result, it may not be possible to effect service of process within the United States, Hong Kong or elsewhere outside of China upon our executive officers, including with respect to matters arising under U.S. federal securities laws or applicable state securities laws, Hong Kong laws or otherwise.

It may also be difficult or impossible for you to bring an action against us or against our directors and executive officers in the Cayman Islands or in China in the event that you believe that your rights have been infringed under the securities laws or otherwise. Even if you are successful in bringing an action of this kind, the laws of the Cayman Islands and of China may render you unable to enforce a judgment against our assets or the assets of our directors and executive officers.

Although there is no statutory enforcement in the Cayman Islands of judgments obtained in the Hong Kong courts or federal or state courts of the United States (and the Cayman Islands are not a party to any treaties for the reciprocal enforcement or recognition of such judgments), a judgment obtained in such jurisdiction will be recognized and enforced in the courts of the Cayman Islands at common law, without any re-examination of the merits of the underlying dispute, by an action commenced on the foreign judgment debt in the Grand Court of the Cayman Islands, provided such judgment (i) is given by a foreign court of competent jurisdiction, (ii) imposes on the judgment debtor a liability to pay a liquidated sum for which the judgment has been given, (iii) is final, (iv) is not in respect of taxes, a fine or a penalty, and (v) was not obtained in a manner and is not of a kind the enforcement of which is contrary to natural justice or the public policy of the Cayman Islands. However, the Cayman Islands courts are unlikely to enforce a judgment obtained from the U.S. or Hong Kong courts under civil liability provisions of the U.S. federal securities law or Hong Kong law if such judgment is determined by the courts of the Cayman Islands to give rise to obligations to make payments that are penal or punitive in nature. Because such a determination has not yet been made by a court of the Cayman Islands, it is uncertain whether such civil liability judgments from U.S. or Hong Kong courts would be enforceable in the Cayman Islands.

Our corporate affairs are governed by our memorandum and articles of association and by the Companies Act (2021 Revision) and common law of the Cayman Islands. The rights of shareholders to take legal action against our directors and us, actions by minority shareholders and the fiduciary

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responsibilities of our directors to us under Cayman Islands law are to a large extent governed by the common law of the Cayman Islands. The common law of the Cayman Islands is derived in part from comparatively limited judicial precedent in the Cayman Islands as well as from English common law, which has persuasive, but not binding, authority on a court in the Cayman Islands. The rights of our shareholders and the fiduciary duties of our directors under Cayman Islands law are not as clearly established as they would be under statutes or judicial precedents in the United States. In particular, the Cayman Islands has a less developed body of securities laws as compared to the United States, and provides significantly less protection to investors. In addition, Cayman Islands companies may not have standing to initiate a shareholder derivative action before the federal courts of the United States.

The recognition and enforcement of foreign judgments are provided for under the PRC Civil Procedures Law. PRC courts may recognize and enforce foreign judgments in accordance with the requirements of the PRC Civil Procedures Law based either on treaties between China and the country where the judgment is made or on principles of reciprocity between jurisdictions. China does not have any treaties or other forms of reciprocity with the United States that provide for the reciprocal recognition and enforcement of foreign judgments. In addition, according to the PRC Civil Procedures Law, the PRC courts will not enforce a foreign judgment against us or our director and officers if they decide that the judgment violates the basic principles of PRC laws or national sovereignty, security or public interest. As a result, it is uncertain whether and on what basis a PRC court would enforce a judgment rendered by a court in the United States.

As a result of all of the above, our public shareholders may have more difficulty in protecting their interests through actions against our management, directors or major shareholders than would shareholders of a corporation incorporated in a jurisdiction in the United States or in Hong Kong.

Since we are a Cayman Islands exempted company, the rights of our shareholders may be more limited than those of shareholders of a company organized in the United States or Hong Kong.

Under the laws of some jurisdictions in the United States, majority and controlling shareholders generally have certain fiduciary responsibilities to the minority shareholders. Shareholder action must be taken in good faith, and actions by controlling shareholders which are obviously unreasonable may be declared null and void. Cayman Islands law protecting the interests of minority shareholders may not be as protective in all circumstances as the law protecting minority shareholders in some U.S. jurisdictions. In addition, the circumstances in which a shareholder of a Cayman Islands company may sue the company derivatively, and the procedures and defenses that may be available to the company, may result in the rights of shareholders of a Cayman Islands company being more limited than those of shareholders of a company organized in the United States.

Furthermore, our directors have the power to take certain actions without shareholder approval which would require shareholder approval under Hong Kong law or the laws of most U.S. jurisdictions. The directors of a Cayman Islands company, without shareholder approval, may implement a sale of any assets, property, part of the business, or securities of the company. Our ability to create and issue new classes or series of shares without shareholders' approval could have the effect of delaying, deterring or preventing a change in control without any further action by our shareholders, including a tender offer to purchase our ordinary shares at a premium over then current market prices.

Furthermore, our Articles of Association are specific to us and include certain provisions that may be different from common practices in Hong Kong, such as the absence of requirements that the appointment, removal and remuneration of auditors must be approved by a majority of our shareholders. See “Information about the Listing” and “Waivers from Strict Compliance with the Hong

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Hong Kong Listing Rules and Exemptions from the Companies (Winding Up and Miscellaneous Provisions) Ordinance—Shareholder Protection” for further details.

Our dual-class ordinary share structure with different voting rights could discourage others from pursuing any change of control transactions that holders of our Class A ordinary shares and ADSs may view as beneficial.

Our ordinary shares are divided into Class A ordinary shares and Class B ordinary shares. Holders of Class A ordinary shares are entitled to one vote per share, while holders of Class B ordinary shares are entitled to ten votes per share. We issued Class A ordinary shares represented by our ADSs in our initial public offering. Our co-founder, chairman and chief executive officer, Robin Yanhong Li, who acquired our shares prior to our initial public offering, holds our Class B ordinary shares. Each Class B ordinary share is convertible into one Class A ordinary share at any time by the holder thereof, while Class A ordinary shares are not convertible into Class B ordinary shares under any circumstances. Upon any transfer of Class B ordinary shares by a holder thereof to any person or entity which is not an affiliate (as defined in our Memorandum and Articles of Association) of such holder, such Class B ordinary shares will be automatically and immediately converted into the equal number of Class A ordinary shares. In addition, if at any time Robin Yanhong Li and his affiliates (as defined in our Memorandum and Articles of Association) collectively own less than 5% of the total number of the issued and outstanding Class B ordinary shares, each issued and outstanding Class B ordinary share will be automatically and immediately converted into one Class A ordinary share, and we shall not issue any Class B ordinary shares thereafter.

Due to the disparate voting powers attached to these two classes, certain shareholders have significant voting power over matters requiring shareholder approval, including election of directors and significant corporate transactions, such as a merger or sale of our company or our assets. This concentrated control could discourage or prevent others from pursuing any potential merger, takeover or other change of control transactions with our company, which could deprive our shareholders and ADS holders of an opportunity to receive a premium for their shares or ADSs as part of a sale of our company and might reduce the price of our listed securities.

As we are seeking a listing as a Grandfathered Greater China Issuer pursuant to Chapter 19C of the Hong Kong Listing Rules (Secondary Listings of Qualifying Issuers) with a WVR structure, certain shareholder protection measures and governance safeguards under Chapter 8A of the Hong Kong Listing Rules (Weighted Voting Rights) do not apply to us pursuant to Rule 19C.12 and our Articles differ from Chapter 8A in a number of ways. As a result, our Articles provide less shareholder protection and have fewer governance safeguards than if our Company were subject to Chapter 8A in its entirety. For a summary of the key differences between our Articles and Chapter 8A, see the section “Information about the Listing—Our Articles of Association.”

Our Articles of Association contain anti-takeover provisions that could adversely affect the rights of holders of our ordinary shares and ADSs.

Our Articles of Association include certain provisions that could limit the ability of others to acquire control of our company, and therefore may deprive the holders of our ordinary shares and ADSs of the opportunity to sell their ordinary shares or ADSs at a premium over the prevailing market price by discouraging third parties from seeking to obtain control of our company in a tender offer or similar transactions. These provisions include the following:

- A dual-class ordinary share structure.

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- Our board of directors has the authority, without approval by the shareholders, to issue up to a total of 800,000,000 preferred shares in one or more series. Our board of directors may establish the number of shares to be included in each such series and may fix the designations, preferences, powers and other rights of the shares of a series of preferred shares.
- Our board of directors has the right to elect directors to fill a vacancy created by the increase of the board of directors or the resignation, death or removal of a director, which prevents shareholders from having the sole right to fill vacancies on our board of directors.

We are a foreign private issuer within the meaning of the rules under the U.S. Exchange Act, and as such we are exempt from certain provisions applicable to U.S. domestic public companies.

Because we qualify as a foreign private issuer under the U.S. Exchange Act, we are exempt from certain provisions of the securities rules and regulations in the United States that are applicable to U.S. domestic issuers, including:

- the rules under the U.S. Exchange Act requiring the filing with the SEC of quarterly reports on Form 10-Q or current reports on Form 8-K;
- the sections of the U.S. Exchange Act regulating the solicitation of proxies, consents, or authorizations in respect of a security registered under the U.S. Exchange Act;
- the sections of the U.S. Exchange Act requiring insiders to file public reports of their stock ownership and trading activities and liability for insiders who profit from trades made in a short period of time; and
- the selective disclosure rules by issuers of material nonpublic information under Regulation FD.

We are required to file an annual report on Form 20-F within four months of the end of each fiscal year. In addition, we intend to publish our results on a quarterly basis as press releases, distributed pursuant to the rules and regulations of Nasdaq. Press releases relating to financial results and material events will also be furnished to the SEC on Form 6-K. However, the information we are required to file with or furnish to the SEC will be less extensive and less timely compared to that required to be filed with the SEC by U.S. domestic issuers. As a result, you may not be afforded the same protections or information that would be made available to you were you **[REDACTED]** in a U.S. domestic issuer.

As a Cayman Islands exempted company listed on Nasdaq, we are subject to Nasdaq corporate governance listing standards. However, Nasdaq rules permit a foreign private issuer like us to follow the corporate governance practices of its home country. Certain corporate governance practices in the Cayman Islands, which is our home country, may differ significantly from Nasdaq corporate governance listing standards. For example, neither the Companies Act (2021 Revision) of the Cayman Islands nor our Memorandum and Articles requires a majority of our directors to be independent and we could include non-independent directors as members of our compensation committee and nominating committee, and our independent directors would not necessarily hold regularly scheduled meetings at which only independent directors are present. We follow home country practice with respect to annual meetings and do not hold an annual meeting of shareholders every year. We undertake we will (i) put forth a resolution at an extraordinary general meeting to be convened by December 31, 2021 (the “**2021 EGM**”) to revise our Articles so that we are required to convene an annual general meeting each year; (ii) the event that this resolution is not passed at the 2021 EGM, to convene an annual general meeting each year with at least 14 days of notice beginning from 2022 and (iii) for so long as we remain listed on the Hong Kong Stock Exchange, to continue to put forth the resolution at each of the annual general meetings after the 2021 EGM, until the resolution is passed,

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even though there may not be any resolutions to be approved by the shareholders at such meetings. If we choose to follow other home country practice in the future, our shareholders may be afforded less protection than they otherwise would under Nasdaq corporate governance listing standards applicable to U.S. domestic issuers.

We may be classified as a passive foreign investment company, or PFIC, which could result in adverse U.S. federal income tax consequence to U.S. Holders of our ADSs or ordinary shares.

A non-U.S. corporation, such as our own, will be considered a PFIC for any taxable year if either (i) at least 75% of its gross income is passive income or (ii) at least 50% of the value of its assets (based on an average of the quarterly values of the assets during a taxable year) is attributable to assets that produce or are held for the production of passive income. The value of our assets is generally determined by reference to the market price of the ADSs and ordinary shares, which may fluctuate considerably. In addition, because there are uncertainties in the application of the relevant rules and because PFIC status is a fact-intensive determination made on an annual basis, no assurance may be given with respect to our PFIC status for the current or any future taxable year.

Based on the market price of our ADSs and ordinary shares, the value of our assets, and the composition of our assets and income, we believe that we were not a PFIC for our taxable year ended December 31, 2020. However, given the lack of authority and the highly factual nature of the analyzes, no assurance can be given. Our PFIC status for the current taxable year ending December 31, 2021 will not be determinable until the close of the taxable year, there can be no assurance that we will not be a PFIC for the current taxable year (or any future taxable year).

If we were treated as a PFIC for any taxable year during which a U.S. Holder (defined below) held an ADS or an ordinary share, certain adverse U.S. federal income tax consequences could apply to the U.S. Holder. See “Item 10.E. Additional Information—Taxation—U.S. Federal Income Tax Considerations—Passive Foreign Investment Company” of our annual report on Form 20-F for our fiscal year ended December 31, 2019, originally filed with the SEC on March 13, 2020.

The different characteristics of the capital markets in Hong Kong and the U.S. may negatively affect the trading prices of our Class A ordinary shares and/or ADSs.

Upon the Listing, we will be subject to Hong Kong and Nasdaq listing and regulatory requirements concurrently. The Hong Kong Stock Exchange and Nasdaq have different trading hours, trading characteristics (including trading volume and liquidity), trading and listing rules, and [REDACTED] bases (including different levels of retail and institutional participation). As a result of these differences, the trading prices of our Class A ordinary shares and our ADSs may not be the same, even allowing for currency differences. Fluctuations in the price of our ADSs due to circumstances peculiar to the U.S. capital markets could materially and adversely affect the price of our Class A ordinary shares, or vice versa. Certain events having significant negative impact specifically on the U.S. capital markets may result in a decline in the trading price of our Class A ordinary shares notwithstanding that such event may not impact the trading prices of securities listed in Hong Kong generally or to the same extent, or vice versa. Because of the different characteristics of the U.S. and Hong Kong capital markets, the historical market prices of our ADSs may not be indicative of the trading performance of our Class A ordinary shares after the [REDACTED].

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Exchange between our Class A ordinary shares and our ADSs may adversely affect the liquidity and/or trading price of each other.

Our ADSs are currently traded on Nasdaq. Subject to compliance with U.S. securities law and the terms of the Deposit Agreement, holders of our Class A ordinary shares may deposit Class A ordinary shares with the depository in exchange for the issuance of our ADSs. Any holder of ADSs may also surrender ADSs and withdraw the underlying Class A ordinary shares represented by the ADSs pursuant to the terms of the Deposit Agreement for trading on the Hong Kong Stock Exchange. In the event that a substantial number of Class A ordinary shares are deposited with the depository in exchange for ADSs or vice versa, the liquidity and trading price of our Class A ordinary shares on the Hong Kong Stock Exchange and our ADSs on Nasdaq may be adversely affected.

The time required for the exchange between Class A ordinary shares and ADSs might be longer than expected and [REDACTED] might not be able to settle or effect any sale of their securities during this period, and the exchange of Class A ordinary shares into ADSs involves costs.

There is no direct trading or settlement between Nasdaq and the Hong Kong Stock Exchange on which our ADSs and our Class A ordinary shares are respectively traded. In addition, the time differences between Hong Kong and New York and unforeseen market circumstances or other factors may delay the deposit of Class A ordinary shares in exchange of ADSs or the withdrawal of Class A ordinary shares underlying the ADSs. [REDACTED] will be prevented from settling or effecting the sale of their securities during such periods of delay. In addition, there is no assurance that any exchange of Class A ordinary shares into ADSs (and vice versa) will be completed in accordance with the timelines [REDACTED] may anticipate.

Furthermore, the depository for the ADSs is entitled to charge holders fees for various services including for the issuance of ADSs upon deposit of Class A ordinary shares, cancellation of ADSs, distributions of cash dividends or other cash distributions, distributions of ADSs pursuant to share dividends or other free share distributions, distributions of securities other than ADSs and annual service fees. As a result, shareholders who exchange Class A ordinary shares into ADSs, and vice versa, may not achieve the level of economic return the shareholders may anticipate.

We are exposed to risks associated with any potential spin-off of one or more of our businesses.

We are exposed to risks associated with any potential spin-off of one or more of our businesses. We have applied for, and the Hong Kong Stock Exchange has granted, a waiver from strict compliance with the requirements in paragraph 3(b) of Practice Note 15 to the Hong Kong Listing Rules such that we are able to spin-off a subsidiary entity and list it on the Hong Kong Stock Exchange within three years of the Listing. While we do not have any specific plans with respect to the timing or details of any potential spin-off listing on the Hong Kong Stock Exchange as at the date of this document, we continue to explore the ongoing financing requirements for our various businesses and may consider a spin-off listing on the Hong Kong Stock Exchange for one or more of those businesses within the three year period subsequent to the Listing. As of the Latest Practicable Date, we have not identified any target for a potential spin-off; as a result we do not have any information relating to the identity of any spin-off target or any other details of any spin off and accordingly, there is no material omission of any information relating to any possible spin-off in this document. The waiver granted by the Hong Kong Stock Exchange is conditional upon us confirming to the Hong Kong Stock Exchange in advance of any spin-off that it would not render the Company, excluding the businesses to be spun off, incapable of fulfilling either the eligibility or suitability requirements under Rules 19C.02 and 19C.05 of the Hong Kong Listing Rules based on the financial information of the entity or entities to be spun-off at

RISK FACTORS

the time of the Company’s Listing (calculated cumulatively if more than one entity is spun-off). We cannot assure you that any spin-off will ultimately be consummated, whether within the three-year period after the Listing or otherwise, and any such spin-off will be subject to market conditions at the time and approval by the Listing Committee. In the event that we proceed with a spin-off, the Company’s interest in the entity to be spun-off (and its corresponding contribution to the financial results of our Group) will be reduced accordingly. For additional information, see “Waivers and Exemptions—Rules Relating to Spin-Off Listings.”

[REDACTED]

RISK FACTORS

[REDACTED]

THIS DOCUMENT IS IN DRAFT FORM, INCOMPLETE AND SUBJECT TO CHANGE AND THAT THE INFORMATION MUST BE READ IN CONJUNCTION WITH THE SECTION HEADED "WARNING" ON THE COVER OF THIS DOCUMENT

INFORMATION ABOUT THIS DOCUMENT AND THE [REDACTED]

[REDACTED]

THIS DOCUMENT IS IN DRAFT FORM, INCOMPLETE AND SUBJECT TO CHANGE AND THAT THE INFORMATION MUST BE READ IN CONJUNCTION WITH THE SECTION HEADED "WARNING" ON THE COVER OF THIS DOCUMENT

INFORMATION ABOUT THIS DOCUMENT AND THE [REDACTED]

[REDACTED]

INFORMATION ABOUT THIS DOCUMENT AND THE [REDACTED]

[REDACTED]

Exchange Rate Conversion

Our reporting currency is the Renminbi. This document contains translations of financial data in Renminbi and Hong Kong dollar amounts into U.S. dollars at specific rates solely for the convenience of the reader. Unless otherwise stated, all translations of financial data in Renminbi and Hong Kong dollars into U.S. dollars and from U.S. dollars into Renminbi in this document were made at a rate of RMB 6.5250 to US\$1.00 and HK\$ 7.7534 to US\$1.00, the respective exchange rate on December 31, 2020 set forth in the H.10 statistical release of the Federal Reserve Board.

No representation is made that any amounts in RMB or US\$ were or could have been or could be converted into Hong Kong dollars at such rates or any other exchange rates on such date or any other date.

Rounding

Certain amounts and percentage figures included in this document have been subject to rounding adjustments. Accordingly, figures shown as totals in certain tables may not be an arithmetic aggregation of the figures preceding them.

INFORMATION ABOUT THIS DOCUMENT AND THE [REDACTED]

Language

If there is any inconsistency between this document and its Chinese translation, this document shall prevail, provided that if there is any inconsistency between the Chinese names of the entities or enterprises established in the PRC mentioned in this document and their English translations, the Chinese names shall prevail. The English translations of the Chinese names of such PRC entities or enterprises are provided for identification purposes only.

[REDACTED]

INFORMATION ABOUT THE LISTING

The Listing

We have applied for a listing of our Class A ordinary shares on the Main Board under Chapter 19C (Secondary Listings of Qualifying Issuers).

We have a track record of good regulatory compliance of at least two full financial years on Nasdaq as required by Rule 19C.04 of the Hong Kong Listing Rules for the purposes of our Listing.

We have applied to the Listing Committee for the listing of, and permission to deal in, our Class A ordinary shares in issue and to be issued pursuant to the [REDACTED] (including the Class A ordinary shares which may be issued pursuant to the exercise of the [REDACTED]) and the Class A ordinary shares to be issued pursuant to the Share Incentive Plans, including pursuant to the exercise of options or other awards that have been or may be granted from time to time and the Class A ordinary shares to be issued after the conversion of Class B ordinary shares.

Our ADSs are currently listed and traded on Nasdaq. We also have outstanding debt securities listed and traded on Singapore Exchange Securities Trading Limited. Other than the foregoing, no part of our Shares or loan capital is listed on or traded on any other stock exchange and no such listing or permission to list is being or proposed to be sought. All [REDACTED] will be registered on the [REDACTED] in order to enable them to be traded on the Hong Kong Stock Exchange.

[REDACTED]

INFORMATION ABOUT THE LISTING

[REDACTED]

INFORMATION ABOUT THE LISTING

[REDACTED]

INFORMATION ABOUT THE LISTING

[REDACTED]

INFORMATION ABOUT THE LISTING

[REDACTED]

Summary of Exemptions as a Foreign Private Issuer in the U.S.

As required by Rule 19C.14 of the Hong Kong Listing Rules, set forth below is a summary of the exemptions from obligations under U.S. securities laws and Nasdaq rules that we enjoy as a foreign private issuer in the U.S.

Exemptions from Nasdaq rules

Foreign private issuers are exempted from certain corporate governance requirements of Nasdaq. Foreign private issuers are permitted to follow home country practice, i.e. for us, the practice of the Cayman Islands, in lieu of such corporate governance requirements, as long as they disclose any significant ways in which their corporate governance practices differ from those required under Nasdaq listing standards and explain the basis for the conclusion that the exemption is applicable. Specifically, we currently enjoy the exemption from requirements to hold annual shareholders meetings. We follow home country practice with respect to annual meetings and did not hold an annual meeting of shareholders in 2019. However, we undertake that (i) put forth a resolution at an extraordinary general meeting to be convened by December 31, 2021 (the “**2021 EGM**”) to revise our Articles so that we are required to convene an annual general meeting each year; (ii) the event that this resolution is not passed at the 2021 EGM, to convene an annual general meeting each year with at least 14 days of notice beginning from 2022 and (iii) for so long as we remain listed on the Hong Kong Stock Exchange, to continue to put forth the resolution at each of the annual general meetings after the 2021 EGM, until the resolution is passed, even though there may not be any resolutions to be approved by the shareholders at such meetings. See “Information about the Listing – Our Articles of Association” for further details. Other than the annual meeting practice described above, there are no significant differences between our corporate governance practices and those followed by U.S. domestic companies under Nasdaq Stock Market Rules.

Exemptions from SEC rules and regulations under U.S. federal securities laws

Foreign private issuers are exempted from Regulation FD under the U.S. Exchange Act. Regulation FD provides that when a domestic U.S. issuer, or someone acting on its behalf, discloses material nonpublic information to certain persons (including securities analysts, other securities market professionals, and holders of the issuer’s securities who could reasonably be expected to trade on the basis of the information), it must make simultaneous public disclosure of that information (in the case of intentional disclosure) or prompt public disclosure (in the case of non-intentional disclosure). However, the SEC expects foreign private issuers to conduct themselves in accordance with the basic principles underlying Regulation FD.

Section 16 of the U.S. Exchange Act does not apply to foreign private issuers. Therefore, directors, executive officers and 10% beneficial owners of foreign private issuers are not required to file Forms

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3, 4 and 5 with the SEC, and are not required to disgorge to the issuer any profits realized from any non-exempt purchase and sale, or non-exempt sale and purchase, of the issuer’s equity securities or security-based swap agreements within a period of less than six months.

Foreign private issuers are exempt from the SEC’s rules prescribing the furnishing and content of proxy statements under the U.S. Exchange Act, which specify the procedures and required documentation for soliciting shareholder votes. Accordingly, foreign private issuers are not required to disclose certain information in their annual proxy statements, such as whether the work of any compensation consultant has played any role in determining or recommending the form or amount of executive and director compensation has raised a conflict of interest, and, if so, the nature of the conflict and how it is being addressed.

Foreign private issuers are also not required under the U.S. Exchange Act to file periodic reports and financial statements with the SEC as frequently or as promptly as domestic U.S. issuers with securities registered under the U.S. Exchange Act. As a result, our shareholders may be afforded less protection than they would under the U.S. Exchange Act rules applicable to domestic U.S. issuers. Unlike domestic U.S. issuers, foreign private issuers are not required to file quarterly reports (including quarterly financial information) on Form 10-Q. They also are not required to use Form 8-K for current reports, and instead furnish (not file) current reports on Form 6-K with the SEC.

Annual reports on Form 10-K by domestic U.S. issuers are due within 60, 75, or 90 days after the end of the issuer’s fiscal year, depending on whether the company is a “large accelerated filer,” a “accelerated filer,” or a “non-accelerated filer.” By contrast, the deadline for foreign private issuers to file annual reports on Form 20-F is four months after the end of their fiscal year.

Our Articles of Association

We are an exempted company incorporated in the Cayman Islands with limited liability and our affairs are governed by our Memorandum and Articles of Association, the Cayman Companies Act and the common law of the Cayman Islands.

The laws of Hong Kong differ in certain respects from the Cayman Companies Act, and our Articles of Association are specific to us and include certain provisions that may be different from common practices in Hong Kong. For example:

- Rule 19C.07 of the Hong Kong Listing Rules provides that the Hong Kong Stock Exchange will consider that an issuer such as us seeking a listing under Chapter 19C has met the requirements of Rule 19.30(1)(b) of the Hong Kong Listing Rules for standards of shareholder protection if it has met the shareholder protection standards by reference to eight criteria set out in Rule 19C.07.
- Rule 19C.07(1)(c) of the Hong Kong Listing Rules requires a voluntary winding-up of the Qualifying Issuer to be approved by a super-majority vote of the Company’s members in general meeting. Article 117 of the Company’s Articles currently state that 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 Companies Act, divide amongst the shareholders the whole or any part of the assets of the Company, and therefore satisfies the requirement under Rule 19C.07(1)(c) of the Listing Rules.
- Rule 19C.07(3) of the Hong Kong Listing Rules requires the appointment, removal and remuneration of auditors to be approved by a majority of a Qualifying Issuer’s (as defined in the

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Hong Kong Listing Rules) members or other body that is independent of the issuer’s board of directors), but our Articles of Association do not contain this or a similar provision.

- Rule 19C.07(4) of the Hong Kong Listing Rules requires a Qualifying Issuer to hold a general meeting each year as its annual general meeting, but holding a general meeting each year is not specifically required under our Articles of Association. We undertake to put forth a resolution at an extraordinary general meeting of the Company to be convened by December 31, 2021, for which 14 days’ notice will be given to our members (the “**2021 EGM**”), to revise the Articles, so that we are required to convene an annual general meeting each year. In the event that this resolution is not passed at the 2021 EGM, we undertake to convene an annual general meeting each year with at least 14 days of notice beginning from 2022.
- Rule 19C.07(5) of the Hong Kong Listing Rules requires a Qualifying Issuer to give its members reasonable written notice of its general meetings, and our Articles of Association provide that any general meetings may be called by not less than 5 days’ notice. While we are of the view that such notice period is reasonable and this notice period has been adopted since our listing on Nasdaq in 2005, we undertake to put forth a resolution at the 2021 EGM, to revise the Articles, so that we are required to provide at least 14 days’ notice for any general meetings of our Company. Prior to this resolution being passed, we undertake to provide 14 days’ notice for any general meetings after the Listing.
- Rule 19C.07(6) of the Hong Kong Listing Rules requires a member to abstain from voting to approve a matter in circumstances required by the Hong Kong Listing Rules. We undertake to put forth a resolution at the 2021 EGM to revise the Articles so that a member’s right to vote is subject to the Hong Kong Listing Rules. Pending this amendment to our Articles, we will stipulate in our proxy statement that a member with material interest in a transaction or arrangement will be required to abstain from voting on resolutions relating to such transaction or arrangement.
- Rule 19C.07(7) of the Hong Kong Listing Rules requires that members holding a minority shareholding in an issuer’s total number of issued shares must be able to requisition an extraordinary general meeting and add resolutions to a meeting agenda. The minimum stake required to do so must not be higher than 10% of the voting rights, on a one vote per share basis, in the share capital of the of the issuer, while the minimum stake set out in our Articles of Association is not less than a majority of the votes attaching to all issued and outstanding Shares. We undertake to put forth a resolution in the 2021 EGM to revise the Articles so that the minimum stake required to convene an extraordinary general meeting and add resolutions to a meeting agenda will be 10% of the voting rights, on a one vote per share basis, in our share capital. Prior to amendment to our Articles, we undertake to convene general meetings at the request of our Shareholders holding in aggregate not less than 10% of our voting rights, on a one vote per share basis.
- Rule 19C.07(8) of the Hong Kong Listing Rules requires that HKSCC must be entitled to appoint proxies or corporate representatives to attend an issuer’s general meetings and creditors meetings and those proxies/corporate representatives must enjoy rights comparable to the rights of other shareholders, including the right to speak and vote. Our Articles of Association provide that any corporation which is a member of the Company to authorize such person as it thinks fit to act as its representative at any meetings of the Company, and that person so authorized shall be entitled to exercise the same powers on behalf of the corporation which he represents as the corporation could exercise if it were an individual member of the Company. The Company’s legal adviser as to Cayman Islands laws has confirmed that our Articles do not prevent HKSCC from appointing more than one corporate representative or more than one proxy that would enjoy rights comparable to the rights of other shareholders, including the right to speak and vote.

INFORMATION ABOUT THE LISTING

Our Controlling Shareholders (being Mr. Robin Yanhong Li and Handsome Reward Limited, which is wholly-owned and controlled by Mr. Li) and Ms. Melissa Ma, Mr. Li’s spouse, will give an irrevocable undertaking to our Company prior to the Listing to use their voting rights to vote in favor of the proposed resolutions outlined above. See “Waivers and Exemptions” for further details, and “Summary of our Constitution and Cayman Companies Act” as set out in Appendix III to this document.

Weighted Voting Rights Structure

Our weighted voting rights structure is specific to us and contain certain features that are different from the requirements under Chapter 8A of the Hong Kong Listing Rules. Material differences in shareholder protection and corporate governance safeguards are set out below:

| <u>Requirement under Chapter 8A of the Hong Kong Listing Rules</u> | <u>Our weighted voting rights structure</u> |
|---|---|
| Rule 8A.11 of the Hong Kong Listing Rules states that at listing, any beneficiaries of weighted voting rights must be members of the applicant’s board of directors. | Immediately upon the completion of the [REDACTED], the WVR beneficiaries will be Mr. Robin Yanhong Li, the chairman and chief executive officer of the Company, Ms. Melissa Ma, the spouse of Mr. Li, and holders of Class B ordinary shares that were affiliated with early stage legacy investors of the Company prior to the listing on Nasdaq. For further details, please see “Share Capital—Weighted Voting Rights Structure”. |
| Rule 8A.17 of the Hong Kong Listing Rules require cessation of weighted voting rights if (i) the beneficiary is deceased; (ii) no longer a member of the issuer’s board of directors; (iii) deemed by the Hong Kong Stock Exchange to be incapacitated for the purpose of performing his or her duties as a director; or (iv) deemed by the Hong Kong Stock Exchange to no longer meet the requirements of a director set out in the Hong Kong Listing Rules. | Subject to the provisions of our Articles of Association, each Class B ordinary share is convertible into one Class A ordinary share at any time by the shareholder. If at any time Mr. Robin Yanhong Li and his affiliates collectively own less than 5% of the total number of issued and outstanding Class B ordinary shares, each issued and outstanding Class B ordinary shares will be automatically and immediately converted into one Class A ordinary shares, and no Class B ordinary shares could be issued by us thereafter. The Class B ordinary shares will be automatically and immediately converted into an equal number of Class A ordinary share (i) upon any sale, pledge, transfer, assignment or disposition of the Class B ordinary shares by the shareholder to any person or entity which is not his/her affiliate; or (ii) where the shareholder has made a transfer of the Class B ordinary shares to his/her affiliate, there is a change of the beneficial ownership of such Class B ordinary shares held by the affiliate. |
| Rule 8A.18(1) of the Hong Kong Listing Rules requires weighted voting rights attached to a beneficiary’s shares to cease upon 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). | |
| Rule 8A.18(2) of the Hong Kong Listing Rules states that a limited partnership, trust, private company or other vehicle may hold shares carrying weighted voting rights on behalf of a beneficiary of weighted voting rights, provided that such an arrangement does not result in a circumvention of Rule 8A.18(1) of the Hong Kong Listing Rules. | |

INFORMATION ABOUT THE LISTING

Requirement under Chapter 8A of the Hong Kong Listing Rules

Under Rule 8A.23 of the Hong Kong Listing Rules, non-WVR shareholders must be able to convene an extraordinary general meeting and add resolutions to the meeting agenda. The minimum stake required to do so must not be higher than 10% of the voting rights on a one vote per share basis in the share capital of the listed issuer.

Rule 8A.24 of the Hong Kong Listing Rules requires weighted voting rights to be disregarded on any resolution to approve certain matters, including (i) changes to the listed issuer’s constitutional documents, however framed; (ii) variation of rights attached to any class of shares; (iii) the appointment or removal of an independent non-executive director; (iv) the appointment or removal of auditors; and (v) the voluntary winding-up of the listed issuer.

Rule 8A.30 of the Hong Kong Listing Rules requires issuer with a WVR structure must establish a Corporate Governance Committee with at least the terms of reference set out in Code Provision D.3.1 of Appendix 14 to the Hong Kong Listing Rules and additional terms as set out under Rule 8A.30 of the Hong Kong Listing Rules.

Our weighted voting rights structure

The holders of Class B ordinary shares that were affiliated with early stage legacy investors of the Company prior to the listing on Nasdaq are corporate shareholders that carry weighted voting rights and are not controlled by any of the directors of the Company.

The minimum stake as currently set out in our Articles of Association is different from the requirement. For further details, please see “Information About the Listing—Our Articles of Association” and “Waivers and Exemptions—Shareholders Protection Requirements.”

Under our weighted voting rights structure, each Class B ordinary share entitles the holder to exercise 10 votes on all matters subject to the vote at general meetings of our Company.

The charter of our corporate governance and nominating committee does not contain the terms otherwise required under Rule 8A.30 and Code Provision D.3.1 of Appendix 14 to the Hong Kong Listing Rules.

With respect to Rule 8A.30 of the Hong Kong Listing Rules, the charter does not contain the following terms: (1) review and monitor whether the listed issuer is operated and managed for the benefit of all its shareholders; (2) confirm, on an annual basis, that the beneficiaries of WVR have been members of the listed issuer’s board of directors throughout the year and that no matters under rule 8A.17 (relating to cessation of WVR) have occurred during the relevant financial year; (3) confirm, on an annual basis, whether or not the beneficiaries of WVR have complied with rules 8A.14 (relating to issue of shares carrying weighted voting rights), 8A. 15 (relating to purchase of own shares), 8A.18 (relating to

INFORMATION ABOUT THE LISTING

Requirement under Chapter 8A of the Hong Kong Listing Rules

Our weighted voting rights structure

restriction on transfer of shares with weighted voting rights) and 8A.24 (relating to matters requiring voting on a one vote per share basis) throughout the year; (4) review and monitor the management of conflicts of interests and make a recommendation to the board on any matter where there is a potential conflict of interest between the issuer, a subsidiary of the issuer and/or shareholders of the issuer (considered as a group) on one hand and any beneficiary of WVR on the other; (5) review and monitor all risks related to the issuer’s WVR structure; (6) make a recommendation to the board as to the appointment or removal of the Compliance Adviser; (7) seek to ensure effective and on-going communication between the issuer and its shareholders; (8) report on the work of the committee on at least a half-yearly and annual basis covering all areas of its terms of reference; and (9) to disclose, on a comply or explain basis, its recommendations to the board in respect of the matters in (4) to (6) above.

With respect to Code Provision D.3.1 of Appendix 14 to the Hong Kong Listing Rules, the charter does not contain the following terms: (1) review and monitor the training and continuous professional development of directors and senior management; (2) review and monitor the issuer’s policies and practices on compliance with legal and regulatory requirements; and (3) review the issuer’s compliance with the corporate governance code and disclosure in the corporate governance report.

As we have applied for a listing of our Class A ordinary shares on the Main Board under Chapter 19C of the Hong Kong Listing Rules as a Grandfathered Greater China Issuer, we will not be subject to, among others, the above provisions of the Hong Kong Listing Rules with respect to weighted voting rights structure as set out under Rule 19C.12 of the Hong Kong Listing Rules. This may afford lower level of shareholder protection to our Shareholders.

INFORMATION ABOUT THE LISTING

Compliance Advisor

We have appointed Somerley Capital Limited as our compliance advisor, or the Compliance Advisor, upon listing of our Class A ordinary shares on the Hong Kong Stock Exchange in compliance with Rule 3A.19 of the Hong Kong Listing Rules. Pursuant to Rule 3A.23 of the Hong Kong Listing Rules, the Compliance Advisor will provide advice to us when consulted by us in the following circumstances:

- (a) before the publication of any regulatory announcement, circular, or financial report;
- (b) where the business activities, development or results of our Company deviate from any forecast, estimate or other information in this document; and
- (c) where the Hong Kong Stock Exchange makes an inquiry to the Company regarding unusual movements in the price or trading volume of our Class A ordinary shares or any other matters in accordance with Rule 13.10 of the Hong Kong Listing Rules.

The term of the appointment shall commence on the Listing Date and end on the date on which we distribute our annual report in respect of our financial results for the first full fiscal year commencing after the Listing Date.

WAIVERS AND EXEMPTIONS

In preparation for the Listing, we have sought the following waivers and exemptions from strict compliance with the relevant provisions of the Hong Kong Listing Rules, the SFO and the Companies (Winding Up and Miscellaneous Provisions) Ordinance and have applied for a ruling under the Takeovers Codes:

| Rules | Subject matter |
|--|--|
| Rule 2.07A of the Hong Kong Listing Rules | Printed Corporate Communications |
| Rules 4.04(3)(a), 4.05(2) and 4.13 of the Hong Kong Listing Rules and Paragraph 31(3)(b) of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance | Disclosure Requirements Relating to the Accountants' Reports |
| Rule 9.09(b) of the Hong Kong Listing Rules | Dealings in Shares prior to Listing |
| [REDACTED] | |
| Rule 13.25B of the Hong Kong Listing Rules | Monthly Return |
| Rule 13.46(2)(b) of the Hong Kong Listing Rules | Laying Annual Financial Statements Before Members at an Annual General Meeting Within Six Months After the End of Financial Year |
| Rules 19C.07(3) and 19C.07(7) of the Hong Kong Listing Rules | Shareholder Protection Requirements |
| Paragraphs 13 and 26 of Appendix 1A to the Hong Kong Listing Rules and Paragraphs 11, 14 and 25 of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance | Particulars of any Commissions, Discounts and Brokerages, Alterations of Capital and Authorized Debentures |
| Paragraph 29(1) of Appendix 1A to the Hong Kong Listing Rules and Paragraph 29 of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance | Disclosure of Information on Subsidiaries Whose Profits or Assets Make Material Contributions to Us |
| Guidance Letter HKEX-GL37-12 | Timing Requirement of Liquidity Disclosure |
| Paragraphs 33(2), 33(3), 46(2), 46(3) of Appendix 1A to the Hong Kong Listing Rules | Disclosure Requirements of the Remuneration of Directors and Five Individuals Whose Emoluments Were Highest |
| Paragraphs 41(4) and 45 of Appendix 1A to and Practice Note 5 of the Hong Kong Listing Rules | Disclosure of Interests Information |

[REDACTED]

WAIVERS AND EXEMPTIONS

| <u>Rules</u> | <u>Subject matter</u> |
|--|---|
| Rule 10.04 and Paragraph 5(2) of Appendix 6 to the Hong Kong Listing Rules | Subscription for Shares by existing Shareholders |
| [REDACTED] | |
| Rules 4.04(2) and 4.04(a) of the Hong Kong Listing Rules | Investments after the Track Record Period |
| Paragraph 27 of Appendix 1A of the Hong Kong Listing Rules and Paragraph 10 of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance | Disclosure Requirements of Options |
| Paragraph 3(b) of Practice Note 15 of the Hong Kong Listing Rules | Rules related to spin-off listings |
| Rule 8A.39 of the Hong Kong Listing Rules | Disclosure of ultimate beneficial owners of Other WVR Beneficiaries |
| Section 4.1 of the Introduction to the Takeovers Codes | Not a public company in Hong Kong under Takeovers Code |
| Part XV of the SFO | Disclosure of interests under Part XV of the SFO |

PRINTED CORPORATE COMMUNICATIONS

Rule 2.07A of the Hong Kong Listing Rules provides that a listed issuer may send or otherwise make available to the relevant holders of its securities any corporate communication by electronic means, provided that either the listed issuer has previously received from each of the relevant holders of its securities an express, positive confirmation in writing or the shareholders of the listed issuer have resolved in a general meeting that the listed issuer may send or supply corporate communications to shareholders by making them available on the listed issuer's own website or the listed issuer's constitutional documents contain provision to that effect, and certain conditions are satisfied.

Our ADSs have been listed on the Nasdaq since 2005. We have a diverse shareholder base with ADS holders globally.

We do not currently produce or send out any corporate communications to our shareholders or holders of ADSs in printed form unless requested or in limited circumstances. We publicly file or furnish various corporate communications with the SEC which are posted on the SEC's website. Our annual reports on Form 20-F and current reports on Form 6-K and all amendments to these reports, are also available free of charge on our website as soon as reasonably practicable after they are filed with or furnished to the SEC. Further, we will post our proxy materials and notices to our shareholders and holders of ADSs on a publicly accessible website. Those documents will also be available on our website. In addition, the depositary bank which administers our ADS program will send a notice as well as an ADS voting instruction card to our ADS holders for annual general meetings and extraordinary general meetings.

Apart from the [REDACTED] that we will [REDACTED] for subscription by the [REDACTED], the [REDACTED] will be placed to professional, institutional, corporate and other [REDACTED] in [REDACTED] and elsewhere in the world. Given our diverse shareholder base and the potential number of countries in which our shareholders are located, we consider that it would not be

WAIVERS AND EXEMPTIONS

practicable for us to send printed copies of all our corporate communications to all of our shareholders. Further, we consider that it would also not be practicable for us to approach our existing shareholders individually to seek confirmation from them of their wish to receive corporate communications in electronic form, or to provide them with the right to request corporate communications in printed form instead.

We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with Rule 2.07A of the Hong Kong Listing Rules on the conditions that we will:

- (a) issue all future corporate communications as required by the Hong Kong Listing Rules on our own website in English and Chinese, and on the Hong Kong Stock Exchange’s website in English and Chinese;
- (b) provide printed copies of proxy materials in English to our shareholders at no costs upon request; and
- (c) ensure that the “Investor Relations” page of our website (ir.baidu.com) will direct **[REDACTED]** to all of our future filings with the Hong Kong Stock Exchange.

DISCLOSURE REQUIREMENTS RELATING TO THE ACCOUNTANTS’ REPORTS

Rules 4.04(3)(a), 4.05(2) and 4.13 of the Hong Kong Listing Rules and Paragraph 31(3)(b) of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance set out certain historical financial information to be included in a listing document that is not required to be disclosed under U.S. GAAP, including in particular:

- (a) balance sheet at a company level;
- (b) aging analysis of accounts receivables;
- (c) aging analysis of accounts payables; and
- (d) adjustments made to show profits of all periods in accordance with the relevant accounting standards in relation to the last fiscal year reported on.

In accordance with U.S. GAAP, we have applied the modified retrospective transition method or prospective transition method to account for the impact of the adoption of the new accounting standards in the Track Record Period. Under the modified retrospective method and prospective method adopted by us, comparative periods in the latest consolidated financial statements are not retrospectively adjusted.

During the Track Record Period, we adopted, among other new accounting standards that did not have a material impact on our consolidated financial statements, Accounting Standards Update 2016-02 “Leases (Topic 842)”, including certain transitional guidance and subsequent amendments (“**ASU 2016-02**”), Accounting Standards Update 2016-13 “Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments”, including certain transitional guidance and subsequent amendments (“**ASC 2016-13**”), and Accounting Standards Update 2019-02 “Entertainment – Films – Other Assets – Film Costs (Subtopic 926-20) and Entertainment – Broadcasters – Intangibles – Goodwill and Other (Subtopic 920-350)” (“**ASC 2019-02**”). The relevant accounting policies upon the adoption of these new accounting standards are disclosed in the Accountants’ Report in Appendix IA and Accountant’s Report of YY Live in Appendix IB to this document.

ASU 2016-02 was adopted on January 1, 2019 using the modified retrospective transition method by applying the new lease standard to all leases existing as of January 1, 2019, and no adjustments were

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made to the comparative periods. The adoption of the new lease standard does not have any significant impact on the consolidated statements of comprehensive income and cash flows and there was no adjustment to the opening balance of retained earnings on January 1, 2019.

ASU 2016-13 was adopted on January 1, 2020 using the modified retrospective method. The cumulative effect of adopting ASU 2016-13 resulted in decreasing the opening balance of retained earnings on January 1, 2020 by RMB314 million, including the allowance for credit losses for account receivable, contract assets and debt securities. For YY Live, the cumulative effect of adopting ASU2016-13 resulted in increasing the opening balance of parent company deficit on January 1, 2020 by RMB785,000.

ASU 2019-02 was adopted on January 1, 2020 using the prospective transition method. After the adoption, the Company reported cash outflows for the costs incurred to obtain rights for both produced and licensed content as operating cash outflows in the statement of cash flows. The adoption of ASU 2019-02 does not have any significant impact on the consolidated balance sheets and there was no adjustment to the opening balance of retained earnings on January 1, 2020 as the prospective transition method was used.

This document includes the following alternative disclosures:

- (a) disclosure of the accounting policy for the adoption of ASU 2016-02 which came into effect on January 1, 2019, as well as the impact of adoption, if any, in the Accountants' Report in Appendix IA and Accountant's Report of YY Live in Appendix IB to this document;
- (b) disclosure of the accounting policies for the adoption of ASU 2016-13 and ASU 2019-02 which came into effect on January 1, 2020, as well as the impact of adoption, if any, in the Accountants' Report in Appendix IA and Accountant's Report of YY Live in Appendix IB to this document; and
- (c) for the new accounting standards that came into effect during the Track Record Period, the accounting policies as well as the impact of adoption, if any, to the retained earnings of initial application (i.e. January 1, 2019 and 2020) has been disclosed in the Accountants' Report in Appendix IA and Accountant's Report of YY Live in Appendix IB to this document, in accordance with the relevant requirements under U.S. GAAP.

As this document has included the above alternative disclosures and the current disclosure in this document contains all information which is necessary for the [REDACTED] to make an informed assessment of the business, asset and liability, financial position, trading position, management and prospect of the Group, we believe that it would be of no material value to the [REDACTED] and be unduly burdensome for the Accountants' Report in Appendix IA and Accountant's Report of YY Live in Appendix IB to this document to include certain required information pursuant to Rules 4.04(3)(a), 4.05(2) and 4.13 of the Hong Kong Listing Rules and Paragraph 31(3)(b) of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance and that the non-disclosure of such information will not prejudice the interests of [REDACTED].

We are of the view that all material information necessary for the public to make an informed assessment of the business, asset and liability, financial position, trading position, management and prospect of our Group has been disclosed in this document, and as such the granting of the waiver and exemption from strict compliance with the relevant content requirements under the Companies (Winding Up and Miscellaneous Provisions) Ordinance and the Hong Kong Listing Rules will not prejudice the interest of the [REDACTED] public.

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We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with the requirements under Rules 4.04(3)(a), 4.05(2) and 4.13 of the Hong Kong Listing Rules. We have applied for[, and the SFC has granted,] an exemption from the requirements under Paragraph 31(3)(b) of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance, to the extent not strictly met by the current disclosure in this document. The SFC has granted the above exemption on the conditions that: (i) the particulars of such exemption are set out in this document; and (ii) this document will be issued on or before [REDACTED].

DEALINGS IN SHARES PRIOR TO [REDACTED]

According to Rule 9.09(b) of the Hong Kong Listing Rules, there must be no dealing in the securities of a new applicant for which listing is sought by any core connected person of the issuer from four clear business days before the expected hearing date until listing is granted (the “**Relevant Period**”).

We had more than 200 subsidiaries and operating entities as of December 31, 2020, and our ADSs are widely held, publicly traded and listed on Nasdaq. We consider that we are therefore not in a position to control the investment decisions of our shareholders or the investing public in the US. As of the Latest Practicable Date, solely based on public filings with the SEC, other than Mr. Robin Yanhong Li, our chief executive officer, chairman of the Board and Controlling Shareholder, individually and through Handsome Reward Limited, which is wholly-owned and controlled by Mr. Robin Yanhong Li, there are no shareholders who held more than 10% of the total issued share capital of us.

Mr. Robin Yanhong Li (our chief executive officer, chairman of the Board and Controlling Shareholder) may from time to time use his Shares as security (including charges and pledges) in connection with financing activities. As of the Latest Practicable Date, none of the Shares beneficially owned by Mr. Li (both in his personal capacity and through Handsome Reward Limited) were used as security.

Furthermore, for a company whose securities are listed and traded in the U.S., we note that it is a common practice for substantial shareholders and corporate insiders, including directors, executives and other members of management, to set up trading plans that meet the requirements of Rule 10b5-1 under the U.S. Exchange Act (the “**Rule 10b5-1 Plans**”) to buy or sell the company’s securities. A Rule 10b5-1 Plan is a written plan, set up with a broker, to trade securities that (a) is entered into at a time when the person trading the securities is not aware of any material non-public information; (b) specifies the amount or value of securities to be purchased or sold and the price at which and the date on which the securities were to be purchased or sold; and (c) does not allow the person trading the securities to exercise any subsequent influence over how, when, or whether to effect purchases or sales. Persons who trade securities pursuant to a Rule 10b5-1 Plan have an affirmative defense against insider trading allegations under U.S. securities law.

On the basis of the above, we consider that the following categories of persons (collectively, the “**Permitted Persons**”) should not be subject to the dealing restrictions set out in Rule 9.09(b) of the Hong Kong Listing Rules:

- (a) Mr. Robin Yanhong Li, our chief executive officer, chairman of the Board and Controlling Shareholder, in respect of (i) use of his Shares as security (including, for the avoidance of doubt, using Shares as security in connection with entering into financing transactions during the Relevant Period as well as satisfying any requirements to top-up security under the terms of financing transactions entered into prior to the Relevant Period), provided that there will be no

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- change in the beneficial ownership of the Shares at the time of entering into any such transactions during the Relevant Period and (ii) the respective dealings by Mr. Li and his close associates pursuant to Rule 10b5-1 Plan that they have set up prior to the Relevant Period (“**Category 1**”);
- (b) our directors other than Mr. Robin Yanhong Li, and the directors and chief executives of our Significant Subsidiaries, in respect of (i) their respective use of the Shares as security (including, for the avoidance of doubt, using Shares as security in connection with entering into financing transactions during the Relevant Period as well as satisfying any requirements to top-up security under the terms of financing transactions entered into prior to the Relevant Period), provided that there will be no change in the beneficial ownership of the Shares at the time of entering into any such transactions during the Relevant Period and (ii) their respective dealings pursuant to Rule 10b5-1 Plans that they have set up prior to the Relevant Period (“**Category 2**”);
 - (c) directors, chief executives and substantial shareholders of our non-Significant Subsidiaries and their close associates (“**Category 3**”); and
 - (d) any other person (whether or not an existing Shareholder) who may, as a result of dealings, become our substantial shareholder and who is not our director or chief executive, or a director or chief executive of our subsidiaries, or their close associates (“**Category 4**”).

For the avoidance of doubt:

- (a) as the foreclosure, enforcement or exercise of other rights by the lenders in respect of a security interest over the Shares (including, for the avoidance of doubt, any security interest created pursuant to any top-up of security) will be subject to the terms of the financing transaction underlying such security and not within the control of the pledgor, any change in the beneficial owner of the Shares during the Relevant Period resulting from the foreclosure, enforcement or exercise of other rights by the lenders in respect of such security interest will not be subject to Rule 9.09(b) of the Hong Kong Listing Rules; and
- (b) persons in Category 1 and Category 2 who use their respective Shares other than as described in this section headed “Dealings in Shares prior to Listing” are subject to the restrictions under Rule 9.09(b) of the Hong Kong Listing Rules.

We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with Rule 9.09(b) of the Hong Kong Listing Rules to be granted on the following conditions:

- (a) Categories 1 and 2 of the Permitted Persons who entered into Rule 10b5-1 Plans have no discretion over dealings in the Company’s ADSs after the plans have been entered into. Where Categories 1 and 2 of the Permitted Persons use the Shares as security, there will be no change in the beneficial ownership of the Shares during the Relevant Period;
- (b) Categories 3 and 4 of the Permitted Persons do not have any influence over the [REDACTED] and do not possess any non-public inside information of our Company given that such persons are not in a position with access to information that is considered material to our Company taken as a whole. Given the large number of our subsidiaries and our vast ADS holder base, our Company and our management do not have effective control over the investment decisions of Categories 3 and 4 of the Permitted Persons in our ADSs;
- (c) we will promptly release any inside information to the public in the United States and Hong Kong in accordance with the relevant laws and regulations of the U.S. and Hong Kong. Accordingly, the Permitted Persons (other than Category 1 and Category 2 persons) are not in possession of any non-public inside information of which we are aware;

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- (d) we will notify the Hong Kong Stock Exchange of any breaches of the dealing restrictions by any of our core connected persons during the Relevant Period when it becomes aware of the same other than dealings by the core connected persons who are Permitted Persons within the permitted scopes set out above; and
- (e) prior to the Listing Date, other than within the permitted scopes set out above, our directors and chief executive and the directors and chief executives of our Significant Subsidiaries and their close associates will not deal in the Shares or the ADSs during the Relevant Period provided that such prohibited dealing in the Shares shall not include the granting, vesting, payment or exercise (as applicable) of RSUs, incentive and non-statutory options, restricted shares, dividend equivalents, and share payments under the Group’s share incentive plans.

[REDACTED]

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[REDACTED]

MONTHLY RETURN

Rule 13.25B of the Hong Kong Listing Rules requires a listed issuer to publish a monthly return in relation to movements in our equity securities, debt securities and any other securitized instruments, as applicable, during the period to which the monthly return relates.

Under the Joint Policy Statement, this common waiver is subject to the condition that the issuer can meet one of the following three conditions:

- (a) it has received a relevant partial exemption from Part XV of the SFO; or
- (b) it publishes a “next day disclosure return” in strict compliance with Rule 13.25A of the Hong Kong Listing Rules, regardless of the waiver of general effect from this Rule for secondary listed issuers; or
- (c) it is subject to overseas laws or regulations that have a similar effect to Rule 13.25B of the Hong Kong Listing Rules and any differences are not material to shareholder protection.

[We have obtained] a relevant partial exemption from strict compliance with Part XV of the SFO. We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with the continuing obligations under Rule 13.25B of the Hong Kong Listing Rules. We will disclose information about share repurchases, if material, in our quarterly earnings releases and annual reports on Form 20-F which are furnished or filed with the SEC in accordance with applicable U.S. rules and regulations.

LAYING ANNUAL FINANCIAL STATEMENTS BEFORE MEMBERS AT AN ANNUAL GENERAL MEETING WITHIN SIX MONTHS AFTER THE END OF FINANCIAL YEAR

Rule 13.46(2)(b) of the Hong Kong Listing Rules requires an overseas issuer to lay its annual financial statements before its members at its annual general meeting within the period of six months after the end of the financial year or accounting reference period to which the annual financial statements relate.

Note 2 to Rule 13.46(2)(b) of the Hong Kong Listing Rules provides that if an issuer has significant interests outside of Hong Kong it may apply for an extension of the six-month period.

Our Company is an issuer with significant interests outside of Hong Kong. By way of illustration:

- (i) our Company was incorporated in the Cayman Islands;
- (ii) our Company is a secondary listed issuer in Hong Kong under Chapter 19C of the Listing Rules, with a primary listing on Nasdaq;

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- (iii) our Company has applied for a ruling from the Securities and Futures Commission on the date hereof that our Company should not be considered a public company in Hong Kong within the meaning of Section 4.2 of the Introduction on the Codes on Takeovers and Mergers and Share Buy-backs; one of the reasons for the application is that our Company has significant interests outside of Hong Kong;
- (iv) as of December 31, 2020, our Group had more than 40,000 full-time employees based in the PRC and less than 20 full-time employees based in Hong Kong;
- (v) for the year ended December 31, 2020, more than 97% of our Group’s net revenues were generated from the PRC, and as of December 31, 2020, more than 75% of our Group’s total assets were based in the PRC; and
- (vi) for the year ended December 31, 2020, less than 2% of our Group’s net revenues were generated from Hong Kong, and, as of December 31, 2020, less than 15% of our Group’s total assets were based in Hong Kong.

Our Company is expected to be listed in March 2021 and will include in this document the audited financial information for the year ended December 31, 2020 and other financial disclosure. Upon the Listing, we will therefore have provided our shareholders with all of the information required under Rule 13.46(2)(b) of the Hong Kong Listing Rules to our shareholders. Accordingly, our shareholders would not be unfairly prejudiced by us not laying our annual financial statements for the financial year ending December 31, 2020 before our members at an annual general meeting no later than June 30, 2021, as required by Rule 13.46(2)(b) of the Hong Kong Listing Rules.

Furthermore, we have not historically held an annual general meeting every year since our listing on Nasdaq, and the procedures for convening an annual general meeting for a company with a dual listing in the U.S. and Hong Kong are burdensome and require global coordination among various parties, including, but not limited to, the ADS depository bank, [REDACTED], and [REDACTED].

Rule 5620(a) of the Nasdaq Stock Market Marketplace Rules (the “**Nasdaq Listing Rules**”) requires that each company listing common stock or voting preferred stock, and their equivalents, shall hold an annual general meeting no later than one year after the end of the company’s fiscal year-end. However, pursuant to Rule 5615(a)(3) of the Nasdaq Listing Rules, a foreign private issuer such as our Company may follow our home country practice in lieu of the Rule 5600 Series corporate governance requirements, including the requirements to hold an annual general meeting under Rule 5620(a). The term “home country” is defined under the U.S. securities laws to mean the jurisdiction in which the company is legally organized, incorporated or established.

We have, in our past practice, elected to follow home country practice pursuant to Rule 5615(a)(3) of the Nasdaq Listing Rules in lieu of the requirement under the Rule 5620(a) to hold an annual general meeting every fiscal year, and has disclosed the same in our annual report on Form 20-F pursuant to the U.S. securities laws.

Under article 35 of our articles of association, our Company shall hold an annual general meeting every year if required by the Companies Law under the Cayman Islands.

Our Cayman Islands counsel confirmed that (a) the Companies Act (as revised) of the Cayman Islands does not require our Company to follow or comply with the requirements of Rule 5620(a); (b) our Company’s non-compliance with Rule 5620(a) will not breach any law, public rule or regulation applicable to us currently in force in the Cayman Islands; (c) our memorandum and articles do not

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prohibit our Company from following our home country practice in lieu of the requirements of Rule 5620(a).

On the basis of the above, our Company’s not holding an annual general meeting before the end of the financial year ending December 31, 2021 does not contravene the relevant requirements under the Nasdaq Listing Rules, U.S. securities laws, laws of the Cayman Islands and our articles of association.

We have applied for[, and the Hong Kong Stock Exchange has granted,] a one-off waiver from strict compliance with Rule 13.46(2)(b) of the Hong Kong Listing Rules in respect of the requirement to lay our Company’s annual financial statements for the year ended December 31, 2020 before our members at an annual general meeting within six months after the financial year ended December 31, 2020, subject to the condition that we shall hold an annual general meeting for the financial year ending December 31, 2021 by June 30, 2022 and lay before our members at the annual general meeting in 2022 the financial statements for the financial year ending December 31, 2021.

SHAREHOLDER PROTECTION REQUIREMENTS

For an overseas issuer seeking a secondary listing on the Hong Kong Stock Exchange, Rule 19.30(1)(b) of the Hong Kong Listing Rules requires the overseas issuer’s primary listing is or is to be on an exchange where the standards of shareholder protection are at least equivalent to those provided in Hong Kong. Rule 19C.06 of the Hong Kong Listing Rules provides that Appendix 3 and Appendix 13 of the Hong Kong Listing Rules do not apply to an overseas issuer that is a Non-Greater China Issuer (as defined in the Hong Kong Listing Rules) or a Grandfathered Greater China Issuer seeking a secondary listing under Chapter 19C of the Hong Kong Listing Rules. Rule 19C.07 of the Hong Kong Listing Rules provides that the Hong Kong Stock Exchange will consider that a Non-Greater China Issuer or a Grandfathered Greater China Issuer seeking a secondary listing has met the requirements of Rule 19.30(1)(b) of the Hong Kong Listing Rules if it has met the shareholder protection standards by reference to eight criteria set out in Rule 19C.07 of the Hong Kong Listing Rules. We were listed on a Qualifying Exchange before December 15, 2017 and is therefore a Grandfathered Greater China Issuer under Chapter 19C of the Hong Kong Listing Rules.

Approval, removal and remuneration of auditors

Rule 19C.07(3) of the Hong Kong Listing Rules requires the appointment, removal and remuneration of auditors to be approved by a majority of the Qualifying Issuer’s members or other body that is independent of the issuer’s board of directors (the “**Auditors Provision**”).

Our Articles do not contain an equivalent Auditors Provision. Pursuant to our Articles, we may, at any general meeting appoint an auditor who shall hold office until the next annual general meeting, and may fix their remuneration. Although we may appoint auditors at annual general meetings, this function has been fulfilled by the audit committee of the Board (the “**Audit Committee**”) since our listing on Nasdaq in 2005.

As a matter of Cayman Island law, our members may express their view on the appointment, removal and remuneration of auditors, by attending the general meeting and speaking, and voting where there are relevant resolutions. Our Articles also allow members holding not less than a majority of the voting rights of our issued Shares that are entitled to vote at general meetings to requisition a general meeting, in which resolutions in respect of appointment, removal and remuneration of auditors may be put forward.

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The Audit Committee is an independent body of the Board on the basis of the independence requirements set out in applicable U.S. laws and Nasdaq rules. The Audit Committee comprises three members, all of whom are independent directors as required by applicable U.S. laws and applicable Nasdaq rules.

We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with the requirements of Rule 19C.07(3) of the Hong Kong Listing Rules.

Changes to requisition of extraordinary general meetings by shareholders

Rule 19C.07(4) of the Hong Kong Listing Rules requires a general meeting to be held each year as the Qualifying Issuer’s annual general meeting. Our Company is not required to hold an annual general meeting under our Articles and the Cayman Companies Act.

Rule 19C.07(7) of the Hong Kong Listing Rules requires that members holding a minority shareholding in a Qualifying Issuer’s total number of issued shares to be able to requisition an extraordinary general meeting and add resolutions to a meeting agenda. The minimum stake required to do so must not be higher than 10% of the voting rights, on a one vote per share basis, in the share capital of the Qualifying Issuer, while the minimum stake as currently set out in the Articles is not less than a majority of the voting rights of our issued Shares that are entitled to vote at general meetings. Under our Articles, a quorum for a shareholders’ meeting consists of one or more shareholders holding at least one third of the paid up voting share capital (being the number of issued shares in our paid up voting share capital), present in person or by proxy or, if a corporation or other non-natural person, by its duly authorized representative.

We will amend the Articles after the Listing to comply with Rule 19C.07(4) and Rule 19C.07(7) of the Hong Kong Listing Rules.

We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with the requirements of Rule 19C.07(4) and Rule 19C.07(7) of the Hong Kong Listing Rules, subject to the following conditions:

- (a) we will convene an extraordinary general meeting by December 31, 2021 (the “**2021 EGM**”), for which at least 14 days’ notice will be given to our members, and put forth resolutions to revise the Articles, so that (sub-paragraph (i) to (iv) below, collectively the “**Proposed Resolutions**”):
 - (i) we are required to convene an annual general meeting each year;
 - (ii) we are required to provide at least 14 days’ notice for any general meetings of the Company;
 - (iii) a member’s right to vote is subject to the requirements under the Hong Kong Listing Rules regarding circumstances requiring a member to abstain from voting to approve a matter under consideration, and any votes in contravention of such abstention shall not be counted; and
 - (iv) the minimum stake required to convene an extraordinary general meeting and add resolutions to a meeting agenda will be 10% of the voting rights, on a one vote per share basis, in the share capital of our Company;
- (b) we will convene general meetings at the request of our Shareholders holding in aggregate not less than 10% of our Company’s voting rights, on a one vote per share basis, prior to the Proposed Resolutions being passed;

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- (c) we will provide 14 days’ notice for any general meetings after the Listing, prior to the Proposed Resolutions being passed;
- (d) in the event that the Proposed Resolutions are not passed at the 2021 EGM, we will convene an annual general meeting each year with at least 14 days of notice beginning from 2022 and, for so long as we remain listed on the Hong Kong Stock Exchange, to continue to put forth the Proposed Resolutions (to the extent not yet passed) at each of the annual general meetings after the 2021 EGM, until the Proposed Resolutions are passed; and
- (e) we will obtain an irrevocable undertaking prior to the Listing from Mr. Robin Yanhong Li, Handsome Reward Limited and Ms. Melissa Ma, Mr. Robin Yanhong Li’s spouse, being existing shareholders with a majority vote in our Company, that they will use their voting rights to vote at the 2021 EGM in favour of the Proposed Resolutions.

Our Cayman Islands counsel has confirmed that there is no legal impediment on the adoption of the transitional arrangements to comply with the relevant requirements before the Proposed Resolutions are passed (being the arrangements set out in (b) to (d) above), and such adoption is not in breach of our Articles or any rules and regulations in the Cayman Islands.

PARTICULARS OF ANY COMMISSIONS, DISCOUNTS AND BROKERAGES AND ALTERATIONS OF CAPITAL AND AUTHORIZED DEBENTURES

Paragraphs 13 and 26 of Part A of Appendix 1 to the Hong Kong Listing Rules and paragraphs 11 and 14 of the Third Schedule of the Companies (Winding Up and Miscellaneous Provisions) Ordinance require the listing document to include the particulars of any commissions, discounts, brokerages or other special terms granted within two years immediately preceding the issue of the listing document in connection with the issue or sale of any capital of any member of the group and the particulars of any alterations of capital within two years immediately preceding the issue of the listing document.

Paragraph 25 of the Third Schedule of the Companies (Winding Up and Miscellaneous Provisions) Ordinance requires particulars of the authorized debentures of our Company and our subsidiaries to be disclosed in this document.

We have identified 12 entities as our Significant Subsidiaries. For further details, see the section headed “History and Corporate Structure—Corporate Structure—Significant Subsidiaries” in this document. We had more than 200 subsidiaries and operating entities as of December 31, 2020. We believe that it would be unduly burdensome for us to disclose this information in respect of all of our subsidiaries as we would have to incur additional costs and devote additional resources in compiling and verifying the relevant information for such disclosure, which would not be material or meaningful to [REDACTED].

The Significant Subsidiaries include all our subsidiaries that meet the financial threshold for “significant subsidiaries” under Regulation S-X in the U.S. and are representative of our business (including those that hold major assets and intellectual property rights). None of the non-Significant Subsidiaries is individually material to us in terms of the financial threshold for “significant subsidiaries” under Regulation S-X in the U.S., and none of the non-Significant Subsidiaries hold any major assets, patents, R&D or intellectual property rights as at the Latest Practicable Date. Based on the book value of the Significant Subsidiaries, the net revenues (taking into account of major adjustments for intra-group transactions) and net income (not taking into account adjustments for intra-group transactions) of the Significant Subsidiaries accounted for 91% and 195% of our total net revenues and total net income, respectively, for the year ended December 31, 2020. Based on the book

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value of the Significant Subsidiaries, the total assets (not taking into account adjustments for intra-group transactions) of the Significant Subsidiaries accounted for 115% of the our total assets as at December 31, 2020. As such, we have disclosed the particulars of the changes in our share capital and the Significant Subsidiaries in the section headed “Statutory and General Information—Further Information About Us” in Appendix IV to this document, and particulars of the commissions, discounts, brokerage fee and authorized debentures in respect of the Significant Subsidiaries and our Company are set out in the section headed “Statutory and General Information—Other Information—Miscellaneous” of Appendix IV to this document.

We are of the view that all material information necessary for the public to make an informed assessment of the business, asset and liability, financial position, trading position, management and prospect of our Group has been disclosed in this document, and as such the granting of the waiver and exemption from strict compliance with the relevant content requirements under the Companies (Winding Up and Miscellaneous Provisions) Ordinance and the Hong Kong Listing Rules will not prejudice the interest of the investing public.

We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from the requirements under paragraphs 13 and 26 of Part A of Appendix 1 to the Hong Kong Listing Rules. We have applied for[, and the SFC has granted,] an exemption from the requirements under paragraphs 11, 14 and 25 of the Third Schedule of the Companies (Winding Up and Miscellaneous Provisions) Ordinance, to the extent not strictly met by the current disclosure in this document. The SFC has granted the above exemption on the conditions that: (i) the particulars of such exemption are set out in this document; and (ii) this document will be issued on or before [REDACTED].

DISCLOSURE OF INFORMATION ON SUBSIDIARIES WHOSE PROFITS OR ASSETS MAKE MATERIAL CONTRIBUTIONS TO US

Paragraph 29(1) of Part A of Appendix 1 to the Hong Kong Listing Rules and paragraph 29 of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance require the listing document to include information in relation to the name, date and country of incorporation, the public or private status and the general nature of the business, the issued capital and the proportion thereof held or intended to be held, of every company the whole of the capital of which or a substantial proportion thereof is held or intended to be held by us, or whose profits or assets make, or will make, a material contribution to the figures in the accountants’ report or the next published accounts.

We believe that it would be unduly burdensome for us to procure this information for the reasons as set out in this section headed “—Particulars of any Commissions, Discounts and Brokerages and Alteration of Capital and Authorized Debentures” above. As such, only the particulars in relation to the Significant Subsidiaries are set out in this document under the sections headed “History and Corporate Structure—Corporate Structure—Significant Subsidiaries” and “Statutory and General Information—Further Information About Us” in Appendix IV to this document, which should be sufficient for potential [REDACTED] to make an informed assessment of our Company in their [REDACTED] decisions. We are of the view that all material information necessary for the public to make an informed assessment of the business, asset and liability, financial position, trading position, management and prospect of our Group has been disclosed in this document, and as such the granting of the waiver and exemption from strict compliance with the relevant content requirements under the Companies (Winding Up and Miscellaneous Provisions) Ordinance and the Hong Kong Listing Rules will not prejudice the interest of the [REDACTED] public.

We are of the view that all material information necessary for the public to make an informed assessment of the business, asset and liability, financial position, trading position, management and

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prospect of our Group has been disclosed in this document, and as such the granting of the waiver and exemption from strict compliance with the relevant content requirements under the Companies (Winding Up and Miscellaneous Provisions) Ordinance and the Hong Kong Listing Rules will not prejudice the interest of the [REDACTED] public.

We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with the requirements under paragraph 29(1) of Part A of Appendix 1 to the Hong Kong Listing Rules. We have applied for[, and the SFC has granted,] an exemption from the requirements under Paragraph 29 of the Third Schedule of the Companies (Winding Up and Miscellaneous Provisions) Ordinance, to the extent not strictly met by the current disclosure in this document. The SFC has granted the above exemption on the conditions that: (i) the particulars of such exemption are set out in this document; and (ii) this document will be issued on or before [REDACTED].

TIMING REQUIREMENT OF LIQUIDITY DISCLOSURE

Paragraph 32 of Part A of Appendix 1 to the Hong Kong Listing Rules requires a listing document to include a statement (or an appropriate negative statement) of a new applicant’s indebtedness as at a specified most recent practicable date (the “**Most Recent Practicable Date**”), and a commentary on its liquidity, financial resources and capital structure (together, the “**Liquidity Disclosure**”).

In accordance with Hong Kong Stock Exchange’s Guidance Letter HKEX-GL37-12 (“**GL37-12**”), the Hong Kong Stock Exchange normally expects that the Most Recent Practicable Date for the Liquidity Disclosure, including, among other things, commentary on liquidity and financial resources such as net current assets (liabilities) position and management discussion on this position, in a listing document to be dated no more than two calendar months before (a) the date of the application proof of the listing document and (b) the final date of the listing document.

As this document is expected to be published in March 2021, we would otherwise be required to make the relevant indebtedness and liquidity disclosures no earlier than January 2021 pursuant to GL37-12. Given that we included in this document an accountants’ report incorporating the audited consolidated financial information of our Group for the year ended December 31, 2020, it would be unduly burdensome for us to re-arrange information for similar liquidity disclosures on a consolidated basis shortly after the end of our current financial year.

Strict compliance with the Liquidity Disclosure requirements would constitute an additional one-off disclosure by us of our liquidity position on a date that would fall within the first quarter of our financial year, which would otherwise not be required to be disclosed to investors in the U.S. under applicable U.S. regulations and Nasdaq listing rules, because we are required to announce quarterly results at the end and not in the middle of each quarter of our financial year. Such a one-off disclosure would likely confuse our existing investors and deviate from our customary practice and that of other U.S. listed companies.

In any event, if there are any material changes to such disclosures, we would be required to make an announcement pursuant to U.S. regulations and Nasdaq rules and disclose relevant material facts in this document pursuant to the Hong Kong Listing Rules.

In the event that there is no material change to such disclosures, any similar disclosures made pursuant to GL37-12 would not give additional meaningful information to [REDACTED].

We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with the timing requirement for the Liquidity Disclosure in this document under GL37-12,

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such that the reported date of indebtedness and liquidity information in this document will not exceed the requirement under GL37-12 by one calendar month (i.e. the time gap between the reported date of our indebtedness and liquidity information and the date of this document would be no more than three calendar months).

DISCLOSURE REQUIREMENTS OF THE REMUNERATION OF DIRECTORS AND FIVE INDIVIDUALS WHOSE EMOLUMENTS WERE HIGHEST

Paragraph 33(2) of Part A of Appendix 1 to the Hong Kong Listing Rules requires the listing document to include information in respect of directors’ emoluments during the financial years ended December 31, 2018, 2019 and 2020. Paragraph 46(2) of Part A of Appendix 1 to the Hong Kong Listing Rules requires the listing document to include the aggregate of the remuneration paid and benefits in kind granted to the directors of the issuer in respect of the last completed financial year, and Paragraph 46(3) of Part A of Appendix 1 to the Hong Kong Listing Rules requires information in relation to an estimate of the aggregate remuneration and benefits in kind payable to directors in respect of the current financial year to be set out in the listing document.

Paragraph 33(3) of Part A of Appendix 1 to the Hong Kong Listing Rules requires the listing document to include information with respect to the five individuals whose emoluments were highest in the group for the year if one or more individuals whose emoluments were the highest have not been included under paragraph 33(2) of Part A of Appendix 1 to the Hong Kong Listing Rules.

The aggregate fees, salaries and benefits paid and accrued to our directors and executive officers as a group are disclosed in the section headed “Directors and Senior Management—Compensation” in this document. We confirm that the current disclosure complies with U.S. annual reporting requirements and is in line with our disclosure in our annual reports on Form 20-F.

We believe that additional disclosure required by Paragraphs 33(2), 33(3), 46(2) and 46(3) of Part A of Appendix 1 to the Hong Kong Listing Rules would be unduly burdensome and would not provide additional meaningful disclosure for potential [REDACTED].

We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with the requirements under Paragraphs 33(2), 33(3), 46(2) and 46(3) of Part A of Appendix 1 to the Hong Kong Listing Rules, to the extent not strictly met by the current disclosure in this document.

DISCLOSURE OF INTERESTS INFORMATION

Part XV of the SFO imposes duties of disclosure of interests in shares. Practice Note 5 and paragraphs 41(4) and 45 of Part A of Appendix 1 to the Hong Kong Listing Rules require the disclosure of interests information in respect of shareholders’ and directors’ interests in this document.

The U.S. Exchange Act and the rules and regulations promulgated thereunder require disclosure of interests by shareholders that are broadly equivalent to Part XV of the SFO. Relevant disclosure in respect of the substantial shareholder’s interests can be found in the section headed “Major Shareholders” in this document.

We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with Practice Note 5 and Paragraphs 41(4) and 45 of Part A of Appendix 1 to the Hong Kong Listing Rules is to be granted on the following conditions:

- (a) the SFC granting us and our shareholders a partial exemption from strict compliance with Part XV of the SFO;

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- (b) our undertaking to file with the Hong Kong Stock Exchange, as soon as practicable, any declaration of shareholding and securities transactions filed with the SEC; and
- (c) our undertaking to disclose in present and future listing documents any shareholding interests as disclosed in an SEC filing and the relationship between our directors, officers, members of committees and their relationship to any controlling shareholders.

[REDACTED]

SUBSCRIPTION FOR SHARES BY EXISTING SHAREHOLDERS

Rule 10.04 of the Hong Kong Listing Rules requires that existing shareholders may only subscribe for or purchase any securities for which listing is sought that are being marketed by or on behalf of a new applicant either in his or its own name or through nominees if the conditions in Rule 10.03 of the Hong Kong Listing Rules are fulfilled. Paragraph 5(2) of Appendix 6 to the Hong Kong Listing Rules states that, without the prior written consent of the Hong Kong Stock Exchange, no allocations will be permitted to be made to directors, existing shareholders of a listing applicant or their close associates, unless the conditions set out in Rules 10.03 and 10.04 of the Hong Kong Listing Rules are fulfilled.

We have been listed on Nasdaq since 2005 and has a wide and diverse shareholder base. Solely based on public filings with the SEC available as of the Latest Practicable Date, with the exception of Ms. Melissa Ma, the spouse of Mr. Robin Yanhong Li, we had no shareholder who was not a director

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and who held 5% or more of our Company’s voting rights. Category 4 of the Permitted Persons (as defined in “—Dealings in Shares prior to the Listing” above) have no influence over the [REDACTED] and are not in possession of any non-public inside information in relation to the Listing given that such persons are not in a position with access to information that is considered material to the Company as a whole, and are effectively in the same positions as the public [REDACTED] of the Company. Category 4 of the Permitted Persons and other public [REDACTED] are referred to as “Permitted Existing Shareholders”.

Considering the nature of those investors and as our Shares are publicly traded on Nasdaq, we are not in the position to prevent any person or entity from acquiring listed securities of our Company prior to the [REDACTED]. In addition, we will only be able to ascertain the change in the shareholding of the relevant Shareholder after we make public disclosure. It would therefore be unduly burdensome for us to seek the prior consent of the Hong Kong Stock Exchange for each of our existing shareholders or their close associates who [REDACTED] Shares in the [REDACTED].

We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with the requirements of Rule 10.04 and Paragraph 5(2) of Appendix 6 to the Hong Kong Listing Rules in respect of the restriction on Permitted Existing Shareholders to [REDACTED] or purchase Shares in the [REDACTED], subject to the following conditions:

- each Permitted Existing Shareholder is interested in less than 5% of our Company’s voting rights before the Listing;
- each Permitted Existing Shareholder is neither a director nor a member of senior management of our Company, and is not a director of any of our Company’s subsidiaries;
- other than the persons in Category 4 of the Permitted Persons, each Permitted Existing Shareholder is not a core connected person of our Company;
- the Permitted Existing Shareholders do not have the power to appoint directors of our Company or any other special rights in our Company;
- the Permitted Existing Shareholders and their close associates do not have influence over the [REDACTED] process and will be treated the same as other applicants and placees in the [REDACTED];
- the Permitted Existing Shareholders and their close associates will be subject to the same book-building and allocation process as other applicants and placees in the [REDACTED]; and
- to the best of their knowledge and belief, each of our Company, the Joint Sponsors and [REDACTED] (based on its discussions with and the confirmations from our Company and [REDACTED] (for itself and on behalf of [REDACTED])), confirms to the Hong Kong Stock Exchange in writing that no preferential treatment has been, nor will be, given to the Permitted Existing Shareholders and their close associates as a placee in the [REDACTED] by virtue of their relationship with our Company.

Allocation to the Permitted Existing Shareholders and/or their close associates will not be disclosed in our [REDACTED] (other than to the extent that such Permitted Existing Shareholders or close associates [REDACTED] shares as [REDACTED]) unless such Permitted Existing Shareholders are interested in 5% or more of our issued share capital after the [REDACTED] as disclosed in any of their public filings with the SEC (the “Available Information”). It would be unduly burdensome for us to disclose such information other than the Available Information given that there is no requirement to disclose interests in equity securities under the U.S. Exchange Act unless the

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beneficial ownership of a person reaches 5% or more, and when there is a subsequent change of ownership of 1% or more, in our issued share capital.

[REDACTED]

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[REDACTED]

INVESTMENTS AFTER THE TRACK RECORD PERIOD

Pursuant to Rules 4.04(2) and 4.04(4)(a) of the Hong Kong Listing Rules, the accountants’ report to be included in a listing document must include the income statements and balance sheets of any subsidiary or business acquired, agreed to be acquired or proposed to be acquired since the date to which its latest audited accounts have been made up in respect of each of the three financial years immediately preceding the issue of the listing document.

Pursuant to Rule 4.02A of the Hong Kong Listing Rules, acquisitions of business include acquisitions of associates and any equity interest in another company. Pursuant to Note 4 to Rule 4.04 of the Hong Kong Listing Rules, the Hong Kong Stock Exchange may consider granting a waiver of the requirements under Rules 4.04(2) and 4.04(4) on a case-by-case basis, and having regard to all relevant facts and circumstances and subject to certain conditions set out thereunder.

Ordinary course Investments since December 31, 2020

During the Track Record Period, we have made minority investments in a number of companies both in China and overseas in our ordinary and usual course of business to further our strategic objectives. Since December 31, 2020 and up to the Latest Practicable Date, we have made or proposed to make minority investments in a number of companies, and we expect to continue to enter into further minority investments subsequent to the Latest Practicable Date and prior to the date of this document (collectively, the “**Investments**”). Details of the Investments up to the Latest Practicable Date include (other than those, the considerations of which were less than RMB20 million—being less than 0.02% of our total assets as of December 31, 2020 and revenue for the year ended December 31, 2020):

| <u>Investment⁽²⁾⁽³⁾</u> | <u>Consideration</u> (approx. in RMB millions) | <u>Percentage of shareholding/equity interest⁽¹⁾</u> | <u>Principal business activities</u> |
|------------------------------------|---|---|--|
| Company A | 350 | 28% | Consulting |
| Company B | 100 | 9% | Medical |
| Company C | 80 | 40% | Medical |
| Company D | 50 | 10% | Consulting |
| Company E | 50 | 9% | Consulting |
| Company F | 33 | 8% | Medical |
| Company G | 30 | 5% | E-commerce |
| Company H | 25 | 23% | Entertainment |
| Company I | 22 | 11% | Education |
| Company J | 20 | 6% | Commerce |
| Company K | 20 | 8% | Medical |
| Company L | 20 | 1% | Medical |
| Company M | 20 | 1% | Technology |

Notes:

- (1) The approximate consideration disclosed in the table represents each of the Investments. The percentage of shareholding/equity interest represents our total pro forma shareholding in each of the Investments after the completion of the relevant transaction.
- (2) None of the core connected persons at the level of our Company is a controlling shareholder of any of the Investments.
- (3) Given that we have not yet entered into legally binding agreements for certain of the above Investments as at the Latest Practicable Date, the terms and information set out above may be subject to further changes.

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We confirm that the investment amounts for each of the Investments are the result of commercial arm’s length negotiations, based on factors including market dynamics, a mutually agreed valuation, and/or capital need of the relevant company’s operations.

Conditions for granting the waiver and its scope in respect of the Investments

We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with Rules 4.04(2) and 4.04(4)(a) of the Hong Kong Listing Rules in respect of the Investments on the following grounds:

Ordinary and usual course of business

We make equity investments in sectors relating to our business as part of our ordinary and usual course of business. We have a history of making minority investments and have conducted a number of minority investments during the Track Record Period.

The percentage ratios of each Investment are all less than 5% by reference to the most recent fiscal year of our Company’s Track Record Period

The relevant percentage ratios calculated in accordance with Rule 14.07 of the Hong Kong Listing Rules for each of the Investments are all less than 5% by reference to the most recent fiscal year of the Track Record Period. We do not believe that the Investments are subject to aggregation under Rule 14.22 of the Hong Kong Listing Rules, because (i) each of the Investments involves the acquisition of interests in a different company and (ii) the Investments were entered into, or are expected to be entered into, with different counterparties.

Accordingly, we believe that the Investments have not resulted in, and does not expect the Investments to result in, any significant changes to its financial position since December 31, 2020, and all information that is reasonably necessary for potential [REDACTED] to make an informed assessment of our activities or financial position has been included in this document. As such, we consider that a waiver from compliance with the requirements under Rules 4.04(2) and 4.04(4)(a) of the Hong Kong Listing Rules would not prejudice the interests of the [REDACTED].

We are not able to exercise any control over the underlying company or business

We only hold and/or expect to only hold a minority equity interest in each of the Investments and does not control their boards of directors, and expects this to remain the case for any subsequent Investments. The minority rights given to us are generally commensurate to its status as a minority shareholder and are for the protection of our interests as a minority stakeholder in the Investments. These rights are neither intended, nor sufficient to compel or require the relevant companies to prepare or to disclose in this document audited financial statements for the purposes of compliance with Rules 4.04(2) and 4.04(4)(a) of the Hong Kong Listing Rules. These disclosures are also not required pursuant to applicable U.S. securities laws. It could be prejudicial and potentially harmful to our portfolio relationships and commercial interests to make such disclosures. In addition, as some portfolio companies are private, disclosing this information could harm their interests and bring them into an unfavorable competitive position. Accordingly, as we do not expect the Investments to result in any material changes to its financial position after the Track Record Period, we do not believe the non-disclosure of the required information pursuant to Rules 4.04(2) and 4.04(4)(a) of the Hong Kong Listing Rules would prejudice the interest of the [REDACTED].

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Alternative disclosure of the Investments in this document

We have disclosed alternative information about the Investments in this document. Such information includes those which would be required for a discloseable transaction under Chapter 14 of the Hong Kong Listing Rules that our directors consider to be material, including, for example, descriptions of the relevant companies’ principal business activities, the investment amounts, and a statement as to whether the core connected persons at the level of our Company is a controlling shareholder of any of the Investments. We have however excluded disclosure on the names of companies in connection with the Investments in this document because: (i) we have entered into confidentiality agreements with these companies and do not have consent for such disclosure; and/or (ii) the transactions have not been disclosed, and are not required to be disclosed, under U.S. regulations. It is commercially sensitive to disclose the identities of the companies we have invested in or proposes to invest in as such information may enable our competitors to anticipate our investment strategy. Since the relevant percentage ratio of each Investment is less than 5% by reference to the most recent fiscal year of the Company’s Track Record Period, we believe the current disclosure is adequate for potential [REDACTED] to form an informed assessment of us.

DISCLOSURE REQUIREMENTS OF OPTIONS

Paragraph 27 of Part A of Appendix 1 to the Hong Kong Listing Rules requires an issuer to set out in the listing document particulars of any capital of any member of the group that is under option, or agreed conditionally or unconditionally to be put under option, including the consideration for which the option was or will be granted and the price and duration of the option, and the name and address of the grantee.

Paragraph 10 of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance further requires an issuer to set out in the [REDACTED], among other things, details of the number, description and amount of any of its shares or debentures which any person has, or is entitled to be given, an option to subscribe for, together with the certain particulars of the option, namely the period during which it is exercisable, the price to be paid for shares or debentures subscribed for under it, the consideration given or to be given (if any) and the names and addresses of the persons to whom it was given.

We and our subsidiaries (including its consolidated affiliated entities) may, from time to time, adopt equity incentive plans, including: (a) our share incentive plan adopted in December 2008 and which expired in 2018 (the “**2008 Share Incentive Plan**”); (b) our share incentive plan adopted in July 2018 (the “**2018 Share Incentive Plan**”, and together with the 2008 Share Incentive Plan, the “**Share Incentive Plans**”); (c) the equity incentive plan adopted in 2010 (the “**iQIYI 2010 Equity Incentive Plan**”) by iQIYI, our majority-controlled subsidiary listed on the New York Stock Exchange, and (d) the share incentive plan adopted in 2017 by iQIYI (the “**iQIYI 2017 Share Incentive Plan**” and, together with the “**iQIYI 2010 Equity Incentive Plan**”, the “**iQIYI Incentive Plans**”). These equity incentive plans are not subject to Chapter 17 of the Hong Kong Listing Rules pursuant to Rule 19C.11 of the Hong Kong Listing Rules. The equity incentive plans allow us, iQIYI and our subsidiaries to grant awards (including options) to employees, directors and consultants. The waiver and exemption therefore only relates to the options that are granted under the Share Incentive Plans and the iQIYI Incentive Plans.

As of December 31, 2020, the outstanding options pursuant to the Share Incentive Plans only accounted for approximately 0.9% of our total issued and outstanding shares. Assuming full exercise of these outstanding options, the shareholding of our Shareholders will be diluted by approximately 0.9%, based on the outstanding shares of our Company in issue as of December 31, 2020.

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As of December 31, 2020, the outstanding options pursuant to the iQIYI Incentive Plans only accounted for approximately 7.7% of iQIYI’s total issued and outstanding shares. Assuming full exercise of these outstanding options, the shareholding of iQIYI’s Shareholders will be diluted by approximately 7.1%, based on the outstanding shares of iQIYI in issue as of December 31, 2020.

Details of the Share Incentive Plans are disclosed in the section headed “Directors and Senior Management—Compensation—Share Incentive Plans” and details of the iQIYI Incentive Plans are disclosed in “Statutory and General Information—Further Information About us—Share incentive plans of iQIYI” in Appendix IV to this document. The disclosure is substantially the same as those in our and iQIYI’s 20-F filings and comply with applicable U.S. laws and regulations, and certain details of the options as required under Paragraph 27 of Part A of Appendix 1 to the Hong Kong Listing Rules and Paragraph 10 of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance are not required to be and have not been disclosed in our Company’s and iQIYI’s previous regulatory filings. In addition, the Share Incentive Plans and iQIYI Incentive Plans are not subject to Chapter 17 of the Hong Kong Listing Rules as it is not applicable pursuant to Rule 19C.11 of the Hong Kong Listing Rules.

For the above reasons, the current disclosure in this document relating to the Share Incentive Plans and the iQIYI Incentive Plans is not in strict compliance with the requirements under Paragraph 27 of Part A of Appendix 1 to the Hong Kong Listing Rules, and the current disclosure in this document relating to the Share Incentive Plans is not in strict compliance with the requirements under Paragraph 10 of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance.

For the reasons stated above, we believe that strict compliance with the above requirements would be unduly burdensome, unnecessary and/or inappropriate for us, and would not be material or meaningful to [REDACTED].

We are of the view that all material information necessary for the public to make an informed assessment of the business, asset and liability, financial position, trading position, management and prospect of the Group has been disclosed in this document, and as such the granting of the waiver and exemption from strict compliance with the relevant content requirements under the Companies (Winding Up and Miscellaneous Provisions) Ordinance and the Hong Kong Listing Rules will not prejudice the interest of the [REDACTED] public.

We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with the requirements under Paragraph 27 of Part A of Appendix 1 to the Hong Kong Listing Rules in relation to the Share Incentive Plans and the iQIYI Incentive Plans. We have applied for[, and the SFC has granted,] an exemption[, from the requirements under Paragraph 10 of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance in relation to the Share Incentive Plans, to the extent not strictly met by the current disclosure in this document, on the conditions that: (i) the particulars of such exemption are set out in this document; and (ii) this document will be issued on or before [REDACTED].

RULES RELATING TO SPIN-OFF LISTINGS

Rule 19C.11 of the Hong Kong Listing Rules provides that, among other things, paragraphs 1 to 3(b) and 3(d) to 5 of Practice Note 15 of the Hong Kong Listing Rules do not apply to a Qualifying Issuer that has, or is seeking, a secondary listing on the Hong Kong Stock Exchange. Such exception limited to circumstances where the spun-off assets or businesses are not to be listed on the Hong Kong Stock Exchange’s markets and the approval of shareholders of the issuer is not required.

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Paragraph 3(b) of Practice Note 15 to the Hong Kong Listing Rules provides that the Listing Committee would not normally consider a spin-off application within three years of the date of listing of the issuer, given the original listing of the issuer will have been approved on the basis of the issuer’s portfolio of businesses at the time of listing, and that the expectation of [REDACTED] at that time would have been that the issuer would continue to develop those businesses.

While we do not have any specific plans with respect to the timing or details of any potential spin-off listing on the Hong Kong Stock Exchange as at the date of this document, in light of our Group’s overall business scale, we may consider spinning off one or more of its mature business units through a listing on the Hong Kong Stock Exchange (each a “**Potential Spin-off**”) within three years after the Listing, if there are clear commercial benefits both to us and the businesses to be potentially spun-off and there will be no adverse impact on the interests of our shareholders. As of the Latest Practicable Date, we have not identified any target for a potential spin-off; as a result, we do not have any information relating to the identity of any spin-off target or any other details of any spin off and accordingly, there is no material omission of any information relating to any possible spin-off in this document. We cannot assure that any spin-off will ultimately be consummated, whether within the three-year period after the Listing or otherwise, and any such spin-off will be subject to market conditions at the relevant time and approval by the Listing Committee of the Hong Kong Stock Exchange. In the event that we proceed with a spin-off, our interest in the entity to be spun off (and its corresponding contribution to the financial results of our Group) will be reduced accordingly.

We have applied for[, and the Hong Kong Stock Exchange has granted,] a waiver from strict compliance with the requirements in paragraph 3(b) of Practice Note 15 to the Hong Kong Listing Rules, on the following grounds:

- (i) no shareholders’ approval with respect to a Potential Spin-off will be required under the Articles under applicable U.S. regulations and Nasdaq listing rules. Further, as we are a Grandfathered Greater China Issuer and therefore exempt from the requirements under Chapter 14 of the Hong Kong Listing Rules pursuant to Rule 19C.11 of the Hong Kong Listing Rules, no shareholders’ approval will be required under the Hong Kong Listing Rules as well;
- (ii) the effect of a spin-off to our shareholders should be the same regardless of whether or not the businesses to be potentially spun-off are to be listed on the Hong Kong Stock Exchange (save with respect to any preferential rights to subscribe for shares that are commonly provided in spin-offs on the Hong Kong Stock Exchange). Given the fact that certain spin-offs by Grandfathered Greater China Issuers are allowed within three years after their listing in Hong Kong pursuant to Rule 19C.11 of the Hong Kong Listing Rules, we believe that the three-year restriction on spin-offs on the Hong Kong Stock Exchange should also be waived and shall not apply to a Potential Spin-off by our Company;
- (iii) in any event, our Company and any subsidiary in respect of which a Potential Spin-off is contemplated will be subject to compliance with all other applicable requirements under the Hong Kong Listing Rules, including the remaining requirements of Practice Note 15 and (in the case of the company to be spun-off) the listing eligibility requirements of Chapter 8, 8A or 19C of the Hong Kong Listing Rules (as the case may be), unless otherwise waived by the Hong Kong Stock Exchange;
- (iv) under U.S. securities laws and Nasdaq rules, we are not subject to any restrictions similar to the three-year restriction under paragraph 3(b) of Practice Note 15 to the Hong Kong Listing Rules in relation to the spin-offs of our businesses, nor is there any requirement for us to disclose any details of its potential spin-off entities when such information is not available because of the absence of any concrete spin-off plan; and

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- (v) the directors owe fiduciary duties to our Company, including the duty to act in what they consider in good faith to be in our best interests; as such they will only pursue a potential spin-off if there are clear commercial benefits both to us and the entity or entities to be spun off; and the directors will not direct our Company to conduct any spin-off if they believe it will have an adverse impact on the interests of our shareholders.

The waiver [was granted by the Hong Kong Stock Exchange] on the following conditions:

- (i) prior to any spin-off of our business through a listing on the Hong Kong Stock Exchange within three years after the Listing, we will confirm to the Hong Kong Stock Exchange with basis that the spin-off would not render us, excluding the business to be spun off, incapable of fulfilling either the eligibility or suitability requirements under Rules 19C.02 and 19C.05 of the Hong Kong Listing Rules based on the financial information of the entity to be spun-off at the time of our listing (calculated accumulatively where more than one entity is to be spun-off);
- (ii) we will disclose in this document our intention relating to any potential spin-off within three years after the Listing and the risks relating to the uncertainty and timing of any potential spin-offs (see section headed “Risk Factors—Risks Related to Our Shares, ADSs and the Listing—We are exposed to risks associated with the potential spin-off of one or more of our businesses” in this document);
- (iii) any potential spin-offs by our Company will be subject to the requirements of Practice Note 15 to the Hong Kong Listing Rules (other than paragraph 3(b) thereof), including that each of our Company and our businesses to be spun off will satisfy the applicable listing eligibility requirements on a standalone basis; and
- (iv) disclosure of this waiver in this document.

DISCLOSURE OF ULTIMATE BENEFICIAL OWNER OF OTHER WVR BENEFICIARY

Rule 8A.39 of the Hong Kong Listing Rules provides that an issuer with a WVR structure must identify the beneficiaries of weighted voting rights in its listing documents and in its interim and annual reports.

Immediately upon completion of the [REDACTED], the WVR beneficiaries will be Mr. Robin Yanhong Li, the chairman and chief executive officer of the Company; Ms. Melissa Ma, the spouse of Mr. Li, and Shimoda Holdings, LLC and Integrity Partners V, LLC, which are affiliated with early stage investors of our Company that invested in our Company before its US IPO in 2005. Details of the WVR beneficiaries are disclosed in “Share Capital—WVR Beneficiaries” in this document.

To our best knowledge Shimoda Holdings, LLC and Integrity Partners V, LLC (together the “**Other WVR Beneficiaries**”) and their respective ultimate beneficial owners are independent third parties of our Company and are not core connected persons of our Company, and the ultimate beneficial owners of the Other WVR Beneficiaries do not have a role in our business and operations.

The disclosure in this document does not include information on the ultimate beneficial owners of the Other WVR Beneficiaries. We [applied for, and the Stock Exchange has granted,] a waiver from strict compliance with the requirements in Rule 8A.39 in relation to this document and our future interim and annual reports on the following grounds:

- (i) **Voting rights controlled by the Other WVR Beneficiaries are immaterial.** Immediately upon the completion of the [REDACTED], the Other WVR Beneficiaries will control in aggregate

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approximately [REDACTED] of our voting rights. We undertake that we will not issue additional Class B ordinary shares to the Other WVR Beneficiaries in the future.

- (ii) **No consent to disclosure has been obtained.** As of the Latest Practicable Date, no consent for disclosure of ultimate beneficial ownership has been received from the Other WVR Beneficiaries.
- (iii) **Risk of breach of the Data Protection Act (As Revised) of the Cayman Islands.** Our adviser as to Cayman Islands law has advised us that there is a risk that disclosure of the ultimate beneficial owners of the Other WVR Beneficiaries without their consent would be in breach of the Data Protection Act (As Revised) of the Cayman Islands, the breach of which may lead to remedial action by the relevant Cayman Islands regulator (the Ombudsman), the imposition of penalties, and criminal sanctions.
- (iv) **Other WVR Beneficiaries are affiliated with early stage investors of the Company.** These early stage investors invested in our Company before its initial public offering on Nasdaq in 2005, which dates back to more than a decade ago.
- (v) **No specific disclosure of ultimate beneficial owner in US filings.** We are an issuer seeking a secondary listing as a Grandfathered Greater China Issuer pursuant to Chapter 19C of the Hong Kong Listing Rules. We have had a long history of listing on Nasdaq, and we have consistently disclosed details of our major shareholders (being holders known to own beneficially more than 5% of our total outstanding shares) pursuant to applicable US laws and Nasdaq rules. The prospectus relating to our initial public offering on Nasdaq in 2005 and our subsequent 20-Fs did not explicitly name the ultimate beneficial owners of the Other WVR Beneficiaries.
- (vi) **Interests of [REDACTED] public not prejudiced.** The exclusion of the ultimate beneficial owners of the Other WVR Beneficiaries from this document, especially given their immaterial shareholding, would not prejudice the interests of the [REDACTED] public. This document currently contains, and the Company expects to include in its future interim and annual reports, alternative disclosure relating to the Other WVR Beneficiaries, including their names, their shareholding, that they are affiliated with early stage investors of the Company that invested in the Company before its US IPO in 2005, and that they and their respective ultimate beneficial owners are an independent third party of and not a core connected person of the Company and the ultimate beneficial owners of the Other WVR Beneficiaries do not have a role in the Company’s business and operations to the best knowledge of the Company.

For the reasons stated above, we believe that strict compliance with the requirements of Rule 8A.39 of the Listing Rules would be inappropriate and not in the best interests of the Company.

NOT A PUBLIC COMPANY IN HONG KONG UNDER THE TAKEOVERS CODE

Section 4.1 of the Introduction to Takeovers Codes provides that the Takeovers Codes apply to takeovers, mergers and share buy-backs affecting, among others, public companies in Hong Kong and companies with a primary listing of their securities in Hong Kong. According to the Note to Section 4.2 of the Introduction to the Takeovers Codes, a Grandfathered Greater China Issuer within the meaning of Rule 19C.01 of the Hong Kong Listing Rules with a secondary listing on the Hong Kong Stock Exchange will not normally be regarded as a public company in Hong Kong under Section 4.2 of the Introduction to the Takeovers Codes. We have applied for a ruling that we are not a “public company in Hong Kong” for the purposes of the Takeovers Codes. The executive issued a ruling and confirmed that, we, as a Grandfathered Greater China Issuer within the meaning of Rule 19C.01 of the Hong Kong Listing Rules after our proposed secondary listing on the Hong Kong Stock Exchange, will not be regarded as a public company in Hong Kong for the purposes of the Takeovers

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Codes. Therefore, the Takeovers Codes do not apply to us. In the event that the bulk of trading in our Shares migrates to Hong Kong such that we would be treated as having a dual-primary listing pursuant to Rule 19C.13 of the Hong Kong Listing Rules, the Takeovers Codes will apply to us.

DISCLOSURE OF INTERESTS UNDER PART XV OF SFO

Part XV of the SFO imposes duties of disclosure of interests in the securities of companies whose securities are listed on the Hong Kong Stock Exchange on the relevant company, its substantial shareholders and its directors/chief executives. Under the U.S. Exchange Act, which we are subject to, any person (including directors and officers of the company concerned) who acquires beneficial ownership, as determined in accordance with the rules and regulations of the SEC and which includes the power to direct the voting or the disposition of the securities, of more than 5% of a class of equity securities registered under Section 12 of the U.S. Exchange Act must file beneficial owner reports with the SEC, and such person must promptly report any material change in the information provided (including any acquisition or disposition of 1% or more of the class of equity securities concerned), unless exceptions apply. Therefore, compliance with Part XV of the SFO would subject our corporate insiders to a second level of reporting, which would be unduly burdensome to them, would result in additional costs and would not be meaningful, since the statutory disclosure of interest obligations under the U.S. Exchange Act that apply to us and our corporate insiders would provide our **[REDACTED]** with sufficient information relating to the shareholding interests of our significant shareholders.

We have applied for, and the SFC has granted, a partial exemption under section 309(2) of the SFO from the provisions of Part XV of the SFO (other than Divisions 5, 11 and 12 of Part XV of the SFO), on the conditions that (i) the bulk of trading in the Shares is not considered to have migrated to Hong Kong on a permanent basis in accordance with Rule 19C.13 of the Hong Kong Listing Rules; (ii) all disclosures of interest filed with the SEC are also filed with the Hong Kong Stock Exchange as soon as practicable, which will then publish such disclosures in the same manner as disclosures made under Part XV of the SFO; and (iii) we will advise the SFC if there is any material change to any of the information which has been provided to the SFC, including any significant changes to the disclosure requirements in the U.S. and any significant changes in the volume of our worldwide share turnover that takes place on the Hong Kong Stock Exchange. This exemption may be reconsidered by the SFC in the event there is a material change in information provided to the SFC.

DIRECTORS AND PARTIES INVOLVED IN THE [REDACTED]

DIRECTORS

| <u>Name</u> | <u>Address</u> | <u>Country of Nationality</u> |
|------------------------|--|-------------------------------|
| Robin Yanhong Li | No. 901, Unit 1, Building 1, Area 2, Shanghe Village, Haidian District Beijing, PRC | Chinese |
| James Ding | Flat A, 31/F, Block 1 Dawning Views 23 Yat Ming Road New Territories Hong Kong | Chinese |
| Brent Callinicos | 4110 Woodleigh Lane La Canada Flintridge CA 91011 USA | American |
| Yuanqing Yang | No.25-5, Green River Manor Huilongguan Town Changping District Beijing, PRC | Chinese |
| Jixun Foo | 25 Phoenix Garden Singapore 668292 | Singapore |

Further information about the directors and other senior management members are set out in “Directors and Senior Management”.

PARTIES INVOLVED IN THE [REDACTED]

Joint Sponsors

Merrill Lynch (Asia Pacific) Limited

55/F Cheung Kong Center
2 Queen’s Road Central
Central
Hong Kong

CLSA Capital Markets Limited

18/F, One Pacific Place
88 Queensway
Hong Kong

Goldman Sachs (Asia) L.L.C.

68/F, Cheung Kong Center
2 Queen’s Road Central
Hong Kong

[REDACTED]

DIRECTORS AND PARTIES INVOLVED IN THE [REDACTED]

[REDACTED]

Our Legal Advisers

As to Hong Kong and U.S. laws:

Skadden, Arps, Slate, Meagher & Flom and affiliates
42nd Floor, Edinburgh Tower
The Landmark
15 Queen’s Road Central
Hong Kong

As to PRC laws:

King & Wood Mallesons

18th Floor, East Tower, World Financial Center
1 Dongsanhuan Zhonglu
Chaoyang District
Beijing, 100020
PRC

As to Cayman Islands laws:

Maples and Calder (Hong Kong) LLP
26th Floor, Central Plaza
18 Harbour Road
Wanchai
Hong Kong

**Legal Advisers to the Joint
Sponsors and [REDACTED]**

As to Hong Kong and U.S. laws:

Davis Polk & Wardwell
18th Floor, The Hong Kong Club Building
3A Chater Road
Hong Kong

As to PRC laws:

Haiwen & Partners
20/F, Fortune Financial Center
5 Dong San Huan Central Road
Chaoyang District
Beijing, 100020
PRC

DIRECTORS AND PARTIES INVOLVED IN THE [REDACTED]

**Auditor and Reporting
Accountants**

Ernst & Young
Certified Public Accountants
Registered Public Interest Entity Auditor
22/F, CITIC Tower
1 Tim Mei Avenue
Central, Hong Kong

Reporting Accountant on YY Live

PricewaterhouseCoopers
Certified Public Accountants
Registered Public Interest Entity Auditor
22/F Prince’s Building,
Central, Hong Kong

Industry Consultant

China Insights Consultancy Limited
10F, Block B, Jing’an International Center,
88 Puji Road, Jing’an District,
Shanghai 200070,
PRC

[REDACTED]

CORPORATE INFORMATION

| | |
|---|---|
| Registered Office | Maples Corporate Services Limited PO Box 309, Ugland House Grand Cayman, KY1-1104 Cayman Islands |
| Principal Executive Offices of Main Operations | Baidu Campus No. 10 Shangdi 10th Street Haidian District, Beijing 100085 The People's Republic of China |
| Address in Hong Kong | Suite 3101, Everbright Centre, 108 Gloucester Road, Wanchai, Hong Kong |
| Company's Website | http://ir.baidu.com/ <i>(The information on the website does not form part of this document)</i> |
| Authorized Representative | Dandan Yuan/ Juan Lin 9/F, 33 Hysan Avenue Lee Gardens One Causeway Bay Hong Kong |
| Audit Committee | Brent Callinicos (Chairman) James Ding Yuanqing Yang |
| Compensation Committee | James Ding (Chairman) Yuanqing Yang Jixun Foo |
| Corporate Governance and Nominating Committee | Yuanqing Yang (Chairman) James Ding |
| Cayman Islands Principal Share Registrar | Maples Fund Services (Cayman) Limited PO Box 1093, Boundary Hall Cricket Square Grand Cayman, KY1-1102 Cayman Islands |

[REDACTED]

CORPORATE INFORMATION

Compliance Advisor

Somerley Capital Limited

20th Floor, China Building

29 Queen's Road Central

Hong Kong

Principal Bank

Citibank, N.A., Hong Kong Branch

Champion Tower

Three Garden Road

Central

Hong Kong

HISTORY AND CORPORATE STRUCTURE

Overview

We commenced our business in January 2000, and have since grown to become a leading AI company and Internet platform. Since our founding in 2000, we have served as the gateway to the Internet by connecting users to an expansive, long-tail and open content network through our search platform. Years of tagging, understanding and intelligently processing all forms of content on the Internet—text, images, videos—with AI has helped us develop Baidu Brain, our core AI engine, which in turn has enabled us to further develop leading AI technologies and commercialize them through products and services for consumers, enterprises and the public sector.

Our Company is a holding company incorporated in the Cayman Islands in January 2000. We conduct our operations in China principally through Baidu Online, our wholly-owned subsidiary, and Baidu Netcom and Beijing Perusal, consolidated affiliated entities, which hold the licenses and approvals necessary to operate our platform and provide value-added telecommunication-based online marketing services.

KEY MILESTONES

Our key business milestones are summarized below:

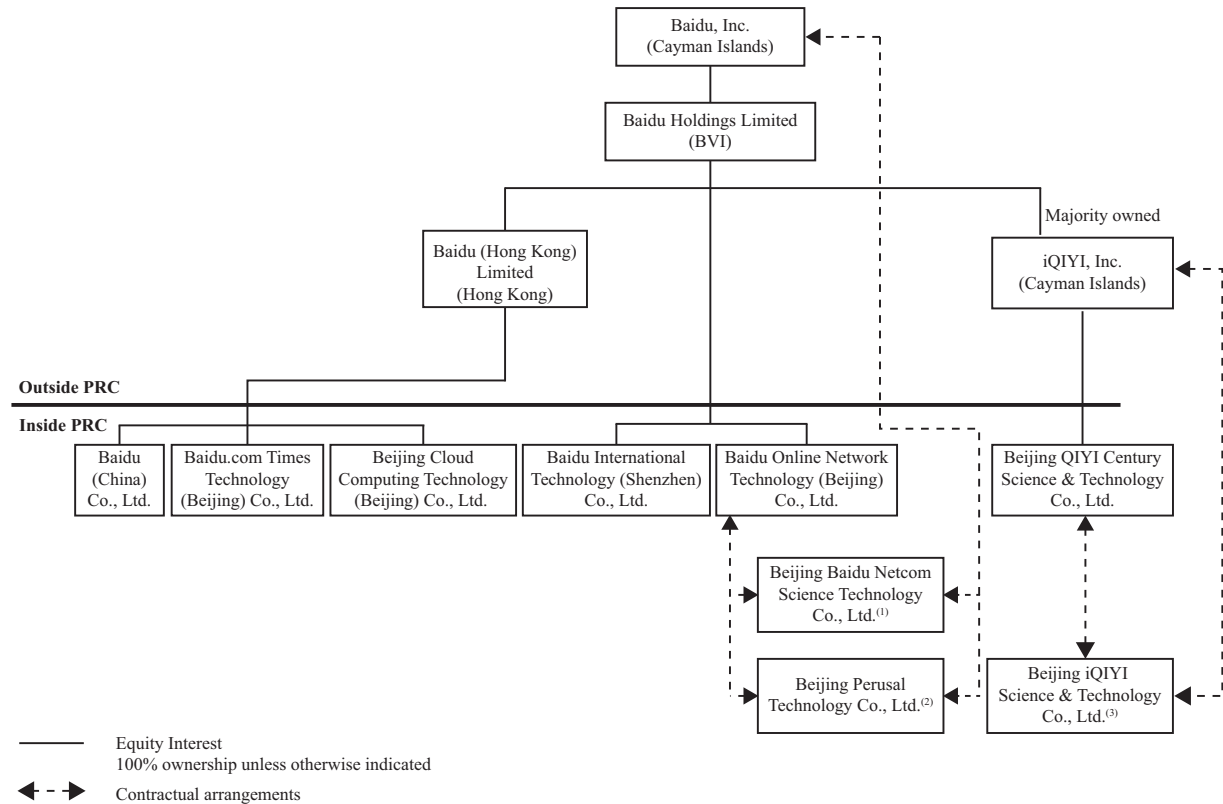
| <u>Date</u> | <u>Event</u> |
|-------------|---|
| 2000 | We incorporated the Company and commenced our business in January. |
| 2005 | In August, we and certain selling shareholders of our Company completed an initial public offering and listed our ADSs on Nasdaq under the symbol “BIDU”. |
| 2010 | We commenced our AI business in January. |
| 2012 | In November, we obtained the controlling interest in iQIYI, one of our main business segments. |
| 2017 | In August, we completed the disposal of Xiaodu Life Technology Ltd., our former subsidiary that was primarily engaged in the business of takeout delivery services, to Rajax Holding. |
| 2018 | In March, iQIYI completed an initial public offering and listed its ADSs on Nasdaq under the symbol “IQ”. |
| | In August, we completed the divestiture of a majority equity stake in our financial services business, Du Xiaoman. |

HISTORY AND CORPORATE STRUCTURE

CORPORATE STRUCTURE

Our corporate structure

The following diagram illustrates our corporate structure, including our principal subsidiaries and consolidated affiliated entities, as at the Latest Practicable Date:



* The diagram above omits the names of subsidiaries and consolidated affiliated entities that are insignificant individually and in the aggregate.

Notes:

- (1) Beijing Baidu Netcom Science Technology Co., Ltd. is 99.5% owned by Mr. Robin Yanhong Li, our chairman and chief executive officer, and 0.5% owned by Ms. Shanshan Cui, an executive officer of the Company. Please see “Major Shareholders” for details of Mr. Robin Yanhong Li’s beneficial ownership in our Company. Ms. Shanshan Cui’s beneficial ownership of our Company is less than 1% of our total outstanding shares.
- (2) Beijing Perusal Technology Co., Ltd. is 50% owned by Ms. Shanshan Cui and 50% owned by Mr. Zhixiang Liang. Both Ms. Shanshan Cui and Mr. Zhixiang Liang are our employees, and their respective beneficial ownership in our Company is less than 1% of our total outstanding shares.
- (3) Beijing iQIYI Science & Technology Co., Ltd. is wholly-owned by Mr. Xiaohua Geng, senior vice president of iQIYI. Mr. Xiaohua Geng is not beneficially interested in any shares of our Company.

HISTORY AND CORPORATE STRUCTURE

Significant Subsidiaries

As of December 31, 2020, we conducted our business operations across more than 200 subsidiaries and operating entities, twelve of which are our Significant Subsidiaries. Their principal business activities and dates of establishment are shown below:

| Name of company | Principal business activities | Date and jurisdiction of establishment |
|--|---|--|
| Baidu Holdings Limited | a holding company | November 30, 1999, BVI |
| Baidu (Hong Kong) Limited | a holding company and a company providing information technology services | November 27, 2007, Hong Kong |
| Baidu Online | a company providing information technology services | January 18, 2000, PRC |
| Baidu (China) Co., Ltd. | a company providing information technology services | June 6, 2005, PRC |
| Baidu.com Times Technology (Beijing) Co., Ltd. | a company providing technology services | April 19, 2006, PRC |
| Baidu International Technology (Shenzhen) Co., Ltd. | a company providing information technology services | November 23, 2010, PRC |
| Baidu Netcom | a consolidated affiliated entity providing internet information services | June 5, 2001, PRC |
| Beijing Perusal | a consolidated affiliated entity providing internet information services | June 6, 2006, PRC |
| iQIYI | a holding company | November 27, 2009, Cayman Islands |
| Beijing QIYI Century | a company providing online entertainment service related technology and operational service | March 8, 2010, PRC |
| Beijing iQIYI | a consolidated affiliated entity providing online entertainment service | March 27, 2007, PRC |
| Baidu Cloud Computing Technology (Beijing) Co., Ltd. | a company providing information technology services | January 5, 2012, PRC |

Major Acquisition and Disposal

Divestiture of majority equity stake in Du Xiaoman

In April 2018, we entered into definitive agreements with certain investors relating to our divestiture of a majority equity stake in our financial services business, Du Xiaoman. The financial services provided by the now-divested Du Xiaoman mainly include consumer credit, wealth management, financial technology services and payment support, through which Du Xiaoman mainly offers technology solutions to financial institution partners covering loan facilitation and risk management aspects and consumer financing to individual customers to meet their cash expenditure needs. To facilitate the divestiture, the Company conducted a series of legal restructuring and recapitalization of entities conducting the financial services business, which were accounted for as transactions under common control.

The divestiture was completed in August 2018 through issuance of preferred shares to third-party investors by Du Xiaoman, following which we held a non-controlling equity interest in Du Xiaoman,

HISTORY AND CORPORATE STRUCTURE

which was accounted for as an equity method investment, and have deconsolidated the financial results of Du Xiaoman from our consolidated financial statements in accordance with U.S. GAAP. To the best of their knowledge having made reasonable inquiry, our Directors believe that the third-party investors, are third parties independent of us and our connected persons. The disposal of Du Xiaoman did not meet the definition of a discontinued operation per ASC Subtopic 205-20, *Presentation of Financial Statements—Discontinued Operations*, as the divestiture did not represent a shift in strategy nor had a major impact to the Group’s operation and financial results.

Divestiture of interests in Xiaodu Life Technology Ltd. (“Xiaodu Life”)

In May 2018, we transferred all of our equity interests in Rajax Holding (“**Rajax**”), which operates the food delivery business under the ele.me brand in China, to Ali Panini Investment Limited. Previously in August 2017, our former subsidiary that was primarily engaged in the business of takeout delivery services and operated Baidu Deliveries, Xiaodu Life, completed its merger with Rajax and became a subsidiary of Rajax.

Acquisition of YY Live

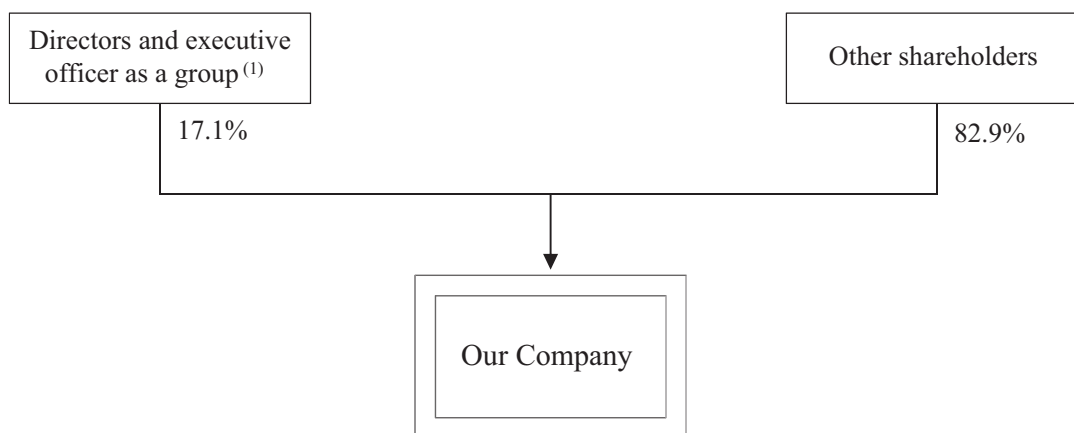
On November 16, 2020, Baidu (Hong Kong) Limited, our wholly-owned subsidiary, entered into a share purchase agreement with JOYY Inc. (Nasdaq:YY) and certain of its affiliates (collectively, “**JOYY**”) to acquire JOYY’s domestic video-based entertainment live streaming business in China (“**YY Live**”), for an aggregate purchase price of approximately US\$3.6 billion in cash, subject to certain adjustments. The purchase price was determined based on arm’s length negotiation, taking into account various factors, including, among others, the performance of YY Live and the potential synergies that YY Live may bring to our own business if the transaction is completed. Our Directors approved the transaction and believed, based on the circumstances that had been in existence at the time, that the terms of the transaction were fair and reasonable and in the interest of the shareholders of the Company as a whole. To the best of their knowledge having made reasonable inquiry, our Directors believe that, JOYY and Mr. David Xueling Li, the ultimate beneficial owner of JOYY, are third parties independent of us and our connected persons. The closing of the transaction is subject to certain conditions. On February 7, 2021, we entered into amended and restated share purchase agreement with JOYY. The acquisition has been substantially completed, with certain customary matters remaining to be completed in the near future. For further details, please refer to “Recent Developments—Business Updates”.

Apart from the above, we have not conducted any major acquisition or disposal during the Track Record Period.

HISTORY AND CORPORATE STRUCTURE

Shareholding structure

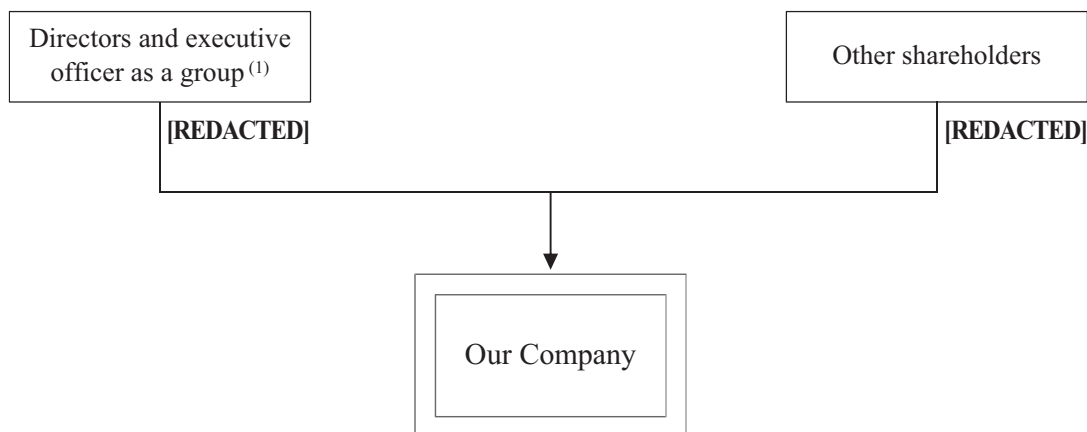
The following diagram illustrates our shareholding structure as at the Latest Practicable Date:



Notes:

(1) See “Major Shareholders” for further details on the voting rights and the beneficial ownership of our Directors and executive officers as a group and other shareholders. Each Class A ordinary share entitles the holder to exercise one vote, and each Class B ordinary share entitles the holder to exercise 10 votes on all matters that require a shareholder’s vote.

The following diagram illustrates our shareholding structure immediately upon the completion of the [REDACTED] (assuming all major shareholders’ shareholdings remain unchanged as of the Latest Practicable Date, the [REDACTED] is not exercised, and no additional Shares are issued under the Share Incentive Plans):



Please refer to the details contained in Note (1) above.

CONTRACTUAL ARRANGEMENTS

PRC laws and regulations restrict and impose conditions on foreign investment in internet content, value-added telecommunication-based online marketing, audio and video services and mobile application distribution businesses. Accordingly, we operate these businesses in China through our consolidated affiliated entities. We have entered into a series of contractual arrangements with our consolidated affiliated entities and the nominee shareholders of our consolidated affiliated entities.

These contractual arrangements enable us to:

- (a) receive the economic benefits that could potentially be significant to our consolidated affiliated entities in consideration for the services provided by our subsidiaries;

HISTORY AND CORPORATE STRUCTURE

- (b) exercise effective control over our consolidated affiliated entities; and
- (c) hold an exclusive option to purchase all or part of the equity interests in our consolidated affiliated entities when and to the extent permitted by PRC law.

These contractual agreements include exclusive technology consulting and services agreements, operating agreements, license agreements, business cooperation agreements, exclusive equity purchase and transfer option agreements, commitment letters, loan agreements, proxy agreements/powers of attorney and equity pledge agreements, as the case may be. Please see “History and Corporate Structure—Contractual Arrangements—Contractual Arrangements Relating to Our Consolidated Affiliated Entities” for further details. We do not have any equity interests in our consolidated affiliated entities. However, as a result of contractual arrangements, we have effective control over and are considered the primary beneficiaries of these companies, and we have consolidated the financial results of these companies in our consolidated financial statements. The nominee shareholders of Baidu Netcom, Beijing Perusal and Beijing iQIYI, our consolidated affiliated entities, are directors or members of senior management of the Company/iQIYI. We/iQIYI consider such people suitable to act as the nominee shareholders of these consolidated affiliated entities because of, among other considerations, their contribution to the Company/iQIYI, their competence and their length of service with and loyalty to the Company/iQIYI. If our consolidated affiliated entities or the nominee shareholders fail to perform their respective obligations under the contractual arrangements, we could be limited in our ability to enforce the contractual arrangements that give us effective control over our consolidated affiliated entities. Furthermore, if we are unable to maintain effective control, we would not be able to continue to consolidate the financial results of our consolidated affiliated entities in our financial statements. In 2018, 2019 and 2020, we derived 33%, 40% and 43% of our external revenues from our consolidated affiliated entities, respectively. Based on the book value of Baidu Netcom and Beijing Perusal and taking into account major adjustments for intra-group transactions, the revenue contribution of Baidu Netcom and Beijing Perusal to the Group for each of the years 2018, 2019 and 2020 was 9%, 14% and 15% and 0%, 0% and 0% respectively. Based on the book value of Baidu Netcom and Beijing Perusal and not taking into account adjustments for intra-group transactions, the net income of Baidu Netcom and Beijing Perusal attributable to Baidu, Inc. for each of the years 2018, 2019 and 2020 was -8%, -6% and 19% and -1%, 41% and -3% respectively. For a detailed description of the regulatory environment that necessitates the adoption of our corporate structure, please see “Regulations.” For a detailed description of the risks associated with our corporate structure, please see “Risk Factors—Risks Related to Our Corporate Structure”.

Contractual Arrangements Relating to Our Consolidated Affiliated Entities

The following is a summary of the material provisions of the contractual arrangements relating to Baidu Netcom, Beijing Perusal and Beijing iQIYI.

Exclusive Technology Consulting and Services Agreement

Pursuant to the exclusive technology consulting and services agreement between Baidu Online and Baidu Netcom, Baidu Online has the exclusive right to provide to Baidu Netcom technology consulting and services related to, among other things, the maintenance of servers, software development, design of advertisements, and e-commerce technical services. Baidu Online owns the intellectual property rights resulting from the performance of this agreement. Baidu Netcom agrees to pay service fees to Baidu Online and Baidu Online has the right to adjust the service fees at its sole discretion without the consent of Baidu Netcom. The agreement will be in effect for an unlimited term, until the term of business of one party expires and extension is denied by the relevant approval authorities.

HISTORY AND CORPORATE STRUCTURE

Each of the exclusive technology consulting and services agreements between Baidu Online and Beijing Perusal and Beijing QIYI Century and Beijing iQIYI contains substantially the same terms as those described above, except that the terms regarding determinant of the service fees may differ and that the initial term of the exclusive technology consulting and services agreement between Beijing QIYI Century and Beijing iQIYI dated November 23, 2011 is ten years, and has been extended.

Operating Agreement

Pursuant to the operating agreement amongst Baidu Online, Baidu Netcom and the nominee shareholders of Baidu Netcom, Baidu Online provides guidance and instructions on Baidu Netcom’s daily operations and financial affairs. In addition, Baidu Online agrees to guarantee Baidu Netcom’s performance under any agreements or arrangements relating to Baidu Netcom’s business arrangements with any third party. In return, Baidu Netcom agrees that without the prior consent of Baidu Online, Baidu Netcom will not engage in any transactions that could materially affect the assets, liabilities, rights or operations of Baidu Netcom, including, without limitation, incurrence or assumption of any indebtedness, sale or purchase of any assets or rights, incurrence of any encumbrance on any of its assets or intellectual property rights in favor of a third party or transfer of any agreements relating to its business operation to any third party. The agreement will be in effect for an unlimited term, until the term of business of one party expires and extension is denied by the relevant approval authorities.

The operating agreement amongst Baidu Online, Beijing Perusal and its shareholders contains substantially the same terms as those described above.

Pursuant to the amended and restated business operation agreement amongst Beijing QIYI Century, Beijing iQIYI and its shareholder, Beijing QIYI Century provides guidance and instructions on Beijing iQIYI’s daily operations and financial affairs. In addition, Beijing QIYI Century agrees to guarantee Beijing iQIYI’s performance under any agreements or arrangements relating to Beijing iQIYI’s business arrangements with any third party. The agreement can only be unilaterally revoked by Beijing QIYI Century. The initial term of the agreement is ten years, which has been extended, and can be further renewed at Beijing QIYI Century’s discretion.

License Agreements

Baidu Online and Baidu Netcom have entered into a software license agreement and a web layout copyright license agreement. Pursuant to these license agreements, Baidu Online has granted to Baidu Netcom the right to use, including but not limited to, a software license and a web layout copyright license. Baidu Netcom may only use the licenses in its own business operations. Baidu Online has the right to adjust the service fees at its sole discretion. The software license agreement and web layout copyright license agreement have been renewed since their original expiration and are in effect for an unlimited term, until the term of business of one party expires and extension is denied by the relevant approval authorities.

The web layout copyright license agreements that Baidu Online has entered into with Beijing Perusal contain substantially the same terms as those between Baidu Online and Baidu Netcom described above. The agreement is in effect for an unlimited term, until the term of business of one party expires and extension is denied by the relevant approval authorities.

Pursuant to the trademark license agreement and the software usage license agreement between Beijing QIYI Century and Beijing iQIYI effective November 23, 2011, Beijing QIYI Century granted a non-exclusive and non-transferable license, without sublicensing rights, to Beijing iQIYI to use its

HISTORY AND CORPORATE STRUCTURE

trademarks and software. Beijing iQIYI may only use the licenses in its own business operations. Beijing QIYI Century has the right to adjust the service fees at its sole discretion. The initial term of the two agreements is five years and the software usage license agreement may be extended upon the written consent of Beijing QIYI Century. The trademark license agreement is automatically extended for successive one-year periods after its expiration unless Beijing QIYI Century early terminates the agreement in accordance with the provisions of the agreement. The software usage license agreement was extended for another 15 years after its initial term.

Business Cooperation Agreement

Pursuant to the business cooperation agreement between Beijing QIYI Century and Beijing iQIYI effective November 23, 2011, Beijing iQIYI agrees to provide Beijing QIYI Century with services, including internet information services, online advertising and other services reasonably necessary within the scope of Beijing QIYI Century’s business. Beijing iQIYI agrees to use, technology services provided by Beijing QIYI Century on its website, including but not limited to, P2P download and video on-demand systems. Beijing QIYI Century agrees to pay specified service fees to Beijing iQIYI as consideration for the internet information services and other services provided by Beijing iQIYI. Beijing iQIYI has the right to waive the service fees at its discretion. The initial term of this agreement is ten years, which has been extended, and can be further renewed at Beijing QIYI Century’s discretion.

Exclusive Equity Purchase and Transfer Option Agreement

Pursuant to the exclusive equity purchase and transfer option agreement by and among the Company, Baidu Online, Baidu Netcom and the nominee shareholders of Baidu Netcom, the nominee shareholders of Baidu Netcom have irrevocably granted the Company or its designated person(s) (including Baidu Online) an exclusive option to purchase, to the extent permitted under PRC law, all or part of the equity interests in Baidu Netcom for the cost of the initial contributions to the registered capital or the minimum amount of consideration permitted by applicable PRC law. The nominee shareholders must remit to Baidu Online any amount that is paid by Baidu Online in connection with the purchased equity interest as requested by the Company or its designated person(s) (including Baidu Online) to the extent permitted by the applicable laws. The Company or its designated person(s) have sole discretion to decide when to exercise the option, whether in part or in full amount. Any and all dividends and other capital distributions from Baidu Netcom to the nominee shareholders must be paid to the Company in full amount. The Company or its designated person(s) (including Baidu Online) also have the exclusive right to cause the nominee shareholders of Baidu Netcom to transfer their equity interest in Baidu Netcom to the Company or any designated third party. The Company will provide unlimited financial support to Baidu Netcom, if Baidu Netcom becomes in need of any form of reasonable financial support in the normal operation of business. If Baidu Netcom were to incur any loss and as a result cannot repay any loans from the Company (through Baidu Online), the Company will unconditionally forgive any such loans to Baidu Netcom upon provision by Baidu Netcom of sufficient proof for its loss and incapacity to repay. The agreement will terminate upon the transfer by the nominee shareholders of Baidu Netcom of all their equity interests in Baidu Netcom to the Company or its designated person(s) or upon expiration of the term of business of the Company or Baidu Netcom.

Each of the exclusive equity purchase and transfer option agreements amongst the Company, Baidu Online, Beijing Perusal and its shareholders and iQIYI, Beijing QIYI Century, Beijing iQIYI and its shareholders contains substantially the same terms as those described above, except that the initial term of the amended and restated exclusive purchase option agreement amongst iQIYI, Beijing QIYI

HISTORY AND CORPORATE STRUCTURE

Century, Beijing iQIYI and its shareholder is ten years, which has been extended, and can be further renewed at iQIYI’s discretion.

Commitment Letters

Pursuant to the commitment letter dated January 30, 2013, under the condition that Beijing iQIYI remains as a consolidated affiliated entity of iQIYI under United States generally accepted accounting principles and the relevant contractual arrangements remain in effect, iQIYI and Beijing QIYI Century undertake to provide financial support to Beijing iQIYI for any financial loss that might affect its business operation occurred before and after the execution of the commitment letter as permitted by relevant laws. Such financial support shall be forgiven by iQIYI and Beijing QIYI Century.

Loan Agreements

Pursuant to loan agreements amongst Baidu Online and the nominee shareholders of Baidu Netcom, Baidu Online provided loans with an aggregate amount of RMB13.4 billion to the nominee shareholders of Baidu Netcom solely for the latter to fund the capitalization of Baidu Netcom. The loans can be repaid only with the proceeds from the sale of the nominee shareholders’ equity interest in Baidu Netcom to Baidu Online or its designated person(s). The term of the loan agreements with the two nominee shareholders of Baidu Netcom will expire on July 9, 2029 and August 19, 2029, respectively, and can be extended with the written consent of both parties before its expiration.

Pursuant to loan agreements amongst the shareholders of Beijing Perusal and Baidu Online, the amount of loans extended to the respective shareholders of Beijing Perusal is RMB3.2 billion. The term of the loan agreements will expire on March 30, 2028 and October 29, 2029, respectively, and can be extended with the written consent of both parties before its expiration. Each of the loan agreements amongst Baidu Online and the respective shareholders of Beijing Perusal, and Beijing QIYI Century and the shareholders of Beijing iQIYI, contains substantially the same terms as those described above, except that the amount of the loans and the contract expiration date varies. Beijing QIYI Century has extended the term of the amended and restated loan agreement.

Proxy Agreement/Power of Attorney

Pursuant to the proxy agreement amongst the Company and the nominee shareholders of Baidu Netcom, the nominee shareholders of Baidu Netcom agree to entrust all the rights to exercise their voting power and any other rights as shareholders of Baidu Netcom to the person(s) designated by the Company. Each of the nominee shareholders of Baidu Netcom has executed an irrevocable power of attorney to appoint the person(s) designated by the Company as their attorney-in-fact to vote on their behalf on all matters requiring shareholder approval. Any action taken by such attorney-in-fact in relation to the entrusted rights shall be directed and approved by the Company. The proxy agreement will be in effect for as long as the relevant nominee shareholder of Baidu Netcom holds any equity interests in Baidu Netcom unless terminated in writing by the Company. Each of the powers of attorney will be in effect for as long as the relevant nominee shareholder of Baidu Netcom holds any equity interests in Baidu Netcom.

Each of the proxy agreements or shareholder voting rights trust agreements amongst the Company and the shareholders of Beijing Perusal and between Beijing QIYI Century and the shareholder of Beijing iQIYI contains substantially the same terms as those described above. Each of the proxy agreements or shareholder voting rights trust agreements will be in effect for an unlimited term unless terminated in writing by the Company or other subsidiaries. Each of the powers of attorney or shareholder voting

HISTORY AND CORPORATE STRUCTURE

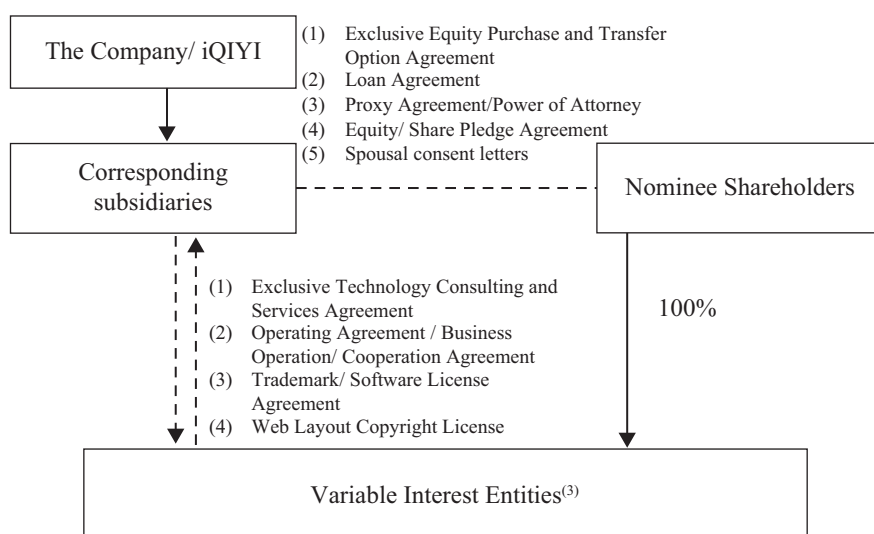
rights trust agreements will be in effect for as long as the shareholder of Beijing Perusal or Beijing iQIYI holds any equity interests in Beijing Perusal or Beijing iQIYI, as the case may be.

Equity Pledge Agreement

Pursuant to the equity pledge agreement amongst Baidu Online and the nominee shareholders of Baidu Netcom, the nominee shareholders of Baidu Netcom shall pledge all of their equity interests in Baidu Netcom to Baidu Online to guarantee their obligations under the loan agreements and Baidu Netcom’s performance of its obligations under the exclusive technology consulting and service agreement. If Baidu Netcom or the nominee shareholders breach their respective contractual obligations, Baidu Online, as the pledgee, will be entitled to certain rights, including the right to sell the pledged equity interests. The nominee shareholders of Baidu Netcom agree not to dispose of the pledged equity interests or take any actions that would prejudice Baidu Online’s interest. The equity pledge agreement will terminate on the date when Beijing Netcom and its shareholders have completed all their respective obligations under the exclusive technology consulting and service agreement and the loan agreements.

Each of the equity pledge agreements amongst Baidu Online and the shareholders of Beijing Perusal and Beijing QIYI Century and the shareholder of Beijing iQIYI, contains substantially the same terms, including its term to expiration, as those described above.

The diagram below illustrates the general structure of the economic flow and control under the VIE structure created by the contractual arrangements described above:



Notes:

- (1) “→” denotes the direction of legal and beneficial ownership.
- (2) “---” denotes the contractual arrangements among the variable interest entities, their nominee shareholders, and corresponding subsidiaries (being Baidu Online and Beijing QIYI Century).
- (3) Baidu Netcom, Beijing Perusal and Beijing iQIYI.

Through design of the aforementioned agreements, the nominee shareholders of these affiliated entities have effectively assigned their full voting rights to the Company/iQIYI, which gives the Company/iQIYI the power to direct the activities that most significantly impact the affiliated entities’ economic performance. The Company/iQIYI obtains the ability to approve decisions made by the affiliated entities and the ability to acquire the equity interests in the affiliated entities when permitted by PRC law. The Company/iQIYI is obligated to absorb losses of the affiliated entities that could potentially be

HISTORY AND CORPORATE STRUCTURE

significant to the affiliated entities through providing unlimited financial support to the affiliated entities or is entitled to receive economic benefits from the affiliated entities that could potentially be significant to the affiliated entities through the exclusive technology consulting and service fees. As a result of these contractual arrangements, the Company/iQIYI is determined to be the primary beneficiary of these affiliated entities. Despite the lack of technical majority ownership, there exists a parent-subsidiary relationship between us and these affiliated entities through these contractual arrangements, and we consolidate these affiliated entities through the Company/iQIYI.

We have also entered into contractual arrangements with several other affiliated entities and their respective nominee shareholders, including iQIYI’s affiliated entities and their respective nominee shareholders, through some of our subsidiaries other than Baidu Online and Beijing QIYI Century, which result in the Company/iQIYI or relevant subsidiaries, as the case may be, being the primary beneficiaries of the relevant affiliated entities. As a result of these contractual arrangements, there exists a parent-subsidiary relationship between us and the relevant affiliated entities, and we consolidate these affiliated entities through the subsidiaries.

Confirmations and risks relating to the variable interest entity structure

Our PRC Legal Adviser is of the opinion that:

- (a) the current ownership structure of our variable interest entities and the corresponding subsidiaries in China is not in violation of applicable PRC laws and regulations currently in effect;
- (b) each of the contractual arrangements entered into by the Company, our variable interest entities, the corresponding subsidiaries and their respective shareholders governed by PRC laws and regulations are validly executed, legal and binding, and does not result in violation of any applicable PRC laws and regulations or their respective articles of association currently in effect; and
- (c) each of the contractual arrangements entered into by our variable interest entities, the corresponding subsidiaries and their respective shareholders governed by PRC laws and regulations have not been deemed as “concealment of illegal intentions with a lawful form” and void under the PRC Contract Law and, subsequent to the expiration of the PRC Contract Law and the PRC Civil Code being effective on January 1, 2021, are not deemed as void under applicable PRC laws and regulations currently in effect.

Based on the above, our directors believe that the agreements underlying the contractual arrangements as described above that confer significant control and economic benefits from the variable interest entities to us are enforceable under the relevant laws. Nevertheless, any violations by the variable interest entities of our agreements with them could disrupt our operations or adversely affect our services. See “Risk Factors—Risks Related to Our Corporate Structure.” Appropriate arrangements have been made to protect the Company’s interests in the event of death or certain indebtedness of the nominee shareholders.

Additionally, we have been advised by our PRC Legal Adviser that there are substantial uncertainties regarding the interpretation and application of current and future PRC Laws. Accordingly, PRC regulatory authorities or courts may take a view that is contrary to the opinion of our PRC Legal Adviser. It is uncertain whether any new PRC Laws relating to contractual arrangements will be adopted, or if adopted, what the Laws would provide. If we or our variable interest entities are found to be in violation of existing or future PRC Laws, or fail to obtain or maintain any of the required permits or approvals, the relevant PRC regulatory authority would have broad discretion to take action in

HISTORY AND CORPORATE STRUCTURE

dealing with the violation or failure, in which case we could be subject to severe penalties, including being prohibited from continuing our operations or unwinding the contractual arrangements. See “Risk Factors—Risks Related to Our Corporate Structure” and “Risk Factors—Risks Related to Doing Business in China.”

We have considered the costs and difficulties of acquiring insurance on commercially reasonable terms, and consider it impractical for us to have insurance to cover these risks. Accordingly, we have not purchased insurance to cover the risks relating to the contractual arrangements.

As of the Latest Practicable Date, we had not encountered any interference or encumbrance from any PRC regulators in operating our business through our variable interest entities under the contractual arrangements.

Listing on Nasdaq

On August 5, 2005, we listed our ADSs on Nasdaq under the symbol “BIDU.” Since the date of our listing on Nasdaq and up to the Latest Practicable Date, our Directors confirm that we had no instances of non-compliance with the rules of Nasdaq in any material respects and to the best knowledge of our Directors having made all reasonable enquiries, there is no matter that should be brought to [REDACTED] attention in relation to our compliance record on Nasdaq. The Joint Sponsors, on the basis of above and independent due diligence conducted (including but not limited to independent searches and interviews with the Company’s management and Directors), concur with the Directors’ view above.

We believe that the Listing on the Hong Kong Stock Exchange will present us with an opportunity to further expand our [REDACTED] base and broaden our access to capital markets.

SAFE Registration

Pursuant to the Circular of the SAFE on Foreign Exchange Administration of Overseas Investment, Financing and Round-trip Investments Conducted by Domestic Residents through Special Purpose Vehicles (關於境內居民通過特殊目的公司境外投融資及返程投資外匯管理有關問題的通知, “**SAFE Circular 37**”), promulgated by SAFE on July 4, 2014 and which replaced the Notice on Issues Relating to the Administration of Foreign Exchange in Fund-Raising and Round-Trip Investment Activities of Domestic Residents Conducted via Offshore Special Purpose Companies (關於境內居民通過境外特殊目的公司融資及返程投資外匯管理有關問題的通知, “**SAFE Circular 75**”), (a) a PRC resident must register with the local SAFE branch before he or she contributes assets or equity interests to an overseas special purpose vehicle (the “**Overseas SPV**”) that is directly established or indirectly controlled by the PRC resident for the purpose of conducting investment or financing, and (b) following the initial registration, the PRC 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 of Overseas SPV’s PRC resident shareholder(s), the name of the Overseas SPV, terms of operation, or any increase or reduction of the Overseas SPV’s capital, share transfer or swap, and merger or division. Pursuant to SAFE Circular 37, failure to comply with these registration procedures may result in penalties.

Pursuant to the Circular of the SAFE on Further Simplification and Improvement in Foreign Exchange Administration on Direct Investment (關於進一步簡化和改進直接投資外匯管理政策的通知), “**SAFE Circular 13**”), promulgated by SAFE on February 13, 2015, the power to accept SAFE registration was delegated from local SAFE to local banks where the assets or interests in the domestic entity are located.

HISTORY AND CORPORATE STRUCTURE

As advised by our PRC Legal Adviser, Mr. Robin Yanhong Li, our chairman, chief executive officer and principal shareholder, who is a PRC resident, has registered, and updated registration when required, with the relevant local SAFE branch.

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The information and statistics set out in this section and other sections of this [REDACTED] were extracted from official government publications, public market research and independent research. In addition, we engaged China Insights Consultancy (CIC), an independent market research and consulting company, for the [REDACTED]. Except as otherwise noted, all of the information contained in this section is derived from CIC’s industry report (CIC Report). We believe that the sources of the information in this section and other sections of this [REDACTED] are appropriate sources for such information, and we have taken reasonable care in extracting and reproducing such information. We have no reason to believe that such information is false or misleading or that any fact has been omitted that would render such information false or misleading. The information from official and non-official sources has not been independently verified by us, [REDACTED], Joint Sponsors, [REDACTED], [REDACTED], any of [REDACTED], any of their respective directors and advisers, or any other persons or parties involved in the [REDACTED], and no representation is given as to its accuracy. Accordingly, the information from official and non-official sources contained herein may not be accurate and should not be unduly relied upon. Our Directors confirm that, after making reasonable enquiries, there is no adverse change in the market information since the date of the CIC Report that would qualify, contradict or have a material impact on the information in this section.

Baidu Core offers products and services in three growth engines, namely Mobile Ecosystem, AI Cloud and Intelligent Driving & Other Growth Initiatives. This section sets out overview of the industries and markets relating to these engines, including China’s (i) knowledge-and information-centric internet platforms, (ii) cloud service market, (iii) intelligent driving industry, (iv) new energy vehicle market, (v) smart devices market, (vi) AI chip industry and (vii) Internet healthcare industry. In addition, with respect to iQIYI, this section provides certain information about the online entertainment industry in China.

Overview of Artificial Intelligence in China

Artificial Intelligence technologies have developed differently in different parts of the world. However, according to the CIC Report, building a powerful AI system requires (i) chips and cloud computing to provide sufficient computational power to process massive amounts of data, (ii) a deep learning framework and model library, especially from open-source AI platforms, to enable developers to build high-quality AI algorithms and (iii) application-level capabilities, such as speech recognition, computer vision, optical character recognition and NLP, that help realize the abilities to perceive, understand and make decisions.

China is at the forefront of AI technology development. In 2019, China ranked No.1 globally in terms of total number of AI research papers published, No.1 globally in terms of number of AI patent applications and No.2 globally in terms of total number of AI companies, according to the CIC Report. Chinese AI companies also raised the highest amount of capital globally from 2015 to 2019. Since 2015, China’s investment in AI has surpassed that of the U.S. and reached approximately US\$46.76 billion in 2019, compared with US\$38.65 billion in the U.S, according to the CIC Report.

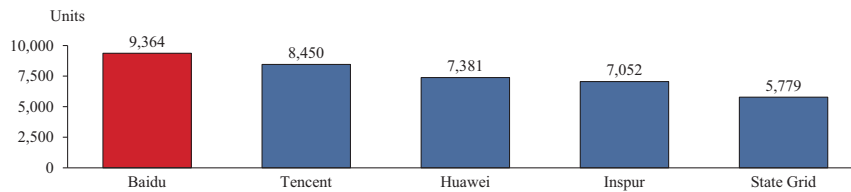
To compete successfully, AI companies shall possess the following criteria: (i) a robust ecosystem where ample data is available for machine learning and algorithm enhancement, (ii) technologically superior and cost-effective hardware and software integrated solutions and (iii) sufficient financial resources to support research and development and talent retention, as the path to monetization can be long and uncertain, according to the CIC Report. To date, Baidu is the only Chinese company to have

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developed full-stack AI capabilities ranging from chip design to deep learning framework and application-level AI capabilities, according to the CIC Report, resulting in its leadership in the following areas:

- Baidu holds the largest number of AI patent applications in China as of October 30, 2020.

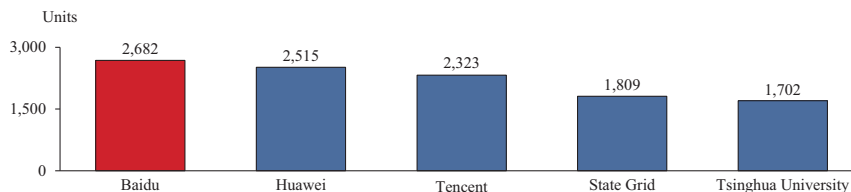
Top Companies by Cumulative Number of AI Patent Applications in China (October 30, 2020)



Source: CIC Report, China National Industrial Cyber Security Development Center

- Baidu holds the largest number of AI patents in China as of October 30, 2020.

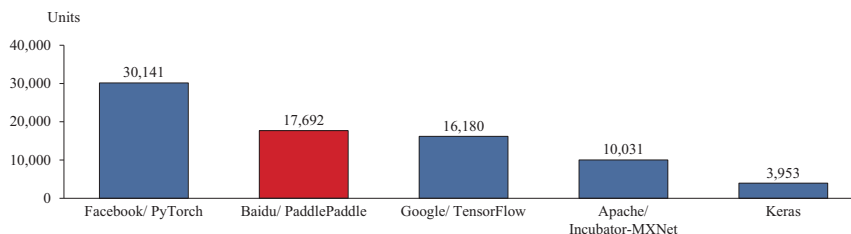
Top Companies by Cumulative Number of AI Patents in China (October 30, 2020)



Source: CIC Report, China National Industrial Cyber Security Development Center

- PaddlePaddle, Baidu’s open-source deep learning framework, ranked No.2 globally in terms of cumulative number of pull requests as measured in GitHub, the most popular open-source technology community in the world, as of December 31, 2020.

Top Open-Source Frameworks Globally by Cumulative Pull Request (December 31, 2020)

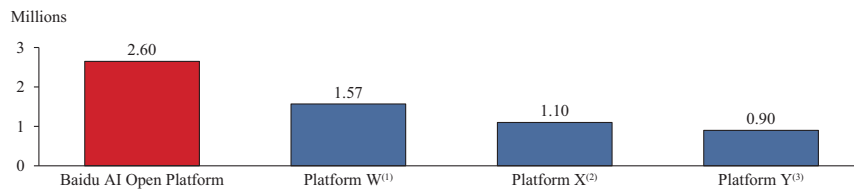


Source: CIC Report, GitHub

- Baidu AI Open Platform ranked No.1 in China in terms of number of developers as of December 31, 2020.

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Top Open Platforms in China by Number of Developers (December 31, 2020)



Notes:

- (1) Platform W is an open platform established by Company W, a voice focused AI solution provider.
- (2) Platform X is an open platform established by a public cloud services provider owned by a leading Internet company, Company X.
- (3) Platform Y is an open platform established by a public cloud services provider owned by a leading Internet company, Company Y.

Source: CIC Report

Advancement in computing power, algorithm and data volume, combined with significant financial resources and human capital, will continue to drive the development of AI technologies and related downstream fields such as AIoT and other AI-enabled products and services. Massive amounts of data will be produced, which will further enhance algorithms to eventually develop human-like intuition and behaviors.

Overview of Knowledge-and-Information-Centric Internet Platforms in China

China’s knowledge-and-information-centric Internet platforms include online search platforms, newsfeed platforms and other knowledge-and-information-centric online platforms. According to the CIC Report, China’s knowledge-and-information-centric Internet platforms play an important role in China’s Internet industry, with over 600 million active users, who spent a daily average of approximately 2.4 hours on these platforms in 2019. AI technologies are crucial for crawling unstructured Internet data, understanding user’s queries and recommending relevant content to users, which make knowledge-and-information-centric Internet platforms an integral part of the Internet space.

As a result of their massive user base and strong ability to help generate high consumer conversion rate, knowledge-and-information-centric Internet platforms have been attractive to brands for empowering their marketing and promotional activities. Consequently, online advertising has been the main source of revenue for knowledge-and-information-centric Internet platforms.

Key Trends and Drivers

According to the CIC Report, the key trends and drivers of the knowledge-and-information-centric Internet platforms include:

- ***Emergence of “super app”***

A super app is an app that encompasses and integrates a variety of functions from other apps and sites, such as search, Q&A, video, live streaming and e-commerce, without the need to direct users to other apps or sites. Therefore, a super app can better analyze and understand user behavior, improve and expand its functions and further increase user time spent in the app.

- ***Combining search and feed***

Search engines traditionally respond to user’s queries by providing a list of links that direct users to other sites for searched information and content. In the era of smart phones, as a result of smaller

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screen size as well as the ability to accurately track user behavior, many platforms aim to provide personalized and curated content. By predicting and recommending to users content from the platforms themselves and third-party sources, apps can offer users higher levels of interaction and result in a higher conversion rate.

- ***AI-enhanced search methods***

Historically, traditional search requires users to manually type key words. AI technologies, such as speech recognition and computer vision, allow users to communicate their intent more naturally and efficiently, through speech and image scanning, than through typing. Search interactions provide valuable user intent information that can be used to further enhance AI recommendation algorithms.

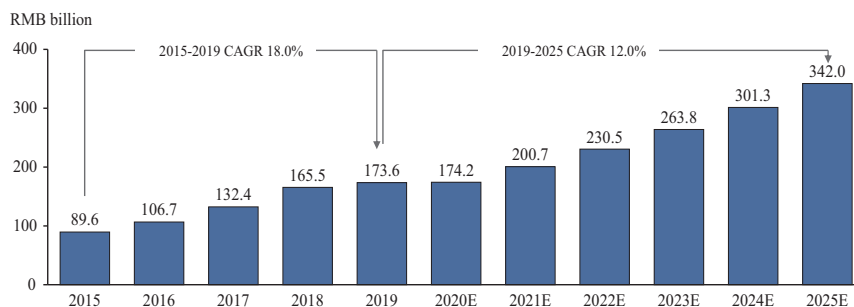
- ***More diversified monetization channels***

Better user understanding and increased user traffic could lead to faster growth in advertising revenue, as well as revenue generated from services provided to individuals (e.g., membership, online literature, online audio, and live broadcasting), which amounted to RMB214.9 billion in 2019, and is expected to increase to RMB750.5 billion in 2025, representing a CAGR of 23.2% between 2019 and 2025.

Market Size

The market size of advertising on knowledge-and-information-centric Internet platforms in China has grown from RMB89.6 billion in 2015 to RMB173.6 billion in 2019, representing a CAGR of 18.0%, according to the CIC Report. The market size is expected to reach RMB342.0 billion in 2025, representing a CAGR of 12.0% between 2019 and 2025.

Market Size of Advertising on Knowledge-and-Information-Centric Internet Platforms in China (2015-2025E)



Source: CIC Report

Competitive Landscape

According to the CIC Report, Baidu has been the No.1 search engine in China in the last decade in terms of revenue and number of users, as well as the No.1 “search-plus-feed” app in China in terms of MAUs and DAUs in December 2020. Baidu is also the No.1 knowledge-and-information-centric Internet platform in China in terms of online advertising revenue in 2019 and the only company with leading position in both search and feed advertisement.

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Our market share in search engine market in China keeps stable in recent 3 years. As illustrated by the table below, we have the highest market share (in terms of revenue in 2020), MAU and DAU among our peers which operate search engines in China.

| Ranking | Companies | Market share in terms of revenue (2020, %) | Average MAUs (2020, in millions) | DAUs (2020, in millions) |
|---------|------------------------------|--|----------------------------------|--------------------------|
| 1 | Baidu | 72.7% | 538.28 | 208.06 |
| 2 | Search engine $\alpha^{(1)}$ | 7.9% | 61.14 | 26.36 |
| 3 | Search engine $\beta^{(2)}$ | 6.6% | 29.94 | 6.79 |
| 4 | Search engine $\gamma^{(3)}$ | N/A | 2.12 | 0.69 |

Notes:

(1) Search engine α is a search engine with over 10 years history.

(2) Search engine β is a search engine acquired by a leading Internet company, Company Y.

(3) Search engine γ is a search engine owned by a leading Internet company, Company X.

Source: CIC report

There are vertical service providers in the forms of mobile apps and/or websites that allow users to search within their closed ecosystems. These players often purchase traffic from search engines and try to retain their users by offering comprehensive services on their platforms. Concurrently, Baidu is also extending its service offerings in various verticals, such as healthcare, business-to-business and live streaming, to increase the vibrancy of its platform.

As illustrated by the table below, we have the highest MAU and DAU among all of the knowledge-and-information-centric Internet platforms in China.

| Ranking | Companies | Average MAUs (2020, in millions) | DAUs (2020, in millions) |
|---------|---|----------------------------------|--------------------------|
| 1 | Baidu | 538.28 | 208.06 |
| 2 | Knowledge-and -information-centric Internet platform $\alpha^{(1)}$ | 446.88 | 182.24 |
| 3 | Knowledge-and -information-centric Internet platform $\beta^{(2)}$ | 422.79 | 123.48 |

Notes:

(1) Internet platform α is a knowledge-and-information-centric platform with over 10 years development history.

(2) Internet platform β is a knowledge-and-information-centric platform owned by a leading Internet company, Company Y.

Overview of Cloud Service Market in China

The concept of cloud services was first commercially introduced by Amazon in 2006. Since then, the market for cloud services has grown steadily globally, as enterprises continued to shift away from on-premise IT infrastructure. According to the CIC Report, China is the world’s second largest cloud service market in 2019. The penetration rate of China’s cloud service market, which is calculated by dividing the market size of cloud services by the total IT spending, was only approximately 5.1% in 2019, implying significant room for further development, according to the CIC Report.

As enterprises undergo digital transformation with a heightened focus to improve cost efficiency, cloud services in China is expected to experience tremendous growth and further penetration in the near future, according to the CIC Report.

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Key Trends and Drivers

According to the CIC Report, the key trends and drivers of China’s cloud service market include:

- ***Continued penetration in traditional enterprises***

Cloud service’s penetration is expected to increase among traditional enterprises, due to their ability to reduce cost and improve productivity. In addition, as traditional enterprises continue to undergo digital transformation by adopting more software solutions, they will become more receptive to the shift away from on-premise infrastructure.

- ***Increased demand from Internet users***

China has a massive number of Internet users, which will continually drive the development and growth of Internet products and services offerings. The surge of products and services will lead to increased demand for cloud services, which is sought after for its flexibility and scalability.

- ***Increased multi-cloud provider preference***

Multi-cloud strategies will reduce vendor dependency and cloud computing cost for enterprises. Thus, more enterprises are expected to adopt multi-cloud strategy. Benefiting from multi-cloud-provider preference, providers with neutrality, large-scale and quick ramp up capabilities are expected to have promising development prospect.

- ***Increased penetration of 5G and IoT will lead to more demand for AI***

The continued deployment of 5G technology will bring about significantly increased data transmission speed. This will benefit the development of video content as well as IoT, which will in turn vastly increase the demand for data storage and processing. In addition, IoT often requires AI technologies to interact with users, which will require deployment of cloud services.

- ***Favorable government policies and increased spending in intelligent transportation system***

During China’s 12th Five-Year Plan (2010-2015), the cloud services industry received significant amounts of investment and such high levels of investments have continued into the 13th Five-Year Plan (2016-2020). Furthermore, to revitalize its economy in light of the impact of COVID-19, the Chinese government ramped up a series of initiatives to boost “New Infrastructure” nationwide, covering areas such as 5G networks, AI technologies, IoT development and inter-city high-speed rail systems, as well as the establishment of research and development institutions related thereto. Almost all of the applications and technologies related to these initiatives require support from cloud services.

In addition, the Chinese government has awarded RMB9.8 billion worth of intelligent transportation system (ITS) contracts in 2019, which mainly includes intelligent vehicle infrastructure cooperative system, intelligent traffic signal control system, and intelligent public transportation system projects. ITS projects are government-led initiatives aimed to mitigate traffic jams, parking difficulties and overcrowding in public transportation faced by urban commuters in China. According to the CIC Report, investment in ITS is expected to reach approximately RMB52.2 billion in 2025, representing a CAGR of 32.0% between 2019 and 2025.

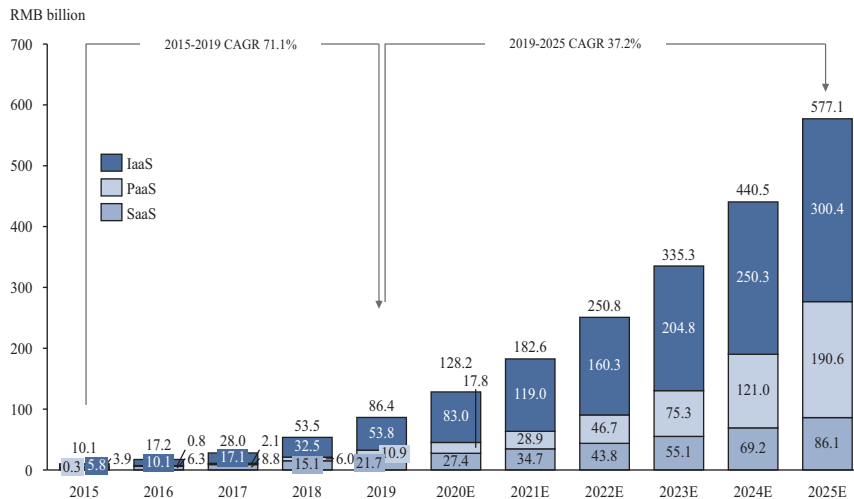
Market Size

China’s cloud service market has experienced significant growth since 2015, and China has become one of the fastest growing markets in the world. IaaS, the most basic type of cloud services, represents

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a large portion of the cloud service market in China. PaaS and SaaS are gaining popularity among developers and enterprises, owing to their customized and function-specific nature. According to the CIC Report, the market size of public cloud services industry in China grew from RMB10.1 billion to RMB86.4 billion between 2015 and 2019, representing a CAGR of 71.1% during that period, and is expected to grow to RMB577.1 billion by 2025, representing a CAGR of 37.2% from 2019 to 2025. The chart below presents the historical and expected market size of public cloud services in China.

Market Size of Public Cloud Services in China (2015-2025E)



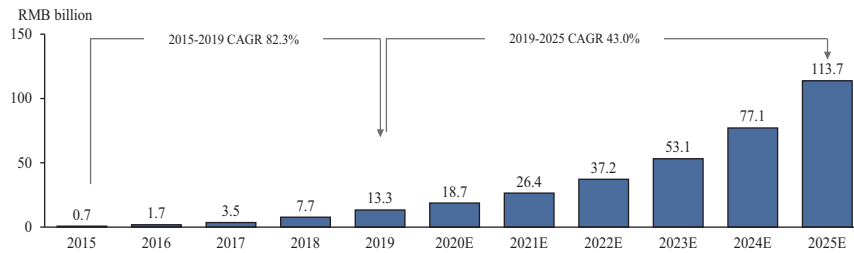
Source: CIC Report

According to the CIC Report, many developers and enterprises are faced with the challenge of integrating AI capabilities into their existing applications and products, as well as obtaining sufficient computing power to train and improve AI algorithms to meet their business needs. It is expensive and time-consuming to build and operate highly intelligent and scalable AI capabilities. Alternatively, AI cloud services can serve as “building blocks” for developers and enterprises by providing AI capabilities in the form of API. Leveraging AI cloud services is a convenient way for developers and enterprises to incorporate AI capabilities into their existing products and services, without spending large amounts of capital to upgrade their companies’ internal IT infrastructure or develop their own AI capabilities. According to the CIC Report, this high level of flexibility is the primary reason why an increasing number of enterprises are adapting cloud-based AI services.

AI cloud solutions can be applied through PaaS and SaaS, or implemented through customized private cloud solutions. According to the CIC Report, the addressable market for AI cloud solution providers has grown from RMB0.7 billion to RMB13.3 billion between 2015 and 2019, representing a CAGR of 82.3% during the period, and is expected to reach RMB113.7 billion by 2025, growing at a CAGR of 43.0% from 2019 to 2025.

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Addressable Market for AI Cloud Solutions Providers in China (2015-2025E)



Source: CIC Report

Competitive Landscape

Baidu is among China’s top four public cloud services providers and the leader in the AI public cloud service market in 2019, according to the CIC Report. Although the AI cloud service market is still at an early stage of development, Baidu has already distinguished itself as a clear market leader, according to the CIC Report. Our AI Cloud is the largest AI public cloud in China, in terms of product portfolio and APIs used by developers in 2020, according to the CIC Report.

| 2020 | AI cloud product portfolio (Unit) | APIs used by developers (Billion) |
|------------------------------|-----------------------------------|-----------------------------------|
| Baidu AI Cloud | ~330 | ~58 |
| Cloud X ⁽¹⁾ | ~260 | ~47 |
| Cloud Y ⁽²⁾ | ~240 | ~45 |

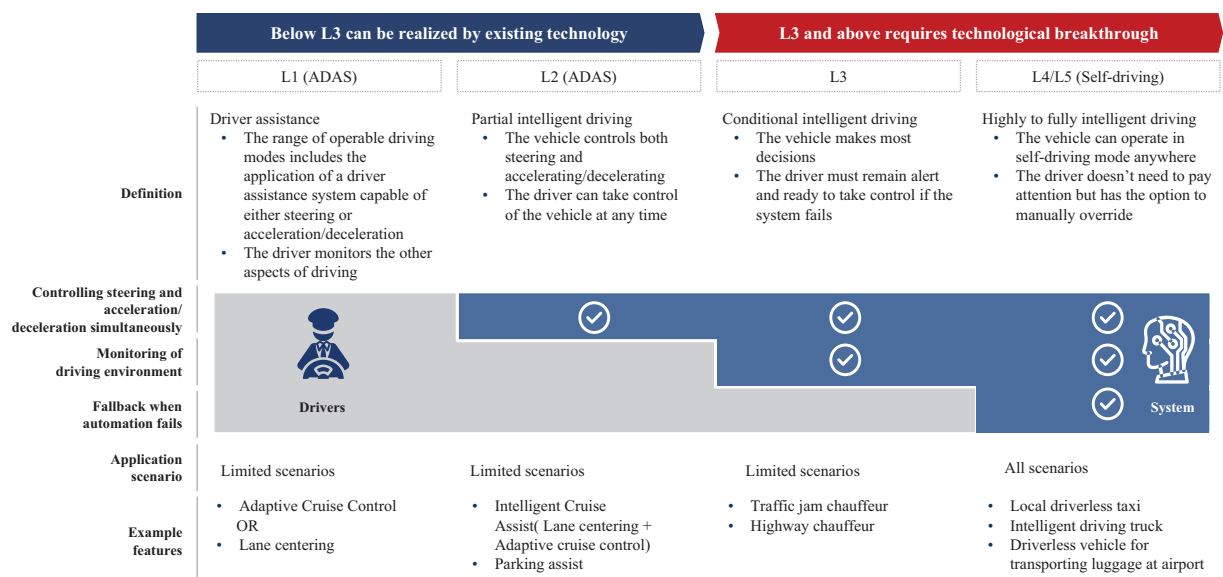
Notes:

- (1) Cloud X is a cloud services provider owned by a leading Internet Company, Company X.
- (2) Cloud Y is a cloud services provider owned by a leading Internet Company, Company Y.

Source: CIC Report

Overview of China’s Intelligent Driving Industry

Significant technological advancements have been made in the area of intelligent driving, which has evolved from providing basic driver assistance to enabling automobiles to sense and react autonomously. The graph below illustrates the key developmental stages of intelligent driving, according to the CIC Report.



Source: CIC Report

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Autonomous driving is perceived as the ultimate goal of intelligent driving, and operating robotaxis, in place of taxi rides, and ride sharing, is one of the largest monetization opportunities for autonomous driving. According to the CIC Report, many intelligent driving technology companies will develop their own proprietary algorithms and then task an automaker to assemble the necessary hardware together to produce fully self-driving vehicles. Although there could be years before robotaxis become fully commercialized due to technological and regulatory reasons, the evolution of intelligent driving is currently taking place. Automated valet parking, which enables vehicles to search for nearby parking and park itself, will be offered by multiple automakers in 2021 car models, according to the CIC Report. Going forward, it is expected that more intelligent driving solutions with a wide range of functionalities and capabilities, will be made available to consumers.

Key Trends and Drivers

According to the CIC Report, the key trends and drivers of the intelligent driving industry in China include:

- ***Increased adoption of intelligent features***

Sensors and cameras are becoming standard features in today’s passenger vehicles. According to the CIC Report, around 40% of new passenger vehicles sold in China in 2019 were equipped with L1/L2 capabilities. Consumers have been increasingly receptive to these new features, due to their ability to significantly improve safety and reduce risk of accidents, which encourages automakers to install such intelligent features in more vehicles in the future.

- ***Continued rise in labor cost***

Labor cost represents a significant portion in the taxi business. Continued rise in labor cost could give solution providers sufficient motivation to come up with alternative options, while encouraging business operators to adopt new technologies and change its existing form of operation.

- ***Reduction in hardware cost***

As prices for hardware, such as GPU, radar, and LiDAR, continued to decline, intelligent driving companies may increase the number of test vehicles and test miles, which will further improve autonomous driving algorithms. Also, a decline in cost also encourages automakers to adopt more advanced hardware and intelligent driving solutions in new car models.

- ***Increased investment***

Intelligent driving has drawn interest from a large number of investors. Continued investment and increase in start-ups entering the field are conducive to both the development of technology and commercialization of intelligent driving.

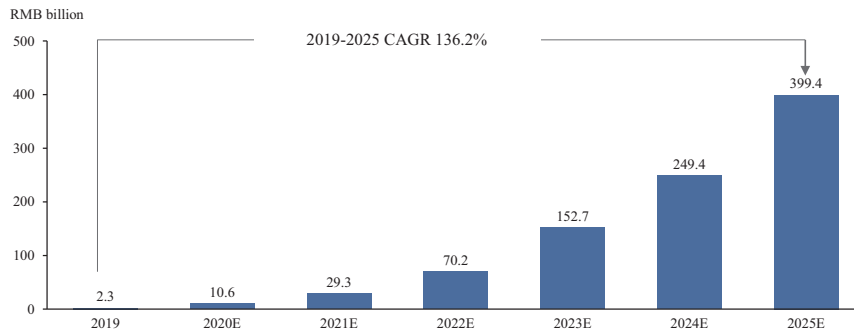
Market Size

The entire intelligent driving industry in China has significant growth potential. The total addressable market of robotaxis fleet operations, which is assumed to be equivalent to the combination of taxi, ride-sharing and rental car markets, is expected to amount to RMB1,458.1 billion in 2025, according to the CIC Report. While the robotaxi market represents significant monetization opportunity for fleet

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operators, it may not reach meaningful commercialization scale before 2023. In the meantime, self-driving services, such as automated valet parking and autonomous navigation, will drive industry growth. The market size for self-driving services in China is expected to increase from RMB2.3 billion to RMB399.4 billion between 2019 and 2025, representing a CAGR of 136.2% during the six-year period. The charts below present the historical and expected market size of self-driving services in China.

Market Size of Self-Driving Services Industry in China (2019-2025E)

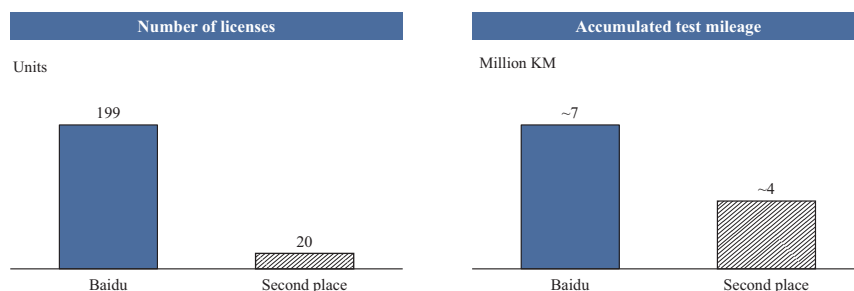


Source: CIC Report

Competitive Landscape of Autonomous Driving in China

As the leader in autonomous driving in China, Baidu Apollo has secured the largest number of autonomous driving licenses and has the highest accumulated test miles as of December 31, 2020, according to the CIC Report. Apollo’s leading scale in the autonomous driving industry, including having the most commercialized robotaxi pilot programs, enables it to collect more road scenarios from more geographic locations, as well as improve its algorithms faster and more efficiently than its peers. Accumulated miles, driving simulation and learnings from autonomous driving are used to strengthen Apollo’s competitiveness in self-driving services and V2X smart transportation solutions, and the network effect of the latter two will also boost Apollo’s strategic advantage for autonomous driving. Apollo’s autonomous driving aims to offer an alternative to Waymo’s LiDAR reliant approach by leveraging vehicle-to-road cooperative system to provide a more economical solution to autonomous driving. Unit economics will be a critical factor to the success of autonomous driving adoption. The chart below illustrates industry ranking of autonomous driving companies in China as of December 31, 2020.

Industry Ranking of Autonomous Driving Companies in China (December 31, 2020)



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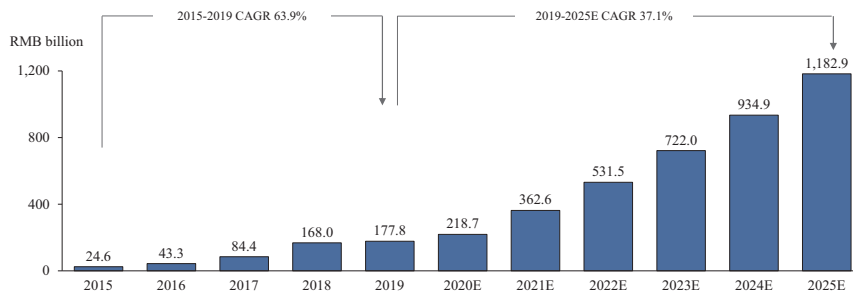
Overview of the New Energy Vehicle (NEV) market in China

China is one of the largest NEV markets in the world, which has significant growth potential due to the rapid development of the Chinese economy, strong support from government and improving awareness on environment protection and energy saving. Developing new energy vehicle is one of the critical solutions to help balance economy development and environment protection, gradually reducing China’s heavy reliance on oil as well as realizing the “carbon neutral” commitment by 2060.

Market Size

NEV sales value has grown from RMB24.6 billion in 2015 to RMB177.8 billion in 2019 in China, representing a CAGR of 63.9%. China’s NEV market is expected to grow at a CAGR of 37.1% from 2019 to 2025, reaching RMB1,182.9 billion in 2025, according to the CIC Report.

Market Size of New Energy Vehicle Industry in China (2015-2025E)



Source: CIC Report

Key Trends and Drivers

According to the CIC Report, the key trends and drivers of NEV development include:

- **Clear government target on EV penetration rate**

According to the “Energy-Saving and New Energy Vehicle Technology Roadmap 2.0” drafted under the instruction of the Ministry of Industry and Information Technology of the PRC in 2020, it is reaffirmed that the overarching development guideline of EV market is to achieve the goal that every other new car sold is an EV by 2035.

- **Various financial incentives in the form of subsidies and tax exemption**

China is one of the earliest countries in the world to provide financial subsidies for EV purchasers, which demonstrates its government’s strong determination to support the development of the NEV market. According to the “Announcement on Exemption of Vehicle Purchase Tax for NEVs,” from January 1, 2021 to December 31, 2022, new energy vehicles purchased will be exempted from vehicle purchase tax.

- **Continued rollout of charging infrastructure**

Ministry of Industry and Information Technology of the People’s Republic of China issued the “New Energy Vehicle Industry Development Plan (2021-2035),” in which it is estimated that the number of EVs will reach 64.2 million in 2030. According to the government target of achieving 1:1 ratio of charging pile and EV, a significant gap of 63.0 million charging piles needs be filled.

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Overview of the AIoT Market in China

Driven by increased mobile penetration and advancement in AIoT technologies, smart home appliances are rapidly gaining popularity in China, having grown at a CAGR of 27.4% from 2015 to 2019 and is expected to grow at a CAGR of 7.2% from 2019 and 2025, or from approximately RMB162.2 billion to RMB233.2 billion. As a comparison, China’s home appliances market grew at a steadily CAGR of 2.2% from 2015 to 2019 and is expected to grow at a CAGR of 2.0% from 2019 to 2025, or from approximately RMB891.0 billion to RMB1,002.1 billion during the period, according to the CIC Report. While AI-enabled home appliances may operate alone, products from different brands and manufacturers do not share a common operating platform, which can be unnecessarily cumbersome to perform simple tasks. Smart devices, which are powered by smart assistant to allow for conversational AI, may serve as the control center for other home devices, as well as providing AI-enabled services, such as voice search and skills store.

Overview of the Smart Devices Market in China

The smart devices market, including smart speakers without display, smart displays and smart earphones that connect with AI-enabled home appliances, are empowered by AI technologies, such as speech recognition, NLP and computer vision. Smart devices, which primarily interact with users through conversational AI, may offer a wide range of proprietary and third-party content and services through its skills store. Baidu is a leading provider of skills through its DuerOS skills store, because it enables developers to convert their smart mini programs from Baidu App, which draws a large developer community with over half a billion MAUs, into DuerOS skills for smart devices and smart vehicles.

Given the wide range of functionalities that a smart device can offer, such as search, music, video, online game, online literature and e-commerce, the large amount of time one can spend at home, and in the case of smart displays, a larger screen than smart phones, there are many monetization possibilities that smart devices can offer.

Key Trends and Drivers

According to the CIC Report, the key trends and drivers of China’s smart device market include:

- ***Increased penetration of WiFi and IoT***

Lower cost and increased demand for the Internet has made Internet connectivity and smart functions more commonly found in home appliances. As smart appliances increase, a network of smart appliances can formed around smart devices powered by a smart assistant, and the smart assistant that better understands human expression, does search well and provides an abundant functionality stand to benefit.

- ***Advancement in AI technologies***

With AI technologies continue to improve, smart devices will be able to better understand and respond to user needs and expand in functionality. While most smart devices are still limited by their placement and typically require voice activation in close vicinity, Xiaodu smart devices, powered by DuerOS smart assistant, is a leader in leveraging AI capabilities, including speech recognition, NLP and computer vision, by using internally designed Baidu Honghu chips. Consequently, Xiaodu smart

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devices enable far field as well as allowing users to interact more naturally through hand gestures and facial expressions, beyond conversational AI.

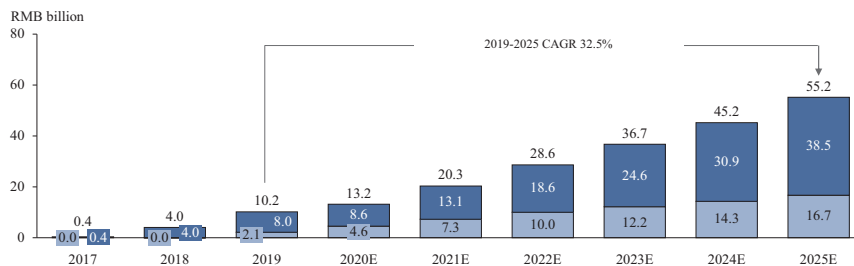
- **Increased adoption of skills store**

With the adoption of skills store from smart devices, online content and services have grown significantly both in terms of genres and volume of offering. Accessibility to content and services may enrich user experience and lead to more monetization opportunities.

Market Size

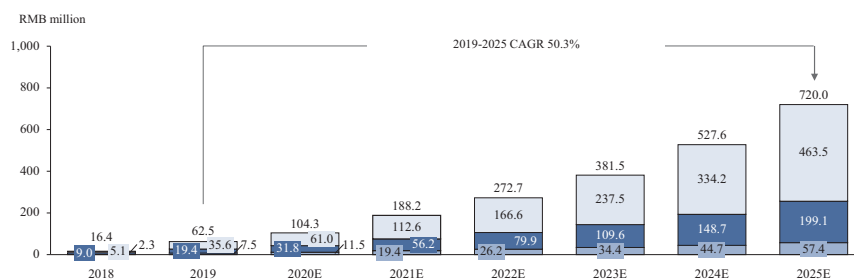
With a total of approximately 59.3 million devices in 2019, China’s smart devices market in terms of hardware revenue is expected to grow at a CAGR of 32.5% from 2019 to 2025, or from RMB10.2 billion to RMB55.2 billion in retail sales during the same period, according to the CIC Report. The non-hardware portion of the market, such as advertisement and content-related services, including paid membership, is expected to experience significant growth as the number of installed devices continues to grow. The charts below present the historical and expected size of the market of hardware and non-hardware revenue of smart devices:

Hardware Revenue of Smart Devices in China (2017-2025E)



Source: CIC Report

Non-Hardware Revenue of Smart Devices in China (2018-2025E)

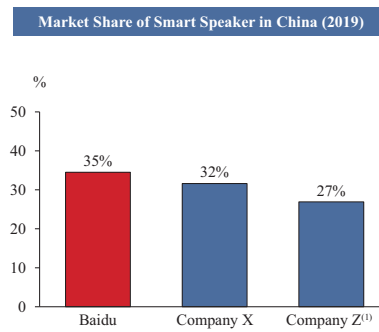
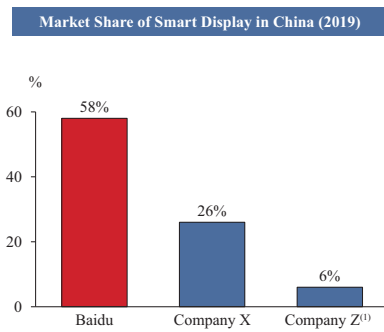


Source: CIC Report

Competitive Landscape

Leveraging its advantage in speech recognition, NLP, computer vision and AI chip design, Baidu has launched a series of Xiaodu-branded smart displays and speakers as well as licensed its DuerOS operating system for smart devices to third-party brands and hardware. The following charts set forth the market share of top smart display and smart speaker providers in China by sales volume in 2019.

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Source: CIC Report

Note:

(1) Company Z is a leading mobile device and IoT company.

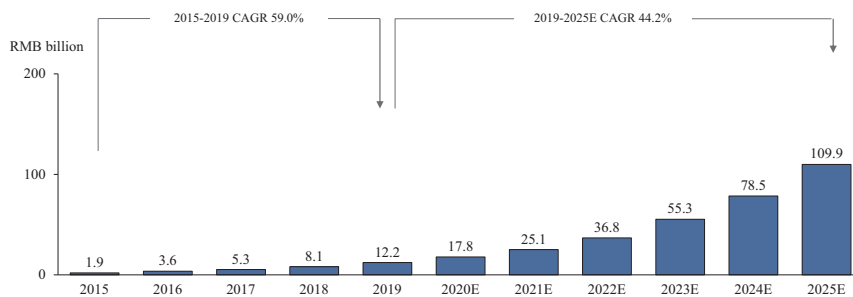
Overview of the AI chip industry in China

AI chip industry is still in the early stage of development in China. The number of AI chip design companies is increasing rapidly, accompanied by the emergence of a number of market leaders. AI chips are mainly applied in areas like cloud computing, data center, edge computing, consumer electronics, smart manufacturing, intelligent driving, intelligent finance and intelligent education.

Market Size

AI chip market has grown from RMB1.9 billion in 2015 to RMB12.2 billion in 2019 in China, representing a CAGR of 59.0%. China's AI chip market is expected to grow at a CAGR of 44.2 % from 2019 to 2025, reaching RMB109.9 billion, according to the CIC Report.

Market Size of AI Chip in China (2015-2025E)



Key Trends and Drivers

According to the CIC Report, the key trends and drivers of AI chip industry include:

- **Support from the Chinese government**

The State Council of the PRC has announced plans to support the development of the AI chip industry from aspects like fiscal and taxation, investment and financing, research and development, import and export, talent development, intellectual property, market applications as well as international cooperation.

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- **Development of the new data economy**

The digital transformation of Chinese companies will bring about increasing demand of AI chips to support efficient handling of massive amounts of data, which will drive fast development and continuous innovation in the AI chip industry.

- **Fast-growing downstream applications**

AI chips have been applied in numerous cutting edge and fast-growing downstream sectors, such as autonomous driving, cloud computing, edge computing, robotics, intelligent manufacturing, “New Infrastructure”, intelligent driving, intelligent finance, intelligent education, and wearable devices. The development in these areas will in turn drive the development of the AI chip industry.

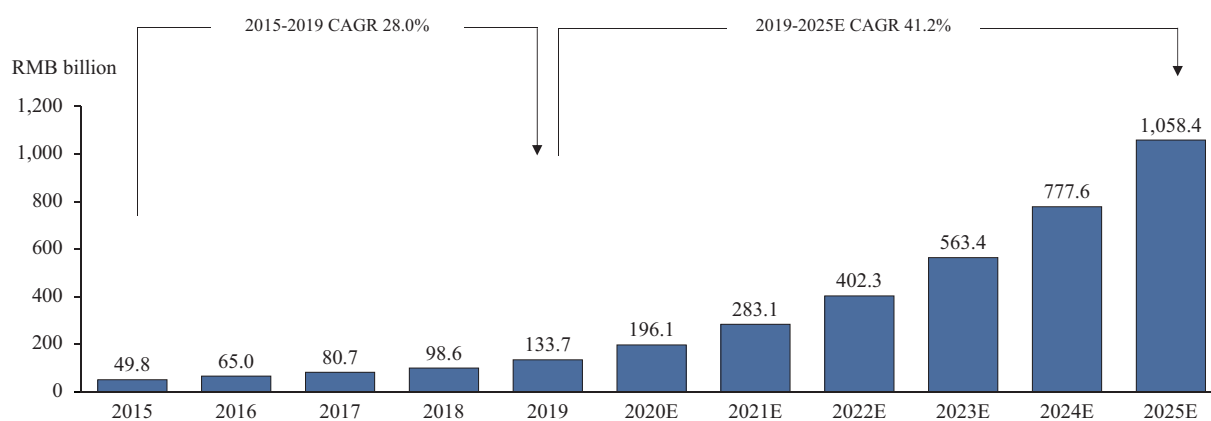
Overview of the Internet healthcare industry in China

China’s Internet healthcare market is in a stage of rapid development. The advancement of digital technology and rapid transformation of traditional hospitals drives the growth of both supply and demand in the Internet healthcare market. The Internet healthcare market mainly consists of digital solutions for hospitals, online consultation and services for patients, online retail pharmacy, healthcare insurance and mobile payment, and digital infrastructure including both hardware and software.

Market Size

The Internet healthcare market has grown from RMB49.8 billion in 2015 to RMB133.7 billion in 2019 in China, representing a CAGR of 28.0%. China’s Internet healthcare market is expected to grow at a CAGR of 41.2% from 2019 to 2025, reaching RMB1,058.4 billion, according to the CIC Report.

Market Size of Internet healthcare in China (2015-2025E)



Source: CIC report

Key Trends and Drivers

According to the CIC Report, the key trends and drivers of the Internet healthcare industry include:

- **Favorable government policies**

The Chinese government has promulgated favorable policies to accelerate the development and penetration of Internet healthcare services. For instance, the government covered Internet healthcare

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expenditures under the government medical insurance and promoted online consultation during covid-19 pandemic.

- ***Advancement of digital technology***

The advancement of digital technology including AI, dig data, and block chain contributes to reducing labor cost of Internet healthcare services, developing customized healthcare services for patients and enhancing mutual trust.

- ***Business expansion to the front line of industry chain***

The growing availability of patient data and importance of health management will incentivize market participants to analyze personal data with digital technology and provide customized health management services for disease prevention.

Overview of Online Entertainment Industry in China

Online entertainment industry in China consists of internet video, live broadcasting, short video, online literature, digital music and recreational internet anime and comic markets. As people spend more time on mobile phones, the market size of China’s online entertainment industry has grown steadily. Online entertainment is popular for the easy access, innovative entertainment formats, customized content and creative flexibility.

Competitive Landscape

iQIYI has developed a diversified monetization model, such as membership services and online advertising, to capture multiple opportunities arising from the rapid growth of the online entertainment industry in China.

The following table presents iQIYI’s average mobile MAU, average mobile DAU and number of paying users, as compared to those of other industry players in China to the extent that information is available, according to the CIC report.

| | Average mobile MAU (in millions) | | Average mobile DAU (in millions) | | Number of Paying Users (in millions) | |
|------------------------------|-------------------------------------|-------|-------------------------------------|-------|---|-----------------------------|
| | 2019 | 2020 | 2019 | 2020 | As of December 31, 2019 | As of September 30, 2020 |
| iQIYI | 557.3 | 549.8 | 113.0 | 107.2 | 106.9 | 104.8 |
| Video Y ⁽¹⁾ | 544.4 | 511.2 | 111.2 | 109.1 | 106.0 | 120.0 |
| Video X ⁽²⁾ | 351.7 | 254.7 | 67.3 | 46.9 | N.A. | N.A. |

Notes:

(1) Video Y is a video platform owned by a leading Internet company, Company Y.

(2) Video X is a video platform acquired by a leading Internet company, Company X.

Source: CIC report

Source of Information

We commissioned CIC to conduct research, provide an analysis of, and to produce the CIC Report on the markets in which we operate. CIC is an independent market research and consulting company that provides industry consulting services, commercial due diligence, and strategic consulting services to both institutional investors and corporations. We incurred a total of RMB650,000 in fees and expenses for the preparation of the CIC Report. CIC undertook both primary and secondary research using a variety of resources. Primary research involved interviewing key industry experts and leading industry participants. Secondary research involved analyzing data from various publicly available data sources,

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including the National Bureau of Statistics of China, Chinese Government releases, annual reports published by relevant industry participants, industry associations, CIC’s own internal database and other relevant sources. CIC’s projection on the size of each of the related markets in China takes into consideration various factors, including (i) that the overall global social, economic, and political environment is expected to maintain a stable trend over the next decade; (ii) that related key industry drivers are likely to continue driving growth in the aforementioned markets during the forecast period, including steady economic growth, fast growing data volume, large amount of investment in AI, and supporting policies and regulations; and, (iii) that there is no extreme force majeure or industry regulations by which the market situation may be affected either dramatically or fundamentally.

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Overview

Our mission is to make the complicated world simpler through technology.

We are a leading AI company with a strong Internet foundation. We have been investing in AI since 2010, to improve search and ad monetization, and have used “Baidu Brain,” our core AI technology engine to develop new AI businesses. The breadth and depth of our AI capabilities provide the differentiating foundational technologies that power all of our businesses. According to the CIC Report, our AI leadership in China is evidenced in the following aspects:

- We hold the largest portfolio of AI patents and AI patent applications in China as of October 30, 2020;
- Our deep learning framework, PaddlePaddle, is the No. 1 deep learning framework in China and No. 2 globally behind Facebook Pytorch in terms of cumulative pull requests as of December 31, 2020;
- Our Baidu Open AI Platform, with a developer community of over 2.65 million members, is the largest open AI platform in China, based on the number of developers as of December 31, 2020; and
- Baidu OSChina, which runs on Baidu cloud infrastructure, is the largest development platform for open source activities of in China and No. 3 globally (behind GitHub and Gitlab), in terms of the number of developers as of December 31, 2020.

We are one of the very few companies that offers a full AI stack, encompassing an infrastructure consists of AI chips, deep learning framework, core AI capabilities, such as natural language processing, knowledge graph, speech recognition, computer vision and augmented reality, as well as an open AI platform to facilitate wide application and usage. Our technological innovation in AI has been well recognized by the global community. For instance, ERNIE, our natural language processing framework, became the first AI model to score above 90 on GLUE (General Language Understanding Evaluation), which is widely considered as the benchmark for testing AI language understanding, and won the SAIL (Super AI Leader) award, the highest honorary recognition at the 2020 World Artificial Intelligence Conference. We have put our leading AI into innovative use. For example, we are the first to receive driverless licenses in China and the U.S. and we are testing driverless vehicles in China.

Baidu was founded as a search engine business in 2000 with the belief that technology can change the way people discover and consume information. At the heart of Baidu search is its ability to better understand a users’ search queries and to answer these queries by matching the most relevant information in ranked search results. To achieve this, we continuously innovate and develop new technologies and products that enhance Baidu search user experience. We began to use AI a decade ago to power these technologies in order to better match user search intent with the large amount of information on the Internet. For instance, our natural language processing, an AI capability, enables the understanding of important details of a query, particularly in complex conversational queries. This helps optimize search results returned and increase the satisfaction rate of users. Years of tagging, understanding and intelligently processing all forms of content on the Internet—text, images and videos—with AI has helped us develop Baidu Brain, our core AI technology engine, which in turn has enabled us to further develop leading AI technologies and commercialize them through products and services for consumers, enterprises and the public sector. Our ability to continuously invest heavily in research and development is made possible by the durable revenue that we generated as a leading Internet platform.

The widespread usage of our open AI platform by developers and businesses creates a network effect for our AI technologies, products and services. The more developers and businesses use our AI

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models, tool kits and services, the better our AI capabilities become, which in turn further increase the attractiveness of our AI platform to developers and business communities. This network effect helps us obtain unique insights into different kinds of products and services that are in demand and have real-world application across different industries, setting a strong foundation for us to make investment decisions and lead with technology, products and services in the markets that we have entered.

Our large portfolio of products and services is accessed by over one billion devices monthly, and our business spans across an ecosystem of hundreds of millions of users, millions of developers and hundreds of thousands of enterprises. Our usage of a strong technology foundation to support an open platform business model not only draws more participants into our ecosystem, but also adds richness and vibrancy to our ecosystem, strengthening the long-term prospect and vitality of our business overall.

We usually start the development of a business with a strong technology platform, on which we build products and services for our customers and users, and through an open platform architecture, we attract a wide array of partners to our ecosystem to expand the offerings to our customers and users. The platform could then grow organically and by leveraging the power of our partners in the ecosystem, which over time feed into a virtuous cycle.

Over the past two decades, we have demonstrated a track record for long-term growth and strong profitability, which has enabled us to invest in a diversified portfolio of products and services with large market opportunities and further improve our long-term growth prospects. Through years of investment in research, AI chip design, developer community, patents and talent development, we are turning AI into innovative use cases. Powered by AI, Baidu Core, which excludes iQIYI and contributed over 70% of our total revenues during the Track Record Period, mainly provides search-based, feed-based, and other online marketing services, as well as products and services from new AI initiatives in the following three growth engines:

- *Mobile Ecosystem*: a portfolio of over one dozen apps, including Baidu App, Haokan and Baidu Post, which provides an open platform that aggregates a wide range of third-party, long-tail content and services through our AI building blocks and which helps communities connect and share knowledge and information;
- *AI Cloud*: a full suite of cloud services and solutions, including PaaS, SaaS and IaaS and uniquely differentiated by our AI solutions; and
- *Intelligent Driving & Other Growth Initiatives (OGI)*: our growth initiatives include intelligent driving (self-driving services, including HD Maps, automated valet parking and autonomous navigation pilot, intelligent electric vehicles and robotaxi fleets), as well as Xiaodu smart devices powered by DuerOS smart assistant and AI chip development.

At the core of our Mobile Ecosystem is Baidu App, which is the No. 1 search-plus-feed app in China with an MAU of 544 million in December 2020. Unlike most mobile apps, which direct traffic to a closed content ecosystem, Baidu App, through our AI building blocks, aggregates content and services from third-party apps and websites, and directs traffic to third-party content and service providers with native-app like experience. Under an open-platform model, Baidu App can continue to grow our huge offering of third-party content and services, by leveraging our network partners of BJH Accounts, Smart Mini Program and Managed Page. Our decade-long experience with AI and the development of

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a powerful knowledge graph allow us to match user intent with long-tail, third-party content and services on our open platform.

Our Mobile Ecosystem also includes a portfolio of over one dozen apps, including Haokan and Baidu Post, providing a platform for people to discover and consume information through search and feed, interact and engage with creators, publishers, service providers and merchants. This native-app like experience from user acquisition to user relationship management to closed loop transactions demonstrates our value to merchants, enabling them to perform user life-time management on our platform, and has made Baidu App a leading online marketing services provider for both search and feed. Within our Mobile Ecosystem, we serve half-a-million customers by enabling them to tap into our massive user base. We monetize primarily through offering comprehensive and effective marketing services to fulfill our customers’ needs. We generate revenue primarily from providing search, feed and other marketing services, which account for a majority of our total revenues during the Track Record Period. We have made extensive use of AI technologies to develop innovative marketing services, such as dynamic ads, which recommends products from our marketing customers most fitting to each search user. Our marketing cloud also provides innovative AI capabilities to our marketing customers, so that users can still make product inquiries during non-business hours and Baidu Brain can automatically carry a conversation with users to facilitate transactions. In addition, the user engagement and user logins that have developed on our platform are enabling us to diversify monetization beyond online marketing into other services, such as live broadcasting, online games and membership.

Our AI Cloud is the leading AI public cloud service provider and a top four public cloud service provider in China in 2019, according to the CIC Report. Our AI Cloud offers a full suite of cloud services and solutions, including PaaS, SaaS and IaaS, and is differentiated with our AI solutions. Leveraging Baidu Brain, our AI solutions provide customers and developers with a comprehensive library of modularized solutions, including open source codes, pre-trained models, end-to-end development kits, tools and components. In addition, our AI Cloud customers can leverage our large library of key AI capabilities, such as knowledge graph, speech recognition and synthesis, natural language processing and computer vision. Our products and services, such as EasyDL and Baidu ML, make it easier for customers to use deep learning and machine learning to solve real world problems, and our cloud services are formulated to serve across different industries, including Internet, media, telecom, financial services, transportation and logistics, education and manufacturing.

Our Intelligent Driving & OGI consist of promising businesses in development with huge market opportunities, and some are at early-stage commercialization with a growing customer base. We are a market leader in intelligent driving and smart devices, and we are pursuing these large growth opportunities by leveraging our unique AI capabilities, data insights and internally developed chips. For example, in autonomous driving, Apollo is the market leader in China with 4.3 million accumulated test miles and 199 autonomous driving licenses across China, as of December 31, 2020. Our 199 autonomous driving licenses reflect the geographic reach of Apollo testing scenarios in China, compared to the second player with approximately 20 licenses. There are currently three Apollo robotaxi pilot programs running in China.

Our strong brand and market leadership in autonomous driving has carried over to intelligent driving. Apollo is a well-recognized brand among automakers. We have signed strategic agreements with 10 leading automakers to power their passenger vehicles with Apollo Self Driving services, which includes Baidu high definition (HD) Maps and automated valet parking (AVP), and we recently announced the availability of Apollo autonomous navigation pilot (ANP). Under smart display, Xiaodu was ranked No. 1 in shipments globally for 2019. We also develop AI chips internally customized for

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Baidu Brain and specific AI usages to improve performance and costs. We believe these initiatives will strengthen our revenue drivers for long-term growth.

iQIYI produces, aggregates and distributes a wide variety of professionally produced content, as well as a broad spectrum of other entertainment-oriented video content.

We believe we have built a large and strong portfolio of products and services to give Baidu the scale necessary to invest heavily in technology, while optimizing our future for sustainable long-term growth. We derive significant synergies by incorporating the AI developed for search into other parts of our business. For example, large daily use of our visual search and voice search may be used to improve Apollo computer vision and DuerOS speech recognition capabilities.

We generated total revenues of RMB102.3 billion, RMB107.4 billion and RMB107.1 billion (US\$16.4 billion) in 2018, 2019 and 2020, respectively. Our revenue in 2020 was impacted by the COVID-19 pandemic, and we experienced revenue change of -7%, -1%, +1% and +5% year over year for the three months ended March 31, June 30, September 30 and December 31, 2020, respectively. We generated net income attributable to Baidu, Inc. of RMB27.6 billion, RMB2.1 billion and RMB22.5 billion (US\$3.4 billion) in 2018, 2019 and 2020, respectively. Net income attributed to Baidu, Inc. in 2019 included a non-cash impairment loss of RMB8.9 billion from investment in Trip.com.

Baidu Core generated revenues of RMB78.3 billion, RMB79.7 billion and RMB78.7 billion (US\$12.1 billion) in 2018, 2019 and 2020, respectively. Baidu Core’s revenue in 2020 was impacted by the COVID-19 pandemic, and Baidu Core experienced revenue change of -13%, -3%, +2% and +6% year over year for the three months ended March 31, June 30, September 30 and December 31, 2020, respectively. We generated net income attributable to Baidu Core of RMB33.6 billion, RMB7.6 billion and RMB26.5 billion (US\$4.1 billion) in 2018, 2019 and 2020, respectively. Net income attributed to Baidu Core in 2019 included a non-cash impairment loss of RMB8.9 billion from investment in Trip.com.

iQIYI generated revenues of RMB25.0 billion, RMB29.0 billion and RMB29.7 billion (US\$4.6 billion) in 2018, 2019 and 2020, respectively. We generated net loss attributable to iQIYI of RMB9.1 billion, RMB10.3 billion and RMB7.0 billion (US\$1.1 billion) in 2018, 2019 and 2020, respectively.

Key Financial and Operating Metrics

Baidu Core

| | For the Month Ended December 31, | | |
|--|-------------------------------------|--------|--------|
| | 2018 | 2019 | 2020 |
| MAU of Baidu App (in millions) | 435 | 500 | 544 |
| DAU of Baidu App (in millions) | 161 | 195 | 202 |
| | For the Year Ended December 31, | | |
| | 2018 | 2019 | 2020 |
| Revenue (RMB in millions) | 78,271 | 79,711 | 78,684 |
| Operating profit (RMB in millions) | 23,808 | 15,261 | 20,538 |

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iQIYI

| | As of December 31, | | |
|---|------------------------------------|---------|---------|
| | 2018 | 2019 | 2020 |
| Subscribing Members (in millions) | 87.4 | 106.9 | 101.7 |
| | For the Year Ended December 31, | | |
| | 2018 | 2019 | 2020 |
| Revenue (RMB in millions) | 24,989 | 28,994 | 29,707 |
| Operating loss (RMB in millions) | (8,306) | (9,258) | (6,041) |

Our Strengths

We believe the following competitive strengths contribute to our success and set us apart from our peers:

Leading technology company with world-class AI capabilities

We have been investing heavily in AI for over a decade, building on an innovation driven company culture, which has enabled us to achieve our leadership position.

Our unique breadth and depth of AI capabilities provide the differentiating technology foundation that powers all of our business areas. We have made our leading AI technologies open to developers and partners alike, to empower their businesses with AI and in turn increase the scale and vitality of our developer community to help improve our products and services. Our AI capabilities encapsulated on Baidu Brain, our core AI technology engine, consists of four layers—foundation, perception, cognition and platform, as well as a security module that ensures security, safety and privacy.

The comprehensive technology stacks of Baidu Brain and our leading AI capabilities have made us the leader in China across multiple dimensions, according to the CIC Report:

Leading Technology

- **Baidu** holds the largest number of AI patents and AI patent applications in China as of October 30, 2020;
- **PaddlePaddle** is the No. 1 deep learning framework among Chinese companies and No. 2 globally in terms of pull requests, as measured by GitHub as of December 31, 2020;

Leading Developer Communities

- **Baidu Open AI Platform** has the largest AI developer community in China, as of December 31, 2020;
- **OSChina** is the largest development platform for open source activities among Chinese companies and No. 3 globally, in terms of number of developers as of December 31, 2020;

Leading Products and Services

- **Baidu App** is the largest search-plus-feed app in China, in terms of MAUs and DAUs in December 2020;
- **Our AI Cloud** is the largest AI public cloud services provider in China, in terms of revenue, product portfolio and APIs used by developers in 2019;
- **Apollo** is the market leader in autonomous driving in China, in terms of accumulated test miles and the number of licenses received; and
- **Xiaodu Smart Display** ranked No. 1 in smart display shipments globally in 2019.

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Mobile Ecosystem: China’s leading content and services discovery ecosystem

Our Mobile Ecosystem serves hundreds of millions of users, millions of content and services providers and hundreds of thousands of businesses, in an ecosystem built upon Baidu App as well as a dozen other apps. In addition to a wide range of third-party content and services offered on our platform, our knowledge-and-information-centric ecosystem is distinguished with other internally developed and well recognized products, such as Baidu Wiki, Baidu Knows and Baidu Post.

As the world’s largest Chinese-based search engine, we have used AI to best meet user intent by learning about the strong correlation between search key words and our search results. Such valuable intent insight coupled with our extensive processing and indexing of the massive amount of information on the Internet has helped us create a huge knowledge graph to improve user experience. Leveraging our deep understanding of users, we added feed to Baidu App in 2016, which has helped Baidu App to become the largest search-plus-feed app in China, with 544 million MAUs in December 2020. Our deep understanding of users is further strengthened with the introduction of AI building blocks—Baijiahao (BJH) Accounts, Smart Mini Program and Managed Page.

Our AI building blocks has attracted a wide range of content and services dispersed across isolated mobile apps and websites onto our platform, so as to tap into our over- half-a-billion user base.

- BJH accounts allow creators and publishers to share their social content in an openly searchable manner, rather than having to maintain multiple social accounts on over one dozen prominent social media and timeline products in China to be easily discoverable.
- Smart Mini Program enables content and services from third-party mobile apps to be searchable and accessible within Baidu App and other apps powered by our AI building blocks without requiring users to separately download each app.
- Managed Page provides hosted solution to website owners, where they could maintain a web presence without having to pay for and maintain website infrastructure, such as servers, software and bandwidth.

In addition to the wide range of third-party content and services on our platform, we complement our Mobile Ecosystem with a large portfolio of internally developed products, to fill a void in China’s online content and services space. We have dedicated tremendous resources to and spent years on building a large portfolio of user generated content (UGC) products sharing knowledge and experience, such as Baidu Wiki, Baidu Knows, Baidu Experience, and Baidu Post. The depth and breadth of our UGC knowledge and experience library is evidenced by the numerous content pieces covering trending topics and long-tail content. Consequently, people come to know Baidu as a leading knowledge-and-information centric platform based on our wide range of third-party content and services and internally developed UGC products .

We offer merchants a marketing cloud platform, which provides CRM capabilities to help them manage and optimize the lifetime value of their customers. Together with the huge traffic and user engagement on our platform, our CRM capabilities create monetization opportunities beyond advertising. For example, merchants may add a live link to their call center as a functionality in their advertisements, and our AI-powered marketing cloud can provide automated management reports on the quality of interaction between their call center and potential customers. By understanding the type of users who are more likely to move from the search landing page to purchase, merchants can buy more effective traffic leveraging the insights of our marketing cloud platform.

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AI Cloud: China’s leading AI cloud service provider

According to the CIC Report, our AI Cloud is the largest AI public cloud services provider and a top four public cloud service provider in China in 2019. Baidu Core’s cloud services revenue reached RMB9.2 billion (US\$1.4 billion) in 2020, increasing by 44% from 2019.

Our AI Cloud offers a comprehensive set of cloud solutions, including IaaS, PaaS and SaaS, differentiated by the following:

- *AI PaaS powering AI solutions, including knowledge graph cloud solutions*

We provide enterprise customers with cloud solutions that leverage the unique AI capabilities from Baidu Brain. For example, an AI PaaS may be installed with specific applications and AI capabilities, such as optical character recognition (OCR) and computer vision, and trained to perform certain tasks, such as simplifying receipt collection and storage for expense reporting, verifying employee identification and attendance through a facial scanner installed at elevator terminal gate, or automating the quality assurance checkpoints of an electronic component assembly line with IoT scanners that record QA testing results.

Leveraging the proprietary knowledge graph that we have built from handling large volume of information on the Internet for the last two decades, we provide differentiated knowledge-graph cloud solutions built on our AI PaaS for specific applications using pre-trained models. Knowledge-graph cloud solutions are particularly applicable when the enterprise customer has a large amount of data that requires a sophisticated knowledge graph to enable AI-powered decision support. For example, a utility company used our knowledge-graph cloud solution to determine the electricity capacity needed to supply a region deploying EV charging stations; a retail bank used our knowledge-graph cloud solution to improve credit risk management for lending to consumers and small and medium-sized businesses; and a large enterprise used our knowledge-graph cloud solution to recommend relevant documents to its employees to support the write up of daily and weekly management reports.

- *AI solutions setting industry standards and product standards across different industries*

Our AI solutions have become standard setting in key industry verticals. For example, in the smart transportation industry, we are a pioneer and industry leader in developing vehicle-to-everything (V2X) road infrastructure. We have won smart transportation projects in over one dozen cities, including Beijing, Shanghai, Chongqing and Guangzhou, to help modern cities improve their traffic condition, road safety and air quality with AI technology. Our V2X road infrastructure also serves as an intelligent vehicle-road coordination platform. For example, it provides intelligent vehicles (self-driving services, intelligent EVs, robotaxis and connected vehicles) information of surrounding traffic and road condition, and, thus, defines the standards for traffic-related applications, which in turn drive industry adoption.

We also offer Mobility-as-a-Service (MaaS), which allows the public sector to offer autonomous driving public transportation, including Apollo robotaxi, robobus and third-party fleets, which users can order from Baidu App or Baidu Maps. Apollo MaaS is also compatible with other in-vehicle smart devices, such as DuerOS smart rear-view mirrors. Apollo MaaS also helps municipal traffic authorities monitor and prioritizes public transportation connected to our platform.

Our cloud solutions also set product standards for common usage across different industries. For example, a major telecom operator installed our automated call center solution powered by Baidu Brain two years ago to handle millions of calls per month, reducing the average call time per customer

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by 40%. The telecom operator has since rolled out our automated call center solution to several other call centers nationwide, and our automated call center solution has since been adopted by enterprise customers across eight different industries.

- *Comprehensive suite of products and services combined with effective cross-selling*

Our AI Cloud also offers a full line of services, including CDN and IaaS for computing, storage, network, database and delivery services. Combined with our effective marketing capabilities, we have been able to demonstrate the ability to cross-sell and up-sell additional products and services to existing customers, which in turn enables us to more efficiently grow our cloud business. For example, a major financial services enterprise customer recently purchased its fifth AI cloud solution from us after its initial purchase of our automated call center solution.

Intelligent Driving & Other Growth Initiatives: Strong leadership in large AI-powered markets

In addition to our Mobile Ecosystem and AI Cloud, we are investing in large growth opportunities that we believe our leading AI capabilities and technology foundation would give us a distinct strategic advantage. Our growth initiatives include intelligent driving, Xiaodu smart devices powered by DuerOS smart assistant, Baidu Health and AI chips.

Intelligent Driving. Intelligent driving, including self-driving services, intelligent EVs and robotaxi fleets, leverages AI and other technologies to make a vehicle, or fleet of vehicles, more intelligent, all with the ultimate goal to be autonomous. Apollo is the market leader in autonomous driving in China, in terms of accumulated test miles and the number of test licenses received. In addition, the services and solutions of intelligent driving are made compatible with other platforms and solutions supporting our smart transportation, which leverages each other to gain a better understanding of traffic and road conditions, as well as to improve cost efficiency. Our leadership in autonomous driving, industry know-how, operating experience, transportation ecosystem understanding (from our platforms and maps), and cost advantage give us strong competitive advantages in leading the development of the intelligent driving industry.

- *Apollo Self Driving.* We have been investing in L3 and L4 self-driving technology to power passenger vehicles. Our self-driving services include, HD Maps, a critical component for L3 and L4 self-driving. In 2018, we introduced automated valet parking (AVP) which allows a driver to get out of the vehicle upon destination arrival and our L4 service would enable the vehicle to autopark, as well as pick up the driver from the self-parked parking lot. In 2020, we introduced Apollo autonomous navigation pilot (ANP), a system powered by Apollo’s computer vision-based autonomous driving technology and tailored for urban road conditions in China, enabling the automatic guidance of the vehicle to follow navigation route on highway, freeway and urban roads. Self-driving services have a high barrier to entry. For example, we are one of the very few companies in China to offer HD Maps. Apollo AVP and ANP services are based on years of heavy investment in autonomous driving, leveraging our knowledge from our massive accumulated test miles and simulated miles, as well as the know-how gathered from our HD Maps. We have signed strategic agreements with 10 leading automakers to install Apollo self-driving services, as of December 2020 .
- *Intelligent Electric Vehicles.* We recently formed a company to offer intelligent EVs, leveraging our knowhow and experience in autonomous driving, intelligent driving and smart transportation. We believe the best use of AI is when an EV is designed with consideration of software and hardware integration in mind. We have entered into a strategic partnership with multinational auto manufacturer Zhejiang Geely Holding Group (Geely) to produce intelligent EVs. Geely, which

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holds the distinction of best-selling Chinese automobile brand in past years, under the Volvo and Geely brands, will contribute its expertise in automobile design and manufacturing.

- *Apollo Robotaxi.* Robotaxi fleet operation represents a massive opportunity, and we currently have three Apollo Go Robotaxi test pilot programs in operations, in cooperation with Beijing, Changsha and Cangzhou. Apollo is the market leader in China with 4.3 million accumulated test miles and 199 autonomous driving licenses across China, as of December 31, 2020. Our 199 autonomous driving licenses reflect the geographic reach of Apollo testing scenarios in China, compared to the second player with approximately 20 licenses. Based on accumulated test miles and the number of autonomous driving licenses received, Apollo is the undisputed market leader in autonomous driving in China. Apollo Robotaxi is also unique in that it leverages the data from Apollo V2X road infrastructure and Baidu Maps, to obtain a better understanding of surrounding traffic and road conditions and a strategic cost advantage.

DuerOS Smart Assistant. Our smart assistant and smart devices have a large and engaged user base. DuerOS is the leading smart assistant in the Chinese language, powering first-party Xiaodu smart devices (smart displays, smart speakers and smart earphones), as well as third-party smart devices (smart phones, children smart watches and story machines). Xiaodu Smart Display ranked No. 1 in smart display shipments globally and Xiaodu smart speakers ranked No. 1 in smart speaker shipments in China for 2019, according to the CIC Report. The average daily activated time span per device for Xiaodu Smart Display was over 3 hours in 2020. Time spent on Xiaodu devices is contributed by the robust offering of the DuerOS skills store, which has over 4,400 skills in wide ranging genres, such as education, video, online game and live streaming, and a developer community of over 47,000. In the fourth quarter of 2020, we raised financing for the Smart Living Group, which develops DuerOS smart assistant, sells Xiaodu smart devices and licenses DuerOS to third-party smart device makers, at a post-money valuation of US\$2.9 billion, and we remain as a super majority shareholder.

Platform-centric model cultivating vibrant ecosystems and capturing huge market opportunities.

Our platform-centric business model focuses on providing a strong technology foundation to attract and support a vibrant ecosystem of customers, users and partners. We start with the development of a strong technology infrastructure using our leading technology, and then add products and services that could be used by our customers, users and partners, as building blocks across multiple use cases, to build a platform. The platform could then grow organically and with partners in the ecosystem adding their products and services, which over time support and drive the long-term growth of our business, as illustrated by the following examples:

- Our Mobile Ecosystem brings together a huge amount of users, creators, publishers, service providers, and merchants on our platform through our AI building blocks—BJH accounts, Smart Mini Program and Managed Page. Creators, publishers and service providers may choose to grow their distinct user bases and communities on any of our family of apps, such as Baidu App, Haokan and Baidu Post, based on their preference of targeted audience. By pooling the massive traffic and consolidating the content and services across our large collection of apps onto one platform, we are able to support a much larger content and services network, which makes our ecosystem more comprehensive and vibrant, and differentiates us from standalone apps.
- By building compatible products and services across smart transportation and intelligent driving, our intelligent driving solutions can utilize Apollo’s unique vehicle-road coordination system and HD Maps to improve a vehicle’s understanding of the surrounding traffic and road conditions, which reduces the hardware needs of intelligent vehicles. The increase in surrounding traffic and road condition understanding and the optimization of cost structure of our intelligent driving

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solutions significantly improve our product performance and commercialization potential. Our leadership in autonomous driving, industry know-how, operating experience, transportation ecosystem understanding (from platforms to maps), and cost advantage give us strong competitive advantages in driving the development of the intelligent driving industry, which also strengthens our position in smart transportation.

- DuerOS for Auto is a smart assistant that powers auto infotainment systems and can be operated with conversational AI. DuerOS for Auto has been installed in over one million new vehicles in 2020. Our platform-centric approach enables the developers of our Smart Mini Program and DuerOS skills to easily convert their applets for the DuerOS for Auto skills store. Such versatility in our technology infrastructure is quite powerful, to enable DuerOS for Auto to leverage the developer resources for the largest search and feed app in China and the largest Chinese-language smart assistant. Our platform model draws strong synergy across the mobile, smart device and auto infotainment markets, not only pooling together our vibrant developer communities across these markets but also allowing our users in the home and auto environment to enjoy familiarity with apps in the mobile environment.

| | Businesses | TAM in 2025 (RMB billion) | CAGR (2019-2025E) |
|------------------------------------|--|------------------------------|----------------------|
| Online Marketing | Knowledge and information-centric Internet platforms | 342 | 12.0% |
| Non-marketing (excluding Robotaxi) | Internet Services | 751 | 23.2% |
| | Cloud services | 577 | 37.2% |
| | Self Driving Services & Intelligent EVs | 1,582 | 43.6% |
| | Smart Devices | 56 | 32.7% |
| | AI Chips | 110 | 44.2% |
| | Internet Health | 1,058 | 41.2% |
| | Non-marketing subtotal (excluding Robotaxi) | 4,134 | 36.5% |
| Robotaxi | Robotaxi | 1,458 | N/A |

The total addressable markets (TAM) for knowledge and information-centric Internet platforms and our non-advertising business (excluding Robotaxi) in China are estimated at RMB342 billion and RMB4,134 billion in 2025, respectively, representing a CAGR of 12.0% and 36.5% between 2019 and 2025, respectively, according to the CIC Report.

The total addressable market of Robotaxi (assuming equivalent to the combined markets of taxi, ride-sharing and rental car) in China is estimated at RMB1,458 billion in 2025, according to the CIC Report.

Strong synergies across our AI-powered markets and offerings

Baidu Brain is the underlying AI technology engine that enables us to serve different markets with AI-powered offerings, including consumer Internet, cloud services, intelligent driving, smart assistant and AI chips. Our total revenue was RMB 107.1 billion (US\$16.4 billion) for the year ended December 31, 2020, and we invested RMB19.5 billion (US\$3.0 billion), representing 18% of our total revenues, into research and development over the same period. Baidu Core revenue was RMB78.7 billion (US\$12.1 billion) for the year ended December 31, 2020, and we invested RMB16.8 billion (US\$2.6 billion), representing 21% of our total Baidu Core revenues, into research and development over the same

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period. Our investment in technology is among the highest in the high-tech industry, as a percentage of sales. By aligning our business around AI, we are able to pool the resources and funding from all of our businesses to support the heavy investment needed to support AI research, including large AI research labs, a huge network of servers, self-designed AI chips, intellectual property patents and a large developer community.

Our AI capabilities were initially developed from our years of analyzing and understanding of information on the Internet. We open up our AI capabilities to the developer community to further improve our models. We also draw synergy from our products, such as visual search and voice search, which serve as reinforcements to further improve our understanding of photos and speech, respectively. Beyond search, products such as autonomous driving solutions help us improve computer vision, while products like Baidu Maps, Baidu IME (mobile keyboard) and DuerOS help us improve our understanding of speech and natural language. By operating in different markets, we not only enable the AI capabilities we build from the search environment to be used in other markets, we are also able to enhance our AI capabilities based on the learnings in other usage scenarios and contribute back to the overall AI capabilities of Baidu Brain.

We have a strategic advantage in the markets that we serve. Not only are we able to leverage our leading AI capabilities in our product and services offerings, we are able to draw upon the synergies we derive from investing in AI infrastructure and the reinforcement from our large portfolio of AI products and services.

Our focus on AI-powered markets makes us a formidable player in each of the markets that we serve, especially if our peers in these markets do not serve the wide range of AI-powered markets that we do.

Management team with decades-long proven track record of technology innovation and commercialization

We benefit significantly from our visionary and experienced management team. Combining solid technology background with in-depth understanding of the industry, together with extensive management experience, our management team is relentlessly pursuing innovative solutions to bring greater value to our users and customers. Robin Yanhong Li, our co-founder and chief executive officer, has been widely recognized as a pioneer and leading figure in China’s internet industry. In 2018, he was named as “the Innovator” by Time Magazine China. Each of Mr. Li and our chief financial officer Herman Yu has over 15 years of experience leading publicly listed companies.

Dr. Haifeng Wang, our chief technology officer, Dr. Dou Shen, our executive vice president, and Dr. Gong Yu, founder and chief executive officer of iQIYI, are reputed technologists and product managers, highly respected in our field with strong track records. Dr. Wang, with close to 30 years of research and development experience, is the president of National Engineering Laboratory for Deep Learning Technology and Applications. Dr. Wang was a fellow and former president of the Association for Computational Linguistics (ACL) and the founding chair of ACL’s Asia-Pacific chapter. Dr. Shen has served in various management roles at Baidu, including web search, display advertising and the financial services group. Prior to joining Baidu, Dr. Shen worked in the adCenter group at Microsoft and was a co-founder of Buzzlabs, a social media monitoring and analysis platform company. Prior to founding iQIYI, Dr. Gong was the president and chief operating officer of umessage.com, a top mobile internet services solution provider in China. Prior to that, Dr. Gong served in the roles of vice president, senior vice president, and chief operating officer at Sohu.com (Nasdaq: SOHU), a Nasdaq-listed company, from 2003 to 2008.

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Our Strategies

We intend to pursue the following strategies to further grow our business:

Continue to invest in technology

We aim to further strengthen our leadership in technology by continuing to invest in research and development focusing on the following areas:

- *AI computing and AI technologies:* We plan to further invest in AI computing and the development of AI technologies to solidify our leading position in the markets that we serve;
- *AI chips:* We plan to optimize existing AI chips and develop next generation chips to further improve the operating performance of Baidu Brain and the competitiveness of our products in the marketplace, such as DuerOS smart devices and infotainment for autos; and
- *Other technologies:* We will continue to invest in cutting-edge technologies, such as blockchain, edge computing, quantum computing and biological computing, which is key to our long-term success as a leading technology company.

Continue to scale our AI Cloud

We will further grow our AI Cloud through commercialization in various industry verticals by offering more value to existing customers and investing in new customer acquisition. We plan to penetrate deeper in the core verticals that we have entered into, by building on our relationship with existing customers, enhancing our comprehensive cloud offerings and delivering tangible value to our customers. We intend to expand and better tailor our AI solutions to cover more verticals with strong growth potential. We will focus on capturing the massive demand from traditional enterprises and public sector organizations with the growth of the cloud market in China. In addition, we also plan to capture potential cross-selling opportunities, leveraging our existing massive marketing customer base. In particular, we will focus on solidifying our leadership position and continue to expand in the smart transportation area, which has huge monetization potential benefiting from the *New Infrastructure Initiative* in China.

Further develop and commercialize intelligent driving and other growth initiatives

We intend to continue improving and promoting the adoption of intelligent driving by continuously improving our products and services offerings and expanding our strategic partnerships with auto makers and the public sector. We plan to further develop and commercialize Apollo Self Driving services. We have partnered with Geely to produce EVs, hoping to leverage our know-how and capabilities in autonomous driving, intelligent driving and smart transportation. We also plan to further expand the scale and coverage of Apollo autonomous driving testing and to work with the public sector to operate robotaxi in more cities across China. We believe our efforts invested in self-driving, intelligent EV and robotaxi have huge long-term monetization potential.

On DuerOS smart assistant, we will focus on increasing its installed base on Xiaodu smart devices as well as on third-party smart devices. We will also continue to grow the offering in the DuerOS store by working closely with existing and attracting new developers. We will continue to invest in Baidu Honghu AI chip to further improve the performance and economics of Xiaodu smart devices. We aim to unlock monetization potential from value-added services on Xiaodu smart devices, especially from membership, skills store revenue share and marketing services.

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We will continue to explore new and innovative application and monetization opportunities leveraging our AI technologies.

Continue to grow our Mobile Ecosystem

We will continue to attract and retain users through the diversified and high-quality offerings of information and services on our platform, to penetrate into broader user groups through multiple channels such as pre-installation of our apps, in particular Baidu App, with OEMs.

We plan to continue to pursue our in-app strategy to enhance user engagement and build a more robust closed-loop content and services ecosystem, including the extension from information to social to purchase. We intend to further enrich our platform with content and services by optimizing our AI building blocks and marketing cloud, in order to attract more third-party content and services providers, as well as users, to our mobile ecosystem. We also plan to offer content in increasingly diversified formats, such as video and live streaming, leveraging our resources from iQIYI and potentially from YY Live.

Furthermore, we intend to strengthen our vertical and community offerings to provide superior experience to users, merchants and content providers. For example, we plan to further develop our online healthcare platform by improving telemedicine and developing other online healthcare services, to expand our content and service offering to our users.

We will continue to improve the effectiveness of our online marketing services with our AI technology, and plan to further diversify monetization channels and generate revenue from non-marketing services, such as e-commerce, online games, live broadcasting and membership.

Selectively pursue M&A and strategic investment

To complement our organic growth, we plan to selectively pursue suitable strategic partnerships, investments, alliances and acquisitions. While keeping our disciplined investment philosophy in mind, we intend to explore opportunities that are complementary to our growth strategies, particularly opportunities that would allow us to strengthen our mobile ecosystem and new AI initiatives, and to expand our user base. We also intend to focus on partnerships, investments, alliances and acquisitions that can attract new participants to our ecosystem and broaden our service offerings. In November 2020, we entered into definitive agreements with JOYY Inc. to acquire its domestic live streaming business in China, which includes YY mobile app, YY.com website and PC YY, among others.

Our Business

Our operations are primarily conducted in China, and our revenues are primarily generated from China. Our business consists of two segments: Baidu Core and iQIYI. Within Baidu Core, our product and services offerings are categorized as follows—Mobile Ecosystem, Baidu AI Cloud and Intelligent Driving & Other Growth Initiatives. Aside from Baidu Core, Baidu Inc. includes iQIYI, which became a stand-alone public company in March 2018.

Our Technology Innovation

Since our inception in 2000, we have been focusing on developing our Chinese language internet search services and solidifying our leadership position in the Chinese language search market by (i) enhancing and expanding both our core search functionality and suite of search products, to achieve traffic growth and market share expansion and (ii) developing and refining our pay-for-performance (P4P) online marketing platform business model to realize the scalability and optimize monetization.

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We are the first mover to bring the search plus feed model to mobile the Chinese market, according to the CIC Report. Search service providers traditionally respond to user queries by providing a list of web-links and directing users to other sites for information and services, whereas Baidu App and other apps aggregate content and services on the Baidu platform and enable users closed loop transactions without leaving the platform. In the era of mobile Internet, as a result of smaller screen size and a platform’s ability to understand user behaviors, the search plus feed model allows users to actively discover information and services through search, and consume personalized and curated push content based on our AI-powered recommendation engine.

In 2010, we began using machine learning, a branch of AI, to improve users’ search experience. By building a large knowledge graph, for example, training a machine to recognize relationships between the huge amount of content on the Internet and key words, we can improve the relevancy of search results for our users. Content on the Internet is usually made up of text, photos with tags and short videos with background sound. By training Baidu Brain, our core AI technology engine, to recognize how the Chinese language is used, we are able to build strong understanding of the Chinese semantics, which has led to the development of our core AI capabilities, including knowledge graph, natural language processing, speech recognition and computer vision. We have then made our AI capabilities available to a large developer community.

Our AI technological innovation has been well recognized by leading institutions. In July 2020, ERNIE, our natural language processing framework that was launched in 2019, won the highest honorary recognition at the 2020 World Artificial Intelligence Conference, the SAIL (Super AI Leader) award. In 2019, ERNIE became the first AI model to score above 90 on GLUE, which is widely considered as the benchmark for testing AI language understanding. The ranking has been otherwise dominated by U.S. technology firms and universities.

With AI increasingly become a key driver for growth, innovation and transformation in many industries, AI deep learning frameworks function as operating systems that empower such changes. PaddlePaddle, our open source deep learning framework accessible to the global developer community, opened its source code to public in 2016. Since then, PaddlePaddle and Baidu Brain, our core AI technology engine and open AI platform that builds on PaddlePaddle, have been adopted by a thriving developer community of more than 2.65 million developers as of December 31, 2020, which is the largest AI developer community in China. This strategic decision has allowed us to continually improve Baidu Brain, PaddlePaddle and AI capabilities, enhance and differentiate our AI solutions through valuable insights from the vibrant developer community, and improve the effectiveness, accuracy and functionalities of our AI solutions, which in turn help Baidu Brain better power our businesses, including Mobile Ecosystem, AI Cloud and Intelligent Driving & Other Growth Initiatives. Below are examples of how our AI capabilities have been applied within Baidu Core:

- **Mobile Ecosystem:** As merchants are increasingly prioritizing mobile conversion, we offer Managed Page to merchants in order to improve their online marketing effectiveness. Merchants can open an account on our platform and port their content and services onto Managed Page as the landing page for their search results. After using Managed Page, merchants can leverage AI technology previously unavailable to them to deploy mobile advertisement with more precision thus better conversion and reach potential customers with similar user profiles. Merchants are rapidly adopting Managed Page due to improved marketing effectiveness powered by our AI capabilities.
- **AI Cloud:** Our AI Cloud differentiates itself by providing AI solutions based on AI capabilities and knowledge graphs. Some examples of our AI cloud solutions include: (i) a

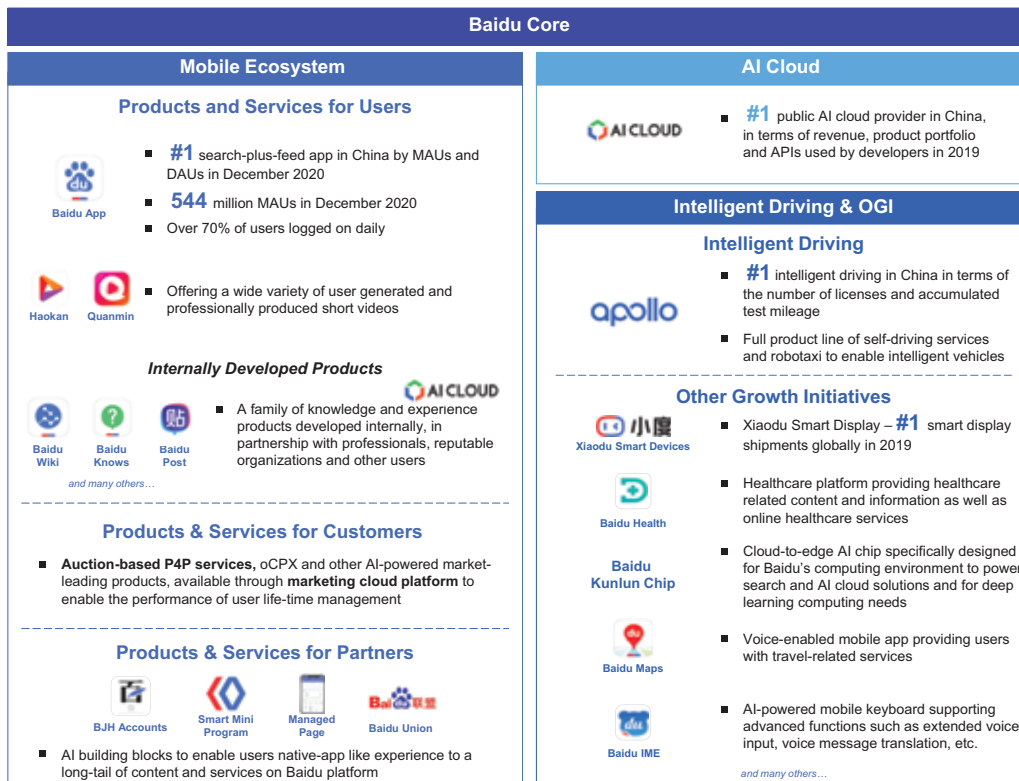
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major telecom operator installing our automated call center solution powered by Baidu Brain to handle millions of calls per month, reducing the average call time per customer by 40%; (ii) a utility company using our knowledge-graph cloud solution to determine the amount of electricity needed to support a geographic region that was deploying EV charging stations; (iii) a retail bank using our knowledge-graph cloud solution to improve credit risk management for consumer and SME lending; and (iv) a large enterprise using our knowledge-graph cloud solution to recommend relevant documents to its employees to support the daily and weekly write up of management reports.

- **Intelligent Driving:** Leveraging our AI capabilities, especially computer vision, we are the market leader in autonomous driving in China, in terms of the number of test miles and test licenses. As of December 31, 2020, Apollo accumulated Test miles in China reached 4.3 million and we have received 199 autonomous driving licenses with extensive geographical coverage in China, compared to the second player which had approximately 20 licenses.
- **DuerOS Smart Assistant:** Xiaodu smart devices are powered by AI technologies, such as ERNIE, our pre-training language understanding framework to provide best-in-class rate of automatic speech recognition, rate of return and rate of satisfaction among similar products in China.

Baidu Core

The chart below visualizes our key products and services under Baidu Core.



Baidu Core—Mobile Ecosystem

Baidu Mobile Ecosystem provides a platform for people to discover and consume information through search and feed and facilitate interaction and engagement among users, creators, service providers, and merchants, alike. In particular, our ecosystem allows merchants, creators, publishers and service

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providers to acquire users, interact with users by provide information, content, products and services, and transact with users. This marketing funnel approach from user acquisition to user engagement to monetization demonstrates our value to merchants, allowing them to build a life-time relationship of users. In addition, this platform-centric approach has enabled our Mobile Ecosystem to start diversifying commercialization beyond online marketing into other services.

Products and Services for Users

Baidu App. Our flagship app enables users to access our search, feed, content and other services through mobile devices. Baidu App offers twin-engine search and feed functions that leverage our AI-powered algorithms and deep user insight to offer users a compelling experience. Through the building blocks of BJH accounts, Smart Mini Program and Managed Page, Baidu App provides users single log-on, native-app-like experience to a wide range of information and services dispersed across isolated mobile apps and HTML5 websites, as well as merchants a full suite of marketing cloud services. Baidu App’s spanning mobile ecosystem has resulted in more users logging in. In December 2020, MAUs and DAUs of Baidu App reached 544 million and 202 million, respectively.

- *Baidu Search.* Users can access our search and other services through Baidu’s properties and Baidu Union partners’ properties. In addition to text inputs, users can conduct AI-powered voice search and visual search. Voice search integrates speech recognition and search technologies to enhance the user experience by providing a more natural and convenient input modality. Visual search enables the use of smart phone cameras to capture images and retrieve related content and services on the Internet. For example, users can take a photo of a plant or a pet, to identify the species.



Visual search showing the brand and detailed information of a product, along with the link to purchase the product



Visual search showing the species of the plant being searched, along with the detailed information from the Baidu wiki

We also endeavor to improve the search experience, through other AI-powered products, such as Top 1, to satisfy user queries with the first displayed search result, which we believe will be an important capability with the adoption of smart devices with smaller screens. In addition, we offer vertical search, such as video search and online literature search to our users.

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- **Baidu Feed.** Baidu Feed provides users with personalized timeline based on their demographics and interests. Baidu Feed complements our core search product, leverages Baidu AI recommendation algorithms and monetization platform, and contributes to user engagement and retention, including content sharing, likes, and comments. Baidu Feed provides text-to-speech function to help users consume Internet content hands free, as well as leverages its large traffic to distribute video content from Haokan, Quanmin, iQIYI and third parties.

Haokan. Haokan offers a wide variety of user generated and professionally produced short videos, usually several minutes long, in coordination with MCNs. Haokan allows users to upload, view, search, rate, share, favorite, comment, and follow. Video creators and curators can distribute their content to build a fan base and receive revenue share for their content contribution.

Quanmin. Quanmin is a flash video app for users to create and share short videos, usually less than one minute long, and live videos with entertainment orientation, such as musical, dance, comedy, acting, and lip-sync. Users can shoot or upload flash videos and edit them with built-in special effects, filters and stickers. Contents are distributed in personalized timeline powered by Baidu AI recommendation algorithms.

Internally Developed Knowledge-and-Information-Centric Products

Our content and services ecosystem also includes a comprehensive portfolio of knowledge and information products developed internally, in partnership with professionals, reputable organizations and other users. For example, we provided live streaming content from healthcare industry experts in 2020, to help users better understand and cope with the COVID-19 pandemic.

Baidu Wiki. A leading wiki in China compiled by experts in specialized fields featuring high-quality columns and videos, such as *Encyclopedia of Intangible Cultural Heritage*, *Digital Museum* and *Recorder of History*.

Baidu Knows. An online community where users can pose questions to other users, such as individuals, professionals, and enterprises. Baidu Knows leverages Baidu’s search capabilities to help users find answers to their questions on the Internet fast and efficiently, while at the same time allow various partners of Baidu Knows to engage with their targeted users.

Baidu Experience. An online platform where users share daily knowledge and experience, providing practical tips and interesting perspectives in areas, such as software, lifestyle, and games, etc.

Baidu Post. A social media built on topical online communities. Users can post text, image, audio and video content and reply to original curation, forming valuable discussion groups. Baidu Post draws new users through close integration with search and user generated content, and has been a popular platform for celebrity fans, online game players, and online novel readers to share topical discussions, especially about current trends.

Products and Services for Partners

We attract numerous partners to our platform through our AI building blocks and Baidu Union, which help create opportunities for us to work with our partners in research and development and other business cooperation and establish long term business relationships.

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AI Building Blocks. The number of smartphones sold in China is on a decline and app installation costs have been rising, causing app developers to take interest in offering their content and services on Baidu App with native-like app experience. Similarly, website owners are experiencing the challenge to grow their business while open in-app search queries are outgrowing browser search queries. To help app developers and website owners grow their business and leverage their traffic more efficiently with AI-powered tools and capabilities, we offer Smart Mini Program and Managed Page to our partners, respectively. We also offer BJH accounts to enable content providers to place their content on our publisher network and make their content searchable.

- *Baijiahao (BJH Accounts).* Our publisher network aggregates articles, photos, short videos, live videos, and augmented reality clips from MCNs, media outlets, and other professional sources, for distribution through search, feed, and short video products. BJH publisher accounts reached 3.8 million in December 2020, representing a growth of 48% over the same period in 2019.
- *Smart Mini Program.* App developers may share their content and services in Baidu App with native-app like experience through increasingly popular applets, known as Smart Mini Program. Users can now search for and access content and services that historically were only available in standalone apps within Baidu App, without having to download and maintain so many apps on their phones. Launched in July 2018, Smart Mini Program has seen large user growth, with MAUs of Smart Mini Program reaching 414 million in December 2020.
- *Managed Page.* Managed Page is a hosted mobile alternative for website owners. Site owners may open an account on our platform, use our tools and services powered by AI and engage with users without having to maintain their own site and pay for server, software and bandwidth costs. Managed Page comes with industry-specific templates and is designed to provide users with more reliable and secure information.

Baidu Union. We match the promotional links of our online marketing services customers to the online properties of Baidu Union partners, which consists of a large number of partners, such as third-party websites, wap sites and mobile apps. Some Baidu Union partners, such as online portal websites and Internet cafes, also embed our products and services, such as Baidu Search or a search function powered by Baidu Search, onto their online properties, which allows Baidu Union partners to provide high-quality, relevant search results to their users without incurring the cost of development and maintenance for advanced search capabilities and monetize their traffic through revenue sharing arrangements with us. Baidu Union partners may use our content recommendation system to provide feed content and ads to their users. We typically pay our Baidu Union partners a portion of the online marketing revenues based on pre-arranged agreements.

In addition, we also enter into arrangements with Baidu Union partners to provide our search engine in their browsers. We typically pay such Baidu Union partners a fee based on prearranged agreements.

Products and Services for Customers

We, through our network of third-party agents and our direct sales team, deliver online marketing services to a diverse customer base consisting of small and medium-sized enterprises (SMEs) across industries, including healthcare, retail, e-commerce, education, personal care, real estate, home furnishing, automobile, financial services, professional services, franchising and online games. In 2020, we served around half a million enterprise customers, who are customers of our online marketing services and business services.

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Our online marketing services enable the delivery of comprehensive, rich, and diversified marketing offerings to fulfill customer needs. Our online marketing services include P4P (pay for performance) services and others. We generate revenues primarily from the sale of P4P online marketing services and other marketing services to our customers, which accounts for a majority of the our total revenue for the years ended December 31, 2018, 2019 and 2020.

P4P. Our auction-based P4P services allow customers to bid for priority placement of paid sponsored links and reach users who search for information related to their products or services. We charge our customers on a cost-per-click basis. Customers may choose to purchase search, feed and other online marketing services and have the option to set daily allowances targeting users by geography in China and specify the time period for their campaign. As our partners adopt Smart Mini Programs and Managed Page, some of them have begun to use these properties as their landing page, in lieu of their own mobile apps and websites.

Search marketing services are mainly provided to customers through our proprietary online marketing system which drives monetization efficiency by improving relevance in paid search and optimizing value for our customers.

Feed marketing services usually comprise image-based or video-based advertising, appearing between the feed headlines or within the feed content. It is powered by Baidu AI in order to better match goods and services providers with their targeted audience while optimizing user experience.

Others. Our other marketing services comprise display-based marketing services and other online marketing services based on performance criteria other than cost-per-click. Customers can choose different mix of our service offerings to optimize their return on investment. BrandZone allows customers to display integrated text, logo, image, and video in a structured and uniform manner on a prominent position of the search result page or in vertical search products, such as Baidu Knows. Programmatic marketing platform supports the placement of advertisement using standard, intelligent, or customized creativity, different purchasing methods (guaranteed delivery or real time bidding), and multiple payment methods.

Marketing cloud platform. Our marketing cloud platform integrates one-stop-shop media purchase with CRM functionalities, to allow our customers to purchase brand and performance-based marketing services, build audience and user engagement, generate leads and maintain relationships with users, leveraging tools and services powered by Baidu AI. Our marketing cloud platform helps us better understand our customers’ needs and enable our customers to leverage Baidu’s AI to simplify their marketing process and improve the effectiveness of their marketing efforts.

Our Mobile Ecosystem, built upon Baidu App as well as a dozen other apps, offers a wide range of third-party content and services to hundreds of millions of users, typically free of charge. Our AI building blocks and other products and services for partners have attracted millions of partners to become participants in our Mobile Ecosystem and generate content and services onto our platform and to tap into our over- half-a-billion user base. The more partners we bring into our Mobile Ecosystem, the better we become at providing users with a more comprehensive reach and cover content and services in more diversified formats than competing products, which in turn attracts more users and partners to our Mobile Ecosystem. For our Mobile Ecosystem business, we generate a substantial majority of our revenues from the provision of online marketing services to our customers and through third-party agents. We charge our customers periodically based on usage while requiring certain customers to pay a deposit. We also offer certain customers credit terms. In addition to offering ads on

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our platform, we serve promotional ads from our customers on the apps or website properties of Baidu Union partners. We also power the search engines of Baidu Union partners.

Baidu Core—AI Cloud

Our AI Cloud offers a comprehensive set of cloud solutions, including AI PaaS and SaaS, based on our unique AI capabilities, and IaaS in computing, storage, network, database and delivery services. Our IaaS services provide our customers the flexibility to quickly scale or cut back on their cloud computing needs without having to provide huge capital layout upfront. Our AI solutions, usually consisting of PaaS and/or SaaS, leverage our AI capabilities to improve our clients’ operational efficiency and service levels. For example, we enabled a client in the manufacturing sector to automate quality assurance checkpoints on its production line by leveraging our computer vision capabilities. This solution helped our client reduce labor cost and improve their operational efficiency. Our goal is to offer a comprehensive set of products, services, and tools to enable enterprises and the public sector to improve productivity and operational efficiency through the use of Baidu AI and cloud infrastructure.

AI Solutions. Developers and enterprises can easily access and build customizable AI solutions for various industries by leveraging our full suite of cloud-based modularized solutions, including algorithms, pre-training models and data sets in areas of speech recognition, computer vision, NLP, OCR, video analysis, and structured data analysis. Our powerful and cost effective cloud-based modularized AI solutions allow developers and enterprises to improve their own products and services and expand their use cases over time. While the services on this platform is free for developers, its wide adoption and application by our large developer community allow us to further improve our AI capabilities over time to maintain our technological advantage. Furthermore, as we have access to where the developer community and its customers are directing their efforts, we use those insights to enhance our AI solutions and direct our investments in AI capabilities targeting industries have the most commercialization opportunities.

Knowledge-Graph Cloud Solutions. We offer our large-scale knowledge graph to establish and pre-train various decision models for our customers. Using our customers’ big data, we can establish systematic knowledge graph and develop various computing models that can provide instantaneous answers to complicated decision making for our customers. Leveraging the knowledge graph that we have built from handling vast amounts of content online for the last two decades, we can provide differentiated knowledge-graph cloud solutions built on our AI PaaS for specific applications and develop various computing models that can be agilely adopted and applied to the needs of different customers across multiple industries. For example, a utility company used our knowledge-graph cloud solution to determine the amount of electricity needed to support a geographic region that was deploying EV charging stations; a retail bank used our knowledge-graph cloud solution to improve credit risk management for consumer and SME lending; and a large enterprise used our knowledge-graph cloud solution to recommend relevant documents to its employees to support the daily and weekly write up of management reports.

Industry Vertical Solutions. Leveraging our PaaS and SaaS solutions and knowledge graph, we have developed customized AI cloud solutions for our customers in specific industries, such as smart transportation, finance, manufacturing, utilities, telecom and media. Our experience in serving industry leaders in these verticals further allows us to quickly scale to provide customizable solution to serve other enterprises in the same space, supporting our deeper penetration in these verticals. For example, in the transportation industry, we are a pioneer and industry leader in developing V2X solutions, the infrastructure backbone to smart transportation, to cities in China to help them improve municipal

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traffic condition, air pollution and road safety, using Baidu AI technology. In August 2020, we won a RMB460 million project to help the city of Guangzhou to improve its traffic efficiency and safety by adopting our V2X solution. The Guangzhou project uses Apollo ACE transportation engine, which, in essence, is a transportation cloud solution that processes traffic information from Apollo MaaS and V2X, DuerOS connected vehicles and Baidu Maps, providing traffic agencies better information to improve traffic management and transportation services and offer autonomous driving services. The Guangzhou project demonstrates our technological capabilities and the advantages of our full-stack solutions, which could help us attract more contracts from other cities. As of December 31, 2020, we have won projects in over one dozen cities including Beijing, Shanghai and Guangzhou. The industry know-how from our existing businesses, such as our Mobile Ecosystem and iQIYI, also provides valuable insights on how to tailor AI Cloud solutions to customers in the technology and media industries.

Others. We offer Baidu Drive, which allows users to store and retrieve photos, videos, and other files on AI Cloud, along with other capabilities, such as group share and data transfer.

For AI Cloud, we generate revenue by providing cloud services and solutions to enterprise clients, consumers and the public sector directly or through solution integrators for a lump-sum fee or on a subscription basis. We also generate revenue from Baidu Drive from membership services provided to individual customers. Baidu Core’s cloud services revenue reached RMB9.2 billion (US\$1.4 billion) in 2020, increasing by 44% from 2019. Baidu Core’s cloud services revenue reached RMB3.3 billion (US\$0.5 billion) in the fourth quarter of 2020. Year-over-year revenue growth rate of our cloud services in 2020 has been accelerating to 67% in the fourth quarter of 2020 with increasing recognition of our AI capabilities and improving COVID-19 condition in China.

Baidu Core—Intelligent Driving & OGI

Intelligent Driving & OGI include developments with large total addressable markets and earlier-stage commercialization with a growing customer base, including Apollo intelligent driving and DuerOS smart assistant.

Intelligent Driving

We are the market leader in autonomous driving in China in terms of number of test miles and number of test licenses. As of December 31, 2020, we had 199 autonomous driving licenses with extensive geographical coverage in China, compared to the second player which had approximately 20 licenses. A well-known research firm, names Apollo as one of the four global leaders in autonomous driving, recognizing us as the top-tier autonomous driving company from China. Apollo is an open platform, which we believe maximizes the reach and value of our technology. As of December 31, 2020, our Apollo ecosystem has more than 200 partners, tier one suppliers and other strategic partners cumulatively.

With its focus on intelligence, Apollo provides a comprehensive, safe, secure and reliable solution that supports all major features and functions of an autonomous vehicle, helping build intelligent vehicles and smart roads through intelligent transformation. We have an extensive portfolio of autonomous driving technology infrastructures. Our experience in implementing and operating V2X solutions, accumulated test miles, and our deep learning capability helps us train models from real world and simulated data to improve the accuracy and effectiveness of our solutions.

Our ecosystem, industry know-how, road and traffic understanding, technology, experience with autonomous driving operations and cost advantage give us strong competitive advantages in

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driving the development of the intelligent driving industry, which includes Apollo Self Driving (HD Maps, AVP and ANP), intelligent EVs and robotaxi (autonomous driving fleet operation).

Apollo Self Driving. We have been investing in L3 and L4 self-driving technology to provide automakers with self-driving services. Under Apollo Self Driving, HD Maps supports L3 and L4 self-driving. In addition, we introduced AVP (our automated valet parking) services in 2018, which allow a driver to get out of the car upon arrival at his or her destination and our L4 solution would enable the vehicle to autopark, and to direct the vehicle to automatically drive to driver’s location out of the parking lot. In December 2020, we introduced ANP (our autonomous navigation pilot) services, which leverage our autonomous driving capabilities. We have signed strategic agreements with 10 leading automakers to power their passenger vehicles with HD maps and/or AVP, and we recently started accepting orders for our ANP services. These products are in the early stage of monetization and their revenue contribution is insignificant.

Intelligent EVs. We recently formed a new EV company and have entered into a strategic partnership with multinational auto manufacturer Zhejiang Geely Holding Group (Geely). We will provide intelligent driving capabilities to power the passenger vehicles, and Geely, which holds the distinction of best-selling Chinese automobile brand in past years under the Volvo and Geely brands, will contribute its expertise in automobile design and manufacturing.

Apollo Robotaxi. Robotaxi operation represents a massive opportunity. We received T4 licenses, the highest level of autonomous driving test license issued by the working group led by Beijing Municipal Commission of Transport, which permits autonomous vehicles to operate in complex driving conditions, including urban roads, tunnels, school zones and other scenarios. In September 2019, Apollo’s first robotaxi pilot program was made available to the public in Changsha, Hunan. Since then, Apollo’s robotaxi service has been made available in Beijing, Changsha and Cangzhou and has expanded into larger networks and more complex road conditions, such as downtown streets. In October 2020, Baidu fully opened the Apollo Robotaxi service to public in Beijing. Robotaxi is in the early stage of monetization and its revenue contribution is insignificant.

OGI

Baidu Health

Baidu Health’s goal is to provide doctors and hospitals more efficient online presence, through social accounts, live streaming seminars, discussion forums and telemedicine, as well as providing them with hosted management tools to remain in contact with their patients efficiently, such as messaging, appointment re-scheduling and monitoring of treatment plans. Conversely, Baidu Health help users find the doctor and hospital that best suits their different healthcare needs. Through our AI building blocks, we promote an information to social to purchase workflow, while connecting users to doctors and hospitals to improve their wellness over a lifetime. Peak-day healthcare related search queries reached 190 million in 2020.

Baidu Health consists of in-depth, authoritative healthcare content, including that from approximately 300,000 doctors and medical experts, by aggregating a wide range of third-party healthcare and wellness information from our AI building blocks, as well as from self-produced products, such as Baidu Healthcare Wiki.

Through BJH accounts, Smart Mini Programs, live streaming, and messaging tools, we enable users to engage with doctors and more than 100 hospitals nationwide and make an informed decision on selecting the doctor or hospital organization that most fits their needs, and continue to gain access to their primary doctor and affiliated hospital.

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DuerOS Smart Assistant. DuerOS is a leading smart assistant for the Chinese language, which powers first-party Xiaodu home smart devices and smart earphones, as well as third-party smart phones, children smart watches and story machines. DuerOS is differentiated by its multi-round conversation AI capabilities, leveraging internally designed Baidu Honghu AI chip, as well as by DuerOS skills store, which offers over 4,400 skills in wide ranging genres, including education, video, online game and live streaming. The wide selection of skills offered on DuerOS has allowed Xiaodu Smart Display to achieve an average daily activated time span per device of over 3 hour in 2020. In 2019, Xiaodu Smart Display ranked No. 1 in smart display shipments globally, and Xiaodu smart speakers ranked No. 1 in smart speaker shipments in China, according to the CIC Report. We generate revenue from the sale of our smart assistant devices to our customers directly and through our distribution network.

Baidu Maps. A voice-enabled mobile app providing users with travel-related services, including POI search, route planning, precise navigation, taxi-hailing service and real-time traffic condition information. Baidu Maps has a MAU of 316 million in December 2020. Baidu Maps also provides professional and stable map services to business partners across different sectors.

iQIYI

iQIYI is an innovative market-leading online entertainment service in China. iQIYI’s platform features iQIYI original content, as well as a comprehensive library of other professionally produced content (PPC), professional user generated content (PUGC) and user-generated content.

Premium content is critical to the success of iQIYI’s business. iQIYI needs to produce and license premium content in order to deliver a differentiated and engaging entertainment experience for its users. Content cost has historically accounted for the biggest portion of iQIYI’s cost of revenues. In 2020, content cost accounted for approximately 75% of iQIYI’s cost of revenues. Our content portfolio consists of original content, content licensed from third party professional content producers, as well as content uploaded by professional and other users. To cater to the tastes of Chinese users across their diverse spectrum, iQIYI licenses content from thousands of professional content providers and have built a vast and diversified library of professionally produced content. iQIYI’s content library included a wide selection of drama series, variety shows, films, kids programs, documentaries, animations, sports programs as well as other various genres of program, covering more than 30 content categories. This vast and diversified content library has helped iQIYI attract users of different ages and backgrounds and increase user engagement.

PPC. iQIYI’s PPC mainly includes original content and licensed content. As of December 31, 2018, 2019 and 2020, iQIYI’s library of professionally produced content included over 60,000, 50,000 and 40,000 titles of drama series, variety shows, films as well as other various genres of program.

- (i) Original content. iQIYI’s original content includes both content produced in-house and content produced in collaboration with quality third-party partners. iQIYI obtains the intellectual property rights through production, adaptation or purchase from third parties, while the partners, typically established entertainment production companies, are responsible for content development and production. iQIYI maintains a high degree of control during the content development and production process. In the content production process, iQIYI leverages its deep understanding of entertainment, users and content, as well as advanced technology, to identify original literary titles or scripts with the most potential, nurture promising artistic talents and execute impactful marketing campaigns. For content produced in-house, iQIYI staffs the production with its own highly professional development team of well-recognized producers, production professionals,

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artists and a post-production editing professionals. For content produced in collaboration with quality third-party partners, iQIYI typically engages quality production companies through individual negotiation or through a competitive bidding process for the right to produce content, and iQIYI pays such production companies in the form of a guaranteed fee and/or revenue sharing.

With an illustrious track record of producing blockbuster original titles and the self-production capability spearheaded by over 50 in-house studios and partnership programs, iQIYI has become a symbol of high-quality video content. Since 2015, iQIYI has released many award-winning multi-genre original titles, such as *The Lost Tomb* (盜墓筆記), *The Mystic Nine* (老九門), *Burning Ice* (無證之罪), *Story of Yanxi Palace* (延禧攻略), *The Thunder* (破冰行動) and *The Bad Kids* (隱秘的角落). iQIYI also pioneered and produced a number of internet variety shows that are highly popular, such as *The Rap of China*, *Idol Producer*, *The Big Band* (樂隊的夏天) and *Qipa Talk* (奇葩說), the last of which was released in 2014 and wrapped up its seventh season. Leveraging its initial success, iQIYI has extended selected popular titles into multi-season format. In order to provide high-quality original content offerings to our users, iQIYI has managed to attract and retain top talents available in market and suitable for the development and production.

- (ii) Licensed content. iQIYI provides users with a curated selection of high-quality PPC from third parties. Leveraging its expertise in content selection, iQIYI have successfully debuted well-received titles such as drama series *iPartment* (愛情公寓), *In the Name of People* (人民的名義), *Go Go Squid* (親愛的，熱愛的), *Qing Yu Nian* (慶餘年), *Reunion: The Sound of the Providence Season 2* (重啟之極海聽雷第二季), and variety show *Keep Running Season IV* (奔跑吧第四季). iQIYI licenses video content typically at fixed rates for a specified term, and pay licensing fees generally in installments upon signing of the contacts and during the licenses period. iQIYI also exchanges rights to distribute licensed content with other internet video streaming services to enrich its content library. In certain cases, iQIYI has the right of first refusal to purchase new content produced by the licensor. iQIYI’s licensed content library also features a rich collection of movies, animations, documentaries and other content.

Other Video Content. iQIYI offers a broad base of other video content with all kinds of genres, formats, and lengths of duration, such as internet movies and dramas, mini variety shows and animations, interactive videos, vertical or horizontal videos, as well as grassroot or influencer uploaded videos, edited video clips, and video blogs, or Vlogs, among others. iQIYI’s other video content expands its library and allows it to capture a broader user base, drive user engagement and enhance user stickiness.

iQIYI has developed a diversified monetization model to capture multiple opportunities arising from the rapid growth of the online entertainment industry in China. iQIYI generates revenues through membership services, online advertising services and a suite of other monetization methods. It pioneered a large scale paid content subscription business in China. It appeals to advertisers through broad and efficient user reach, as well as innovative and effective advertising products. iQIYI’s sophisticated monetization model fosters an environment for high-quality content production and distribution on its platform, which in turn expands its user base and increases user engagement, creating a virtuous cycle.

Membership Services. iQIYI’s membership services generally provide subscribing members with superior entertainment experience that is embodied in various membership privileges. Subscribing members have access to a large collection of VIP-only content comprising drama series, movies, animations, and cartoons, among others, and have earlier access to certain content aired on the iQIYI platform. Membership privileges generally include substantially ad-free streaming, 1080P or 4K high-

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definition video, enhanced audio experience, accelerated downloads and others. Subscribing member privileges also include coupons and discounts on paid on-demand films, as well as special privilege in offline events, such as exclusive access to live concerts. The number of subscribing members increased 22.3% from 87.4 million as of December 31, 2018 to 106.9 million as of December 31, 2019. Excluding individuals with trial memberships, the number of subscribing members increased by 22.7% from 86.1 million as of December 31, 2018 to 105.7 million as of December 31, 2019. As of December 31, 2020, the number of iQIYI’s subscribing members and the number of subscribing members excluding individuals with trial memberships were 101.7 million and 100.7 million, respectively.

Online Advertising. The prices of iQIYI’s advertising services depend upon various factors, including form and size of the advertising, level of sponsorship, popularity of the content or event in which the advertisements will be placed, and specific targeting requirements. Prices for the brand advertising service purchased by each advertiser or advertising agency are generally fixed under sales contracts.

Content Distribution

iQIYI sub-licenses procured third-party content within the authorized scope to other internet video streaming services. iQIYI also entered into barter agreements to exchange internet broadcasting rights of licensed content with other internet video streaming services. We distribute our selected original content to regions outside of China and to TV stations in China. Exclusive licensing agreements iQIYI enters into with the content licensors has a specified license period and provides iQIYI rights to sub-license these contents to other parties, while non-exclusive licenses do not provide iQIYI with the right to sub-license. iQIYI enters into a non-exclusive sub-license agreement with a sub-licensee for a period that falls within the original exclusive license period, for cash or exchanging online broadcasting rights of licensed copyrights.

Technology

We focus on technology and innovation. To stay at the forefront of the internet industry and to achieve long-term growth and success, we invest heavily in research and development. We have established several research labs in China and the United States, to enhance our research and development capabilities, including AI, quantum computing and other areas.

Baidu AI

We have been investing in AI since 2010, and have developed “Baidu Brain,” our core AI technology engine, which has become a powerful technology platform that powers all of our business. We have opened up our AI platform to a large community of developers, which helps improve our AI capabilities and accelerate large-scale implementation of our AI. Request on Baidu Brain has peaked over 1 trillion hits per day in 2020.

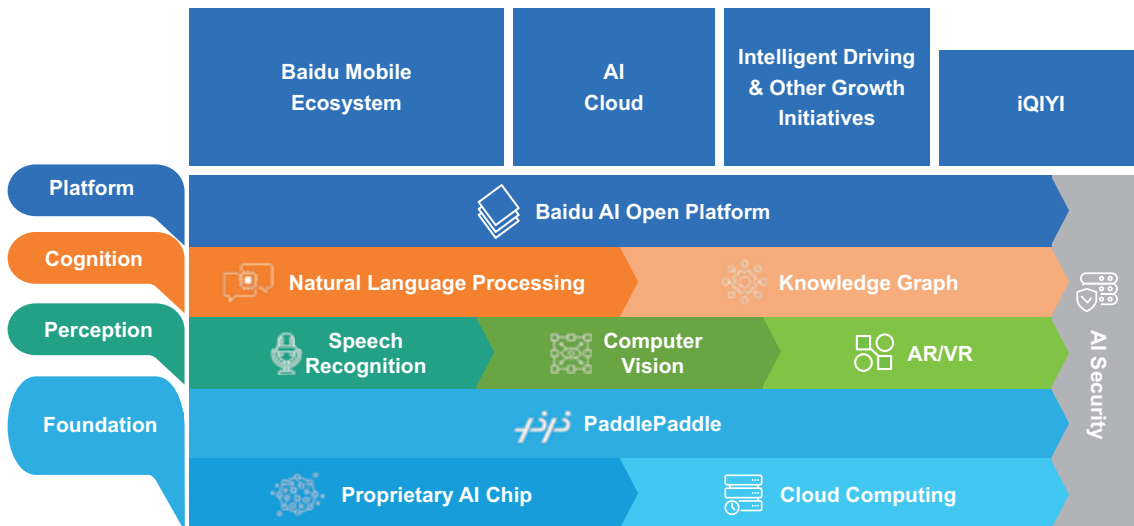
Our AI capabilities encapsulated on “Baidu Brain,” our core AI technology engine, consist of four layers and one module, as follows:

- a foundation layer, consisting of PaddlePaddle, our open source deep learning framework and platform, as software, Kunlun AI chips as hardware and databases as fuel;
- a perception layer, aggregating internally developed algorithms for speech recognition and synthesis, computer vision and augmented reality & virtual reality;
- a cognition layer, consisting of algorithms for natural language processing and knowledge graph;

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- a platform layer, opening our technologies to partners and developers to develop a strong AI ecosystem; and
- an AI security module that ensures Baidu Brain’s security, safety and privacy.

Baidu Brain



AI Capabilities. Baidu Brain 6.0, which was launched in September 2020, making available over 270 AI capabilities, including natural language processing, knowledge graph, speech recognition and synthesis, computer vision, etc.

- **Knowledge Graph.** Baidu AI consists of heterogeneous knowledge graphs of entity-graph, attention graphs, events, POIs, and industry-knowledge, which transform immense multi-element and multi-modal data into a holistic semantic network containing hundreds of millions of nodes and hundreds of billions of relationships.
- **NLP.** ERNIE (Enhanced Representation through kNowledge IntEgration), our NLP framework, is capable of continual learning various knowledge from massive data and has achieved state-of-the-art results in both Chinese and English language understanding tasks. ERNIE has been widely used in the fields of reading comprehension, emotional analysis, search intelligent Q&A, video recommendation, click-through rate prediction. As to machine translation, Baidu Translate provides translations to 203 languages and the number of characters translated daily reached over 100 billion.
- **Speech Recognition and synthesis.** In 2019, Baidu launched the streaming multi-layer truncated attention model (SMLTA) to improve the accuracy of speech recognition, making it possible to recognize mixed Chinese and English or mixed Mandarin dialect speech. Meitron, a voice synthesis technology we developed, maps the tone, style, emotion and other elements into different sub-spaces, which allows a user to switch the voice of an application to his/her voice by recording a voice input of 20 sentences. The Meitron-based voice customization function has been added to Baidu Maps.
- **Computer Vision.** Visual semantics allow the machine to understand videos and extract structured semantic knowledge by recognizing people, movements, items and associated time series. Visual understanding has been applied widely in our video applications. With synthetic virtual image technology, including facial, limb and mouth shape generation, we have developed

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“virtual” customer representative, to be paired with our automated customer service cloud solutions, powered by Baidu Brain.

Our technological innovation in AI has been well recognized by leading institutions. For example, in 2019, ERNIE became the first AI model to score above 90 on GLUE (General Language Understanding Evaluation), which is widely considered as the benchmark for testing AI language understanding. The ranking has been otherwise dominated by U.S. technology firms and universities.

Our unique breadth and depth of AI capabilities provide the differentiating foundational technologies that power all of our businesses. We are one of the very few companies in the world that offers full-stack AI technologies encompassing AI chips, software framework and applications. We believe our strength in AI open platform allows us to apply and commercialize AI across a diverse product portfolio across the consumer, enterprise and public sector.

PaddlePaddle. PaddlePaddle is our deep learning framework, which we open sourced in 2016, and is the No. 1 deep learning framework in China, according to the CIC Report. PaddlePaddle provides: (i) a DL framework based on programming logic enabling both development flexibility and stability; (ii) the ultra-large-scale training capacity for real-time updates of trillion-level parameters of deep learning models; (iii) end-to-end deployment of high-performance inference engines designed for diverse platforms and devices; and (iv) open source industry-grade models covering a wide range of applications.

AI Chips. Baidu Kunlun, a cloud-to-edge AI chip, was introduced in 2018, specifically designed for Baidu’s computing environment, to power search and AI cloud solutions, as well as for our deep learning computing needs. Baidu Kunlun optimizes our AI capabilities on AI Cloud servers while improving cost efficiency. In addition, we have also developed Baidu Honghu to power DuerOS smart devices and in-vehicle infotainment to improve speech recognition performance and provide a cost advantage in our AI offerings.

We have also developed a proprietary technological infrastructure which consists of technologies for search, marketing services, and large-scale systems. Our established infrastructure serves as the backbone for AI, mobile and PC platforms.

Mobile Ecosystem Technologies

Search Technologies. Our search is powered by a set of industry-leading technologies, including the following, among others:

- *Ranking.* We compare search queries with the content on web pages to help determine relevance. We have significantly improved the relevancy, freshness and authority of ranking using our machine learning modules to analyze the rich content on the Internet and user intent, to prioritize the search results. We began using machine learning in 2010, to better understand the semantics beyond simple text of the search keywords, and in 2013, we began to apply deep learning in our search ranking system, which is playing an increasingly important role. In 2019, we began to develop Top 1 (satisfying user with the first search result) by significantly enhancing the results of question parsing and analysis, answer matching, extraction, page content understanding and other aspects of our search engine, which has greatly improved user satisfaction with our search products.
- *Multi-modal search.* We have greatly improved the accuracy of speech recognition in scenarios, such as long sentences, mixed Chinese and English, and strong accent, and thus significantly

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improve user satisfaction of our speech search. We have built a terminal visual interaction engine v1.0 for visual search and facilitated the implementation of convolutional neural network models, reducing the training costs through unsupervised or semi-supervised models.

Marketing Services Technologies. Our marketing services platform serves billions of relevant, targeted sponsored links each day based on search terms users enter or content they view on web pages or in our apps. Our key marketing services technologies include Phoenix Nest, a web-based auction system to enable customers to bid for keywords and automatically deliver relevant, targeted promotional links on Baidu’s properties and Baidu Union partners’ properties. Designed to generate more relevant results, Phoenix Nest helps customers to identify popular keywords and provides them with tools for budget management and marketing effectiveness measurement.

Large-Scale Systems and Technologies. Our large scale and massive amounts of user traffic require our systems to efficiently and effectively allocate resources among the products and services in our large product portfolio. Our key large-scale systems and technologies include our internally developed automated management platform for large size clusters, which enables us to intelligently manage and allocate resources and automatically debug and relocate services, thereby, allowing the huge volume of requests on Baidu search platform to function stably across multiple internet data centers and a large network of servers.

Research and Development

We have a team of experienced engineers who are based mostly in Beijing, Shanghai and Shenzhen, China. We also have development centers in Sunnyvale, California and Seattle, Washington. We compete aggressively for engineering and recruit most of our engineers locally and have established various recruiting and training programs with leading universities in China. We have also recruited experienced engineers globally.

In the years ended December 31, 2018, 2019 and 2020, our research and development expenditures were RMB15.8 billion, RMB18.3 billion and RMB19.5 billion (US\$3.0 billion), representing 15%, 17% and 18% of our total revenues, respectively. Our research and development expenses primarily consist of salaries and benefits for research and development personnel. We expense research and development costs as they are incurred, except for certain internal-use software.

Intellectual Property

We rely on a combination of patent, trademark, copyright and trade secret protection laws in China and other jurisdictions, as well as confidentiality procedures and contractual provisions, to protect our intellectual property and our brand. We have over 7,800 issued patents in China covering invention, utility model and design, and intend to apply for more patents to protect our core technologies and intellectual property. We also enter into confidentiality, non-compete and invention assignment agreements with our employees and consultants, and nondisclosure agreements with selected third parties. “百度,” our company’s name “Baidu” in Chinese, has been recognized as a well-known trademark in China by the Trademark Office of National Intellectual Property Administration under the State Administration for Market Regulation. In addition to owning “” and the related logos, we have applied for registration of various other trademarks. We also have registered certain trademarks in the United States, Australia, Brazil, Canada, Hong Kong, India, Indonesia, Japan, Malaysia, Mexico, New Zealand, Russia, Singapore, South Africa, South Korea, Thailand, the European Union and several other jurisdictions. In addition, we have registered our domain name *baidu.com* and certain other domain names with authorized registrars of ICANN (Internet Corporation for Assigned Names

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and Numbers). We have also successfully become designated Registry Operator for *.baidu* top-level domain names by ICANN.

Internet, technology and media companies are frequently involved in litigation based on allegations of infringement or other violations of intellectual property rights. Furthermore, the application of laws governing intellectual property rights in China and abroad is uncertain and evolving and could involve substantial risks to us. See “Risk Factors—Risks Related to Our Business and Industry—We may face intellectual property infringement claims and other related claims, which could be time-consuming and costly to defend and may result in an adverse impact over our operations” and “—We may be subject to patent infringement claims with respect to our P4P platform.”

Sales and Distribution

We offer products and services for Baidu Mobile Ecosystem through our network of third-party agents and our direct sales team. We typically enter into framework sales agreements with third-party agents, where third-party agents will sell online marketing services to customers such as SMEs, domestic businesses and multinational companies on our behalf. The sales agreements typically limit the industry focus of the third-party agents. The third-party agents provide our online marketing customers with numerous services, including identifying customers, collecting payments, assisting customers in setting up accounts with us, suggesting keywords to maximize ROI and engaging in other marketing and educational services aimed at acquiring customers. We have direct sales presence in Beijing, Shanghai, Guangzhou, Shenzhen, and other cities, covering the major regional markets for our online marketing services and other services. We cover our key accounts through direct sales team and enter into agreements with such key accounts directly.

For AI Cloud, we sell our cloud solutions including IaaS, PaaS and SaaS to our enterprise clients directly or through solution integrators. We offer smart transportation solutions directly to provide tailored solutions to meet the specific needs of our clients.

For Intelligent Driving and OGI, we sell our products and services to our clients directly and through our third-party agents.

iQIYI’s brand advertising is sold through third-party advertising agencies, including members of American Association of Advertising Agencies, or 4As, and leading Chinese advertising agencies, as well as through a direct sales force. Feed advertising services is sold primarily through third-party advertising agencies, whose existing long-term relationships and network resources we strategically leverage, to increase our sales and expand our advertiser base.

Marketing

We focus on continually improving the quality of our products and services, as we believe satisfied users and customers are more likely to recommend our products and services to others. Through these efforts and the increased use of internet in China, we have built our brand with modest marketing expenditures.

We have implemented a number of marketing initiatives designed to promote our brand awareness among potential users, customers and Baidu Union partners. In addition to our brand positioning in the market, we have also initiated a series of marketing activities to promote our products and technologies among existing and potential users and customers, including, but not limited to, Baidu World Conference.

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Competition

For Baidu Core business, our primary competitors are mainly internet companies and online marketing platforms in China. We compete with these entities for both users and customers on the basis of user traffic, cyber security, quality (relevance) of search (and other marketing and advertising) results, availability and user experience of products and services, distribution channels and the number of associated third-party websites. We also face competition from U.S.-based internet search providers providing Chinese language services and online marketing platforms, as well as traditional advertising media.

Online Marketing Platforms, Internet, Cloud and Smart Device Companies in China. Chinese internet companies, such as Alibaba, Tencent, ByteDance, and Xiaomi, offer a broad range of online services, including search, feed, cloud services and smart devices. These companies have widely recognized brand names in China and significant financial resources. Furthermore, some of these companies are private and are able to expend significant resources without consideration for near-term return on investment. We compete with these companies primarily for user traffic, user time, content, advertising budget and marketing resources. We leverage our AI technology, user traffic, product design and various marketing to enhance users’ reliance on our platforms and services.

U.S.-based Internet Search Providers and Online Marketing Platforms. U.S.-based internet search providers and online marketing platforms, such as Microsoft, Google and Facebook, have a strong global presence, well established brand names, more users and customers and significantly greater financial resources than we do. We may also continue to face competition from other existing competitors and new entrants in the markets of Chinese language search, online marketing, cloud services and smart devices.

Other Advertising Media. Other advertising media, such as newspapers, yellow pages, magazines, billboards, other forms of outdoor media, television, radio and mobile apps compete for a share of our customers’ marketing budgets.

iQIYI competes with Tencent Video and Youku for both users and advertising customers. iQIYI also competes with other internet media and entertainment services, such as internet and social platforms and short-form video platforms, as well as major television stations. iQIYI competes with these market players primarily on the basis of obtaining IP rights to popular content, conducting brand promotions and other marketing activities, and making investments in and acquisitions of business partners.

Our user traffic tends to be seasonal. For example, we generally experience less user traffic during public holidays and other special event periods in China. In addition, advertising and other marketing spending in China has historically been cyclical, reflecting overall economic conditions as well as budgeting and buying patterns. Our results of operations may fluctuate due to the cyclicity and seasonality in our business.

Customers and Suppliers

We have a broad base of customers, and our top five customers accounted for less than 10% of our total revenues for each of the years ended December 31, 2018, 2019 and 2020, respectively. Our top five suppliers accounted for less than 20% of our purchases for each of the years ended December 31, 2018, 2019 and 2020, respectively.

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Our Environmental, Social and Governance (ESG) Initiatives

We are committed to corporate social responsibility and meeting society’s changing needs despite the challenging economic environment. We have established an internal environmental, social and governance communications and management mechanism to comprehensively improve our corporate governance and benefit society.

We have continuously improved our corporate social responsibility initiatives under the guidance of our ESG framework. We appreciate the oversight, guidance and feedback from different parties and are committed to collaborating closely with domestic and international organizations to support broader industry-wide ESG practices, to explore multi-dimensional use cases for our technology, to empower traditional industries with our capabilities and to promote a healthier lifestyle and the long-term sustainability of our society.

Environmentally Sustainable Mindset

We are a strong supporter of the Ten Principles of the United Nations Global Compact and the UN’s 17 Sustainable Development Goals (SDGs). We have participated in the Climate Group’s EV100 campaign, a global initiative bringing together forward-looking companies committed to accelerating the transition to electric transportation, and are committed to making Baidu a low-carbon, energy-efficient and eco-friendly company through concrete actions. For example, to improve energy efficiency, we implemented various power supply solutions including HVDC offline and BBU (Battery Back-up Unit) in our data centers. Furthermore, our data centers are equipped with large-scale water cooling systems with a free cooling module and OCU (Overhead Cooling Unit) supplemented by fine-tuning operation optimization. As a result of these measures, we improved power usage effectiveness (PUE) of our data centers and further reduced our carbon emissions. We have also adopted various water and energy conservation measures, such as recycling heat energy and introducing electric commuter shuttle busses on our campus to make our offices more environmentally friendly. These initiatives reduced our carbon emissions by over 180,000 tons, as calculated by deducting carbon emissions in project scenario from carbon emissions in baseline scenario, in 2019.

While we rigorously implement environmentally sustainable policies and initiatives, we also encourage our users and the general public to adopt similar measures. For example, by adding new features to the app, we encourage the users of Baidu Maps app to take eco-friendly transportation options including biking and walking to reduce carbon emissions. In 2019, the total number of eco-friendly trips reached 100 million, reducing carbon emissions by approximately 44,000 tons, as calculated by aggregating carbon emissions reduced through various eco-friendly transportation options: (i) for carbon free transportation options such as walking, running and cycling, the amount of carbon emission reduced equals the quotient of the total distance so traveled by the average carbon emission factor of a typical fuel-based vehicle, and (ii) for transportation options with a lower carbon footprint such as taking a bus, the amount of carbon emission reduced equals the quotient of the total distance so traveled by the average carbon emission factor differential between a typical fuel-based vehicle and a typical bus on a per capita basis. We also cooperate with non-profit organizations, such as the International Fund for Animal Welfare, to conduct a series of events that promote public awareness of conservation efforts and science.

Building Social Trust and Developing Talent

Data Privacy and Data Security. As a reputable hi-tech company serving a large community of users, we put data privacy protection and data security as our top priorities. Within the company, we have

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established the Baidu Security Committee and Baidu Data Privacy Committee, comprised of senior decision makers to oversee these two areas, ensure compliance with applicable laws and regulations and to ensure that we are meeting the expectations of our users. We communicate with our users in an easy-to-understand manner to help them understand their rights under applicable laws and regulations. Through our data privacy and data security policies, users can learn about and control how their data is used and provide consent for data collection when necessary. We have put in place a comprehensive auditing mechanism across our business, to keep track of the data privacy and data security actions taken throughout the lifecycle of our products and services. We utilize a complete set of data privacy and data security management systems that allow us to continuously review and improve our processes. We have designed the General Privacy Policies and have drawn up specific privacy policies for individual products and services. We have also built an independent one-stop privacy protection platform, from which users can learn about our data privacy policies and provide feedback. Baidu believes that we can make a complex world simpler through AI, but such vision can only be realized if AI is used properly.

Outlook on Talent and Organizational Development. Our employees are our most important asset. To promote work-life balance for our employees, we have adopted flexible working arrangements and a system of paid leave and compensatory leave, in addition to statutory annual leave. Since 2019, we have been working with an insurance company to introduce commercial healthcare coverage for both our employees and their parents. We are the early adopter among Chinese internet companies to offer such customized coverage. Moreover, we provide a multitude of benefits to our employees and their family members, including pregnant and nursing employees. To better understand employee satisfaction, help employees address work challenges and improve the company’s overall work environment, we conduct annual human capital assessment surveys with all of our employees. We also provide a variety of channels for employees to provide feedback and file complaints. We fully respect and value our employees’ suggestions and feedback.

Innovation and Practice in Social Responsibility

We care about the society that we live in, and we encourage our employees across different product lines to leverage Baidu AI technologies to make our community a better place for everyone.

We retooled our AI capabilities to help users, municipalities and health organizations better cope with the COVID-19 pandemic, as part of our corporate social responsibility effort:

- We provided tens of millions of free online doctor consultations on our healthcare platform and made available our online healthcare services, such as pneumonia screening, to third-party medical apps, to free up hospitals for critical emergencies.
- We donated nearly 20,000 Xiaodu Smart Displays to frontline doctors and their families, allowing them to use contact-less, voice-enabled Internet and conveniently video conference home to stay in touch with their loved ones, while minimizing virus infection. DuerOS also partnered with online education organizations to enable home teaching for kids, while schools were closed down.
- More than 100 Apollo-powered autonomous vehicles have been deployed across 17 cities in China, including Wuhan, Beijing, Shanghai, Shenzhen and Xiamen, to provide medication, face mask and food deliveries, as well as unmanned fever screening and sterilization services.
- Baidu AI call center solution was retooled to allow local municipalities and health commissions to call people and survey their health conditions and travel information. Our smart call center handled over 3 million calls in the first two months, which is equivalent to the workload of approximately 1,000 full-time employees over a month’s period. Our smart call center was also

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used to update the new hours of operation for businesses on Baidu Maps, as restaurants, shops and supermarkets re-opened for business.

- We open-sourced LinearFold, our RNA analysis algorithm, to researchers worldwide for research on COVID-19. LinearFold can accelerate the prediction time of a virus’s RNA secondary structure, potentially from 55 minutes to 27 seconds, affording researchers an opportunity to better understand the pandemic and develop effective vaccines.

We are actively exploring the application of voice-based Xiaodu Smart Display for the education sector and aiding the elderly and the disadvantaged. We have donated Xiaodu Smart Display to 50 primary schools in China where they serve as classroom voice assistants to provide students with an extensive selection of high-quality educational resources. We have worked with an elderly community in Beijing to turn Xiaodu Smart Display into an “elderly care station,” allowing its senior citizens to access community services at any time through far-field voice activation. This service has benefited hundreds of elderly people. Xiaodu Smart Display has also been adopted to help visually impaired students in schools and masseurs in their workplaces in more than 40 cities across China. Xiaodu Smart Display allows visually impaired students to access a wealth of information on the Internet and visually impaired masseurs to control the lighting and room temperature of their work place through far-field voice commands.

As the leading search engine in China, we leverage our platform to reduce gender discrimination and provide charitable organizations with opportunities to be discovered and heard by the public. We have optimized search results for gender-related keywords and deploy technologies to help eliminate gender discrimination on the Internet. To help people build more confidence and cope with mental health issues, we worked with leading psychology institutions in China to launch a Smart Mini Program, an applet within Baidu App, that provided more than 1.2 million users/accounts with timely support and counseling in 2019. To empower charitable organizations and use technology to create a better Internet community, we launched the Common Benefit Project to promote and allow 200 charitable programs to be easily discovered.

Building on our close communication and collaboration with all stakeholders, we will continue to benefit our society. As part of our efforts to create value for our society, we attach great importance to communication and engagement with our users, partners, social organizations and third-party agencies.

Corporate Governance

In July 2005, our board of directors adopted a code of business conduct and ethics (the “Code of Ethics”) that applies to our directors, officers, employees and advisors. The Code of Ethics contains general guidelines for conducting our business consistent with the highest standards of business ethics, and is intended to qualify as a “code of ethics” within the meaning of Section 406 of the Sarbanes-Oxley Act of 2002 and the rules promulgated thereunder. It is designed to deter wrongdoing and to promote (i) compliance with applicable governmental laws, rules and regulations, (ii) honest and ethical conduct, and (iii) full, fair, accurate and timely disclosure in regulatory filings and other public communications made by the Company. The Code of Ethics contains guidelines on fair employment practices and working environment, relationships with counterparties, fair transactions, public disclosure and confidentiality and protection of Company information. We have posted a copy of our code of business conduct and ethics on our website.

We announce our unaudited financial results for every quarter and file our annual reports on Form 20-F for every fiscal year to keep our shareholders and the investing public abreast of the developments of

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the Group. We have also consistently disclosed material events by filing Form 6-Ks with the SEC. We regularly host events, summits and roadshows to facilitate communication between investors and our management. We also strive to maintain open channels for queries from investors and respond to them in a timely fashion — our website contains an Information Request form for requests of additional information. Alternatively, investor inquiries and feedback can be directed by e-mail to irfeedback@baidu.com or by mail to our address. The Company’s investor relations function strives to ensure that shareholders and investors can communicate their opinions to the Company by (1) maintaining the Company’s investor relations website and ensuring that the investor relations mailbox is open for investor contact, (2) maintaining contact with current shareholders and prospective [REDACTED] through various channels such as email, telephone calls, investor tours and conferences, and post-earnings release roadshows; (3) maintaining relationships between the Company and other capital markets intermediaries and (4) facilitating the Company’s earnings calls, collecting investor questions in advance and preparing responses to questions ahead of the conference call. It also hosts designated sessions for investors to communicate directly with members of management at designated events throughout the year. The Company plans to further enhance corporate governance of its investor relations function via management reports on investor relation to the audit committee, which is comprised of independent directors. The audit committee will be added to a distribution list and e-mails sent to irfeedback@baidu.com will be simultaneously received by the audit committee, which will help audit committee determine any key issues that may need further attention. This will enhance the communication between investors, the Company’s management and independent members of the Board, as our investor relations function will be able to seek their guidance, as appropriate. Our independent directors bring a wealth of experience from and serve on boards across different sectors and are well placed to provide insight into investor relations. The Company held an extraordinary general meeting in 2021 and has undertaken to hold annual general meetings thereafter, for which 14 days’ notice will be given to members, in addition to its regular quarterly earnings calls, to facilitate communication with shareholders.

Further, we have three committees under the board of directors: an audit committee, a compensation committee and a corporate governance and nominating committee. We have adopted a charter for each of the three committees. Please see “Directors and senior management — Board practices” for further details.

Investments Management

We invest our excess cash in highly liquid investments, primarily short-term investments with maturities less than one year. Our audit committee approves our treasury policy and reviews our short-term investment portfolio on a regular basis. Addition of new financial institution and investment product are assessed and approved by the treasury, accounting and legal departments, as applicable.

For long-term investments, the Company conducts commercial, financial and legal due diligence on new opportunities and approvals from the investment committee and the Board of the Company depending on materiality.

Properties

Our corporate headquarters, Baidu Campus, is located in Shangdi, Haidian district of Beijing. We own the office building of Baidu Campus and a nearby office building, Baidu Science Park, both located in Shangdi. We are in the process of obtaining the land use permit with the local authority for Baidu Science Park and may result in us paying additional land transaction fee. Besides Beijing, we own and occupy office buildings in Shanghai and Shenzhen.

We also lease offices in Beijing, many other cities in mainland China and places outside of mainland China, including in California (USA), Washington (USA), Hong Kong, Japan and Singapore.

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Our servers are hosted at the internet data centers of major telecom operators, including China Telecom, China Unicom and China Mobile, in over ten selected cities across China. Our content delivery network covers most of the major cities in China.

In 2018, we completed the construction of our Shanxi cloud computing center, which serves as one of our internet data centers in China. In 2019, we completed the construction of our office building in Shenzhen, China.

Employees

We had approximately 40,000, 38,000 and 41,000 full time employees as of December 31, 2018, 2019 and 2020, respectively. As of December 31, 2020, we had approximately 24,000 employees in research and development, 10,000 employees in sales and marketing, 4,000 employees in operation and service, and 3,000 employees in management and administration. As of December 31, 2020, we had approximately 26,000 employees in Beijing, 14,000 employees outside of Beijing but within China, and approximately 300 employees outside of China. We also hire temporary employees and contractors from time to time.

As required by regulations in China, we participate in various government statutory employee benefit plans, including social insurance funds, namely a pension contribution plan, a medical insurance plan, an unemployment insurance plan, a work-related injury insurance plan and a maternity insurance plan, and a housing provident fund. We are required under PRC law to contribute to employee benefit plans at specified percentages of the salaries, bonuses and certain allowances of our employees up to a maximum amount specified by the local government from time to time.

We enter into standard labor contracts with our employees. Our employees are not covered by any collective bargaining agreement. We also enter into standard confidentiality and non-compete agreements with our senior management. The non-compete restricted period typically expires one year after the termination of employment, and we agree to compensate the employee with a certain percentage of his or her pre-departure salary during the restricted period.

We consider our relations with our employees to be generally good. However, as our operations and employee base further expand, we cannot assure you that we will always be able to maintain good relations with all of our employees. See “Risk Factors—Risks Related to Our Business and Industry—We may not be able to manage our expanding operations effectively.”

Insurance

We have purchased insurance to cover certain liabilities, properties and employees in connection with our intelligent driving business. We only have limited business liability or disruption insurance coverage for our operations in China. We provide social security insurance including pension insurance, unemployment insurance, work-related injury insurance, maternity insurance and medical insurance for our employees. See “Risk Factors—Risks Related to Our Business and Industry—We have limited business insurance coverage.”

Legal Proceedings

From time to time, we have been involved in litigation, administrative proceedings or other disputes regarding, among other things, copyright and trademark infringement, defamation, unfair competition, labor disputes, and anti-monopoly inquiries. Our search results provide links to materials, and our P4P,

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Baidu Wenku, Baidu Post, Baidu Wiki, Baidu Knows, Baidu Feed, Baidu Drive, iQIYI and certain other products or services may contain materials, in which others may allege to own copyrights, trademarks or image rights or which others may claim to be defamatory or objectionable.

In 2020, 3,288 complaints were filed against us before various courts in China, and the aggregate amount of the damages sought in these complaints totals approximately RMB628 million (US\$96 million). As of December 31, 2020, 2,127 cases against us were pending before various courts in China. The aggregate amount of damages sought under these pending cases is approximately RMB854 million (US\$131 million). As of December 31, 2020, 7 cases against us were pending before various courts outside China. Some of these proceedings are in a preliminary stage with undetermined damages sought.

In November 2018, an individual, together with his related company, filed a complaint alleging acts of defamation and libel, commercial disparagement, tortious inference with prospective business relations, intentional infliction of emotional distress and civil conspiracy against, among others, us and Robin Yanhong Li in his capacity as our chairman and chief executive officer, in the Supreme Court of New York. The complaint alleged, among other things, that the defendants published articles containing false and defamatory statements concerning the plaintiffs, and sought damages in an aggregate amount of US\$11 billion, including purported punitive damages of US\$10 billion. The defendants moved the complaint to the U.S. District Court for the Eastern District of New York and filed motions to dismiss the complaint. The plaintiff voluntarily dismissed that complaint, and then added us and Mr. Li as defendants to the Second State Court Lawsuit. We filed motions to dismiss that complaint, which were not opposed. The Plaintiff filed a notice of voluntary discontinuance of the complaint in the Second State Court Lawsuit, and subsequently filed a nearly identical complaint in the U.S. District Court for the Eastern District of New York. In January 2020, the U.S. District Court for the Eastern District of New York dismissed that complaint in its entirety with prejudice, and the time for plaintiff to appeal that dismissal has expired. In February 2020, the Supreme Court of New York granted defendants' motions to discontinue the Second State Court Lawsuit with prejudice. No appeal of that order has been filed as of the date of this disclosure. We believe these claims to be without merit and intend to continue to defend ourselves vigorously. The Joint Sponsors with the assistance of their legal advisors, have conducted independent due diligence in relation to the claims, including but not limited to, (i) independent litigation searches on the law suit, including among others, review of the U.S. District Court Docket, the claims in the complaint filed in November 2018 and the order dismissing case from U.S. District Court for Eastern District of New York in January 2020, (ii) desktop searches on the plaintiffs, and (iii) inquiries with the Directors to understand their involvement in litigations or disputes. Based on the due diligence conducted by the Joint Sponsors, nothing material has come to the Joint Sponsors' attention to disagree with the Company's view on the claims.

For many of the above-mentioned legal proceedings, we are currently unable to estimate the reasonably possible loss or a range of reasonably possible loss as the proceedings are in the early stages, or there is a lack of clear or consistent interpretation of laws specific to the industry-specific complaints among different jurisdictions. As a result, there is considerable uncertainty regarding the timing or ultimate resolution of such proceedings, which includes eventual loss, fine, penalty or business impact, if any, and therefore, an estimate for the reasonably possible loss or a range of reasonably possible loss cannot be made. With respect to the limited number of proceedings for which we are able to estimate the reasonably possible loss or the range of reasonably possible loss, such estimates are immaterial. However, we believe that such proceedings, individually and in the aggregate, when finally resolved, are not reasonably likely to have a material and adverse effect on our results of operations, financial position and cash flows.

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In April 2020, a short seller report was published by Wolfpack Research (the Wolfpack Report). In sum and substance, the Wolfpack Report alleges that iQIYI inflated its user numbers, inflated its revenue and deferred revenue in connection with certain parts of iQIYI’s business, inflated its expenses and the purchase prices of certain assets to conceal revenue inflation, and provided misleading financial statements of cash flows by adopting an incorrect accounting method. Following the publication of the Wolfpack Report, the SEC requested iQIYI to produce certain financial, operating, and other documents and records primarily relate to the allegations in the Wolfpack Report. In particular, the SEC requested that iQIYI voluntarily provide it with documents and information relating to, among other things, iQIYI’s organizational charts, accounting policies, and financial books and records from 2018 to the present, as well as documents relating to iQIYI’s acquisition or investments in certain entities mentioned in the Wolfpack Report and the valuation of those entities at the time of those transactions. On April 7, 2020, iQIYI publicly addressed the allegations contained in the Wolfpack Report in a press release on its website, noting that iQIYI “believes that the report contains numerous errors, unsubstantiated statements and misleading conclusions and interpretations regarding information relating to the Company.” iQIYI also reiterated that “it has always been and will remain committed to maintaining high standards of corporate governance and internal control, as well as transparent and timely disclosure in compliance with the applicable rules and regulations of the Securities and Exchange Commission and the Nasdaq Global Select Market.” On August 13, 2020, iQIYI issued another press release announcing its second quarter financial results, and also disclosed that the SEC’s Division of Enforcement is seeking the production of certain financial and operating records dating from January 1, 2018, as well as documents related to certain acquisitions and investments that were identified in a report issued the Wolfpack Report. In addition, iQIYI disclosed that shortly after the publication of the Wolfpack Report, iQIYI engaged professional advisers to conduct an internal review into certain of the key allegations in the Wolfpack Report and to report their findings to its audit committee. These professional advisers examined iQIYI’s books and records and undertook testing procedures that, in their judgment, were necessary and appropriate to evaluating the key allegations in the Wolfpack Report, including accounting policy analysis, data analytics on whether iQIYI manufactured orders and inflated revenues and/or expenses. On October 5, 2020, iQIYI publicly disclosed that the internal review within the agreed scope has been substantially completed and did not uncover any evidence that would substantiate the allegations. The SEC has also sought the production of certain documents and records from iQIYI related to such internal review and other related information. iQIYI is cooperating with the SEC. iQIYI has voluntarily and publicly disclosed the SEC’s request for information, and, through its legal counsel, it has been providing the SEC with requested documents and information. As a matter of U.S. law, as confirmed by iQIYI’s U.S. legal counsel, the initiation of a request for information is not a finding of fact or an indication by the SEC or its enforcement staff that any violation of the federal securities laws has occurred. We are unable to predict the timing, outcome, or consequences of the SEC investigation of iQIYI, or from the SEC’s review of the documents and records requested from iQIYI. Because the SEC has not charged iQIYI or any of its officers and directors with any wrongdoing, there is no factual basis to offer even a speculative prognosis as to what the “worst case scenario” may be. As advised by iQIYI’s U.S. legal counsel, successful enforcement actions by the SEC (which can pursue only civil and administrative, not criminal, remedies) against other companies in the past have typically resulted in civil fines and disgorgement and other equitable remedies such as injunctions to refrain from further violations of law. However, there is no basis to conclude at this point whether there will be an enforcement action brought against iQIYI, whether any such action will be successful, or what the “worst case scenario” will be.

Furthermore, starting in April 2020, iQIYI and certain of its current and former officers and directors were named as defendants in four federal putative securities class actions alleging that they made

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material misstatements and omissions in documents filed with the SEC regarding certain of the key allegations contained in the Wolfpack Report. Plaintiffs allege, in sum and substance, that iQIYI’s disclosures materially misled investors by: (i) overstating the number of iQIYI’s daily active users; (ii) overstating deferred revenue; (iii) overstating membership services revenue; (iv) overstating the amounts paid to acquire an equity interest in Xin’ai Sports; and (v) improperly recording as deferred revenue and revenue the non-cash portion of the purchase price paid, in the form of content and services, iQIYI purportedly will and has provided to Xin’ai Sports in exchange for its equity stake. Plaintiffs allege that these false and misleading statements artificially inflated the value of iQIYI’s securities and constituted violations of Sections 10(b) and 20(a) of the Securities and Exchange Act of 1934, and Sections 11 and 15 of the Securities Act of 1933. These cases remain in their preliminary stages, and the substantive allegations are subject to change as the litigations progress or if Plaintiffs file amended complaints. Because these actions remain in their preliminary stages, we cannot predict the timing, outcome or consequences of these federal actions. For similar reasons, there is not sufficient information to estimate the aggregate amount of monetary damages sought at this time, and plaintiffs have also not yet alleged the amount of monetary damages being sought. These four actions are captioned, respectively, as (i) *Lee v. iQIYI et al.*, No. 1:20-cv-01830-LDH-SJB (U.S. District Court for the Eastern District of New York, Amended Complaint filed Jan. 19, 2021) (the “*Lee Action*”); (ii) *Le Rivage LLC v. iQIYI, Inc. et al.*, No. 1:20-cv-03068 (U.S. District Court for the Eastern District of New York, filed June 15, 2020) (the “*Le Rivage Action*”); (iii) *Jenkins v. iQIYI et al.*, No. 1:20-cv-03068 (U.S. District Court for the Northern District of California, filed April 27, 2020) (the “*Jenkins Action*”); and (iv) *Shiferaw v. iQIYI, Inc. et al.*, No. 1:2020-cv-03115 (U.S. District Court for the Southern District of New York, filed April 17, 2020) (the “*Shiferaw Action*”). All four of these cases allege claims under Sections 10(b) and 20(a) of the Exchange Act and Rule 10b-5 promulgated thereunder, and the *Lee Action* also alleges claims under Sections 11 and 15 of the Securities Act. On June 15, 2020, plaintiffs in the *Shiferaw Action* (filed in the Southern District of New York) voluntarily dismissed their complaint. On July 9, 2020, the *Jenkins Action* (filed in the Northern District of California) was transferred to the U.S. District Court for the Eastern District of New York. On January 19, 2021, plaintiffs in the *Lee Action* (pending in the Eastern District of New York) filed their consolidated amended complaint, adding the Company and others as new defendants. Save for the *Shiferaw Action* which is dismissed, all actions remain in a preliminary stage. As confirmed by iQIYI’s U.S. legal counsel, iQIYI intends to vigorously defend itself against these claims, including by arguing that Plaintiffs have failed to state any claim as a matter of law. Based on the internal review overseen by iQiyi’s independent audit committee that had substantially been completed and which did not uncover any evidence that would substantiate the Wolfpack allegations, iQiyi believes that the Wolfpack allegations are without merit.

Starting in August 2020, we and certain of our current officers were named as defendants in two federal putative securities class actions alleging that defendants made material misstatements and omissions in documents filed with the SEC regarding certain of the key allegations contained in the Wolfpack Report. Both cases allege claims under Sections 10(b) and 20(a) of the Exchange Act and Rule 10b-5 promulgated thereunder and remain in their preliminary stages.

Because all of the ongoing securities class actions against iQIYI or Baidu are in their preliminary stages, the parties have not yet requested nor produced any discovery or admissible evidence to support or refute plaintiffs’ allegations. Nor has any court yet ruled on whether the plaintiffs have sufficiently stated a claim to relief under the relevant federal securities laws. Accordingly, there is no factual basis to offer even a speculative prognosis as to what the “worst case scenario” may be. In general, all of the aforementioned ongoing securities class actions seek monetary damages under the U.S. Securities Act of 1933 and/or the U.S. Securities Exchange Act of 1934 for alleged damages incurred as a result of

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defendants’ alleged misstatements or omissions in various public disclosures. In the view of the Directors, which is based on Baidu’s and iQIYI’s U.S. legal counsel, in the event that a court finds that iQIYI, Baidu and/or other defendants violated any of these securities laws, or in the event that iQIYI, Baidu and/or other defendants choose to reach a settlement with plaintiffs, iQIYI and/or Baidu may be liable for civil monetary damages and the potential financial, operational and reputational impact on iQIYI and/or Baidu may be material. However, we cannot predict the timing, outcome or consequences of these class actions, and there is no basis to conclude at this point whether such actions will be successful or whether the Company will be subject to any damages, let alone how much.

Unrelated to the Wolfpack Report, we and certain of our current officers were also named as defendants in a federal putative securities class action alleging that defendants made material misstatements and omissions in documents filed with the SEC relating to contents on our platform. In this lawsuit, filed in or about April 2020, plaintiffs allege, in sum and substance, that the Company’s disclosures were materially false or misleading as they misrepresented Baidu’s ability to monitor and filter illicit or improper content on its platform, and failed to disclose alleged investigations and violations of PRC regulatory requirements relating to the monitoring or filtering of illicit or improper content online. Plaintiffs allege that these false and misleading statements constituted violations of Sections 10(b) and 20(a) of the Securities and Exchange Act of 1934. The case remains at a preliminary stage, with the parties awaiting the Court’s ruling on a motion-to-dismiss, and the Company is therefore unable to predict the potential or likely outcome, or “worst case scenario,” of this litigation.

We and iQIYI will have to defend against these putative securities class action lawsuits, as applicable, including any appeals of such lawsuits should our or iQIYI’s initial defense be unsuccessful. We are currently unable to estimate the possible outcome or loss or possible range of loss, if any, associated with the resolution of these lawsuits. In the event that our or iQIYI’s initial defense of these lawsuits is unsuccessful, we cannot assure you that we or iQIYI will prevail in any appeal. Any adverse outcome of these cases, including any plaintiff’s appeal of a judgment in these lawsuits, could have a material adverse effect on our or iQIYI’s business, financial condition, results of operation, cash flows, and reputation. Similarly, we are currently unable to predict the timing, outcome, or consequences of the SEC investigation of iQIYI, or from the SEC’s review of the documents and records requested from iQIYI. The litigation or SEC investigation process may utilize a significant portion of our or iQIYI’s resources and divert management’s attention from the day-to-day operations, all of which could harm our business.

The Joint Sponsors have conducted independent due diligence in relation to the above class action lawsuits, including but not limited to, independent background, litigation and bring-down searches, as well as inquiries with the management, to understand the latest status of the class actions. Based on the due diligence conducted by the Joint Sponsors, nothing material has come to the Joint Sponsors’ attention to disagree with the Company’s view on the materiality of such class actions.

In the opinion of our PRC Legal Adviser, except as disclosed in the “Risk Factors” section in this document, our Significant Subsidiaries incorporated in the PRC were in compliance with relevant PRC laws and regulations in all material aspects during the Track Record Period. For the risks related to anti-monopoly matters such as failure to file prior notification of concentrations of undertaking, please see “Risk Factors—Risks Related to Doing Business in China—Any failure or perceived failure by us to comply with the enacted Anti-Monopoly Guidelines for Internet Platforms and other anti-monopoly laws and regulations may result in governmental investigations or enforcement actions, litigation or claims against us and could have an adverse effect on our business, financial condition and results of operations.” and “—PRC regulations establish complex procedures for some acquisitions conducted by

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foreign investors, which could make it more difficult for us to pursue growth through acquisitions in China.” As of the date of this document, we are unable to predict SAMR’s position toward our transactions related to such concentrations of undertaking. Because the PRC Anti-Monopoly Law gives SAMR wide latitude in imposing penalties including asset divestiture, restoring market competition, financial fines, among others, we are not able to predict exactly what penalties SAMR would impose on us, if we were deemed as failing to file prior notification of concentrations of undertaking. However, based on current applicable laws and regulations and with reference to precedents of failure-of-notification including the three recent cases involving VIE structure, SAMR so far has only imposed financial fines of no higher than RMB500,000 for each transaction constituting failure to file notification of concentrations of undertaking. Therefore, we believe it is reasonable to estimate that SAMR may only impose on us a financial fine of not higher than RMB500,000 for each transaction constituting failure of filing prior notification of concentrations of undertaking. Our Directors believe that such financial fines would not have a material adverse effect on our financial and business operations. In the opinion of the PRC Legal Adviser, although failure of filing prior notification of concentrations of undertaking may subject us to fines of up to RMB500,000 per case, and in the most extreme case being ordered to terminate the contemplated concentration, to dispose of our equity or assets within a prescribed period, to transfer our business within a prescribed time or to take any other necessary measures to return to the pre-concentration status, such measures other than financial fines have never been instituted by SAMR in any previous case; with reference to all past failure-of-notification precedents including the three recent cases involving VIE structure, the likelihood that SAMR orders us to terminate any contemplated concentration, dispose of its equity or assets, or transfer its business is relatively low. Based on our assessment, the non-compliance as set out in such risk factors, if raised by the relevant competent authorities and determined against us, would not have a material adverse effect on the business operation and finance of our Company.

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The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and the related notes included in the Accountants’ Report in Appendix IA, in “Our Business.” This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results and the timing of selected events could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set out under “Risk Factors” and elsewhere in this document. We have prepared our consolidated financial statements in accordance with U.S. GAAP. Our fiscal year ends on December 31 and references to fiscal years 2018, 2019 and 2020 are to the fiscal years ended December 31, 2018, 2019 and 2020, respectively.

Overview

We are a leading technology company with world-class artificial intelligence (AI) capabilities. We were founded to enable people to quickly find relevant information on the Internet, amidst the huge volume of information generated daily. As the gateway to the Internet, we connect our users to a large information and knowledge-centric content and services ecosystem through our open search-plus-feed platform. Years of tagging, understanding and intelligently processing all forms of content on the Internet with AI—text, images and videos—has helped us build and refine our unique AI capabilities and develop Baidu Brain, our core AI technology engine. Baidu Brain in turn has enabled us to further develop leading AI technologies and commercialize them through products and services for consumers, enterprises and the public sector.

Our operations are primarily conducted in China, and revenues are primarily generated from China. Our total revenues increased by 5% from RMB102.3 billion in 2018 to RMB107.4 billion in 2019. Our total revenues were RMB107.1 billion (US\$16.4 billion) in 2020, which was basically flat from 2019. Our operating profit decreased by 59% from RMB15.5 billion in 2018 to RMB6.3 billion in 2019, and increased by 127% from RMB6.3 billion in 2019 to RMB14.3 billion (US\$2.2 billion) in 2020. Net income attributable to Baidu, Inc. decreased by 93% from RMB27.6 billion in 2018 to RMB2.1 billion in 2019, and increased by 992% from RMB2.1 billion in 2019 to RMB22.5 billion (US\$3.4 billion) in 2020. Net income attributed to Baidu, Inc. in 2019 included a non-cash impairment loss of RMB8.9 billion from investment in Trip.com.

Rule 13.46(2) of the Hong Kong Listing Rules requires an overseas issuer to send an annual report or a summary financial report within four months after the end of the financial year to which the report relates. As an issuer seeking a listing as a Grandfathered Greater China Issuer pursuant to Chapter 19C of the Hong Kong Listing Rules, we are not subject to the disclosure requirements under notes 4(a) and (b) to Rule 13.46(2) of the Hong Kong Listing Rules. As this document already includes the financial information of the Company for the year ended December 31, 2020, the Company will not separately prepare and send an annual report to its shareholders for the year ended December 31, 2020, which will not be in breach of its constitutional documents, laws and regulations of the Cayman Islands or other regulatory requirements.

Selected Statements of Operations Items

Revenues

Revenue Generation

Baidu Core. Baidu Core revenues primarily comprise of (i) auction-based P4P online marketing services that include search and feed online marketing services; (ii) other online marketing services,

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including display advertisement, based on performance criteria other than CPC; (iii) cloud services and solutions; (iv) non-marketing consumer-facing services such as membership, live streaming and online games; (v) intelligent driving; and (vi) smart devices and services. We expect Baidu Core to continually earn a majority of our revenues.

A majority of Baidu Core’s revenues are derived from P4P services. Our P4P platform is an online marketplace that introduces internet search users to customers, who pay us a fee based on click-throughs for priority placement of their links in the search results. We also provide feed online marketing services to our customers. Our feed platform helps customers target relevant feed users, and customers pay us based on a CPC basis or advertisement displays of their products. In addition, we provide our customers with other performance-based and display-based online marketing services.

Apart from the online marketing services, we derive revenue for Baidu Core by providing products and services ranging from cloud services and solutions, non-marketing consumer-facing services, intelligent driving and smart devices and services.

iQIYI. iQIYI is an innovative market-leading online entertainment service in China. iQIYI’s platform features iQIYI original content, as well as a comprehensive library of other professionally produced content (PPC), professional user generated content (PUGC) and user-generated content. iQIYI derives a majority of its revenues from membership services and online marketing services.

iQIYI offers membership packages to provide its members with (i) access to streaming of a library of premium content, (ii) certain commercial skipping and other viewing privileges, (iii) merchandise selection and privilege, and (iv) higher community status in iQIYI Paopao social platform. Most of iQIYI’s online marketing services are in the form of brand advertising.

Operating Costs and Expenses

Our operating costs and expenses consist of cost of revenues, selling, general and administrative expenses, and research and development expenses. Share-based compensation expenses are allocated among these three categories, based on the nature of the work of the employees who have received share-based compensation.

Cost of Revenues

Our cost of revenues primarily consist of content costs, traffic acquisition costs, depreciation costs, costs of goods sold, bandwidth costs and other cost of revenues.

Selling, General and Administrative Expenses

Our selling, general and administrative expenses primarily consist of promotional and marketing expenses, salaries and benefits for our sales, marketing, general and administrative personnel, and legal, accounting and other professional services fees.

Research and Development Expenses

Research and development expenses primarily consist of salaries and benefits for research and development personnel. We expense research and development costs as they are incurred, except for capitalized software development costs that fulfill the capitalization criteria under Accounting Standards Codification (“ASC”).

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Taxation

Cayman Islands and British Virgin Islands

We are not subject to income or capital gain tax under the current laws of the Cayman Islands and the British Virgin Islands. Additionally, upon payments of dividends by us, no Cayman Islands withholding tax will be imposed.

Hong Kong

Subsidiaries in Hong Kong are subject to the uniform tax rate of 16.5% and foreign-derived income is exempted from income tax. There is no withholding tax in Hong Kong on remittance of dividends.

Japan

As a result of the Japanese tax regulations amendments, the effective income tax rates are approximately 31%, 31% and 31% for the years ended December 31, 2018, 2019 and 2020, respectively.

PRC Enterprise Income Tax

Effective from January 1, 2008 and amended on December 29, 2018, the PRC’s statutory enterprise income tax, or EIT, rate is 25%. An enterprise may benefit from a preferential tax rate of 15% under the EIT Law if it qualifies as a “High and New Technology Enterprise” strongly supported by the state. A “High and New Technology Enterprise” certificate is effective for a period of three years. A number of our PRC subsidiaries and consolidated affiliated entities, such as Baidu Netcom, obtained the “High and New Technology Enterprise” certificates. The related tax holiday under such “High and New Technology Enterprise” certificates of these entities will expire in 2022 and 2023.

If any entity fails to maintain the “High and New Technology Enterprise” qualification under the EIT Law, its tax rate will increase, which could have a material and adverse effect on our results of operations and financial position. Historically, all of the PRC subsidiaries and consolidated affiliated entities mentioned above successfully re-applied for the certificates when the prior ones expired.

An enterprise may benefit from a tax exemption or preferential tax rate of 10% under the EIT law if it qualifies as a “Key Software Enterprise.” Enterprises wishing to enjoy the “Key Software Enterprise” status will be subject to relevant governmental authorities’ assessment each year as to whether they are entitled to the tax exemption or preferential tax rate of 10%. Due to the “Key Software Enterprise” status, Baidu Online was entitled to a preferential income tax rate of 10% from 2010 to 2019, so was Baidu China from 2015 to 2019, and Baidu International from 2016 to 2019. The “Key Software Enterprise” status of Baidu Online, Baidu China and Baidu International for 2020 will be filed with tax authorities before May 2021 and will be subject to relevant governmental authorities’ assessment.

If our PRC subsidiaries or consolidated affiliated entities that have enjoyed preferential tax treatment no longer qualify for the preferential treatment, we will consider available options under applicable law that would enable us to qualify for alternative preferential tax treatment. To the extent we are unable to offset the impact of the expiration of existing preferential tax treatment with new tax exemptions, tax incentives or other tax benefits, the expiration of existing preferential tax treatment may cause our effective tax rate to increase. The amount of income tax payable by our PRC subsidiaries and consolidated affiliated entities in the future will depend on various factors, including, among other things, the results of operations and taxable income of, and the statutory tax rate applicable to, each of the entities. Our effective tax rate depends partially on the extent of the relative contribution of each of our subsidiaries and consolidated affiliated entities to our consolidated taxable income.

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Withholding Tax

Under the EIT Law and its implementation rules, dividends, interests, rent or royalties payable by a foreign-invested enterprise, such as our PRC subsidiaries, to any of its non-resident enterprise investors, and proceeds from any such non-resident enterprise investor’s disposition of assets (after deducting the net value of such assets) are subject to the EIT at the rate of 10%, namely withholding tax, unless the non-resident enterprise investor’s jurisdiction of incorporation has a tax treaty or arrangement with China that provides for a reduced withholding tax rate or an exemption from withholding tax.

The British Virgin Islands, where Baidu Holdings Limited, the sole shareholder of certain of our PRC subsidiaries such as Baidu Online, was incorporated, does not have such a tax treaty with China.

Hong Kong, where Baidu (Hong Kong) Limited, our wholly owned subsidiary and the sole shareholder of certain of our PRC subsidiaries such as Baidu Times and Baidu China, was incorporated, has a tax arrangement with China that provides for a lower withholding tax rate of 5% on dividends subject to certain conditions and requirements, such as the requirement that the Hong Kong resident enterprise own at least 25% of the PRC enterprise distributing the dividend at all times within the 12-month period immediately preceding the distribution of dividends and be a “beneficial owner” of the dividends.

In 2020, certain of our PRC subsidiaries have declared and distributed profits earned to Baidu (Hong Kong) Limited, the dividend payments are subject to withholding tax. We have made tax provisions based on the corresponding tax rate. If our PRC subsidiaries further declare and distribute profits earned after January 1, 2008 to us in the future, the dividend payments will be subject to withholding tax, which will increase our tax liability and reduce the amount of cash available to our company. For the potential distributable profits to be distributed to our qualified Hong Kong incorporated subsidiary, the deferred tax liabilities are accrued at a 5% withholding tax rate. For more information on related risks, please see “Risk Factors—Risks Related to Doing Business in China—If our PRC subsidiaries declare and distribute dividends to their respective offshore parent companies, we will be required to pay more taxes, which could have a material and adverse effect on our result of operations.”

Tax Residence

Under the EIT Law and its implementation rules, an enterprise established outside of the PRC with “de facto management body” within the PRC is considered a resident enterprise and will be subject to the EIT at the rate of 25% on its worldwide income. The term “de facto management body” refers to “the establishment that exercises substantial and overall management and control over the production, business, personnel, accounts and properties of an enterprise.”

If our offshore entities are deemed PRC resident enterprises, these entities may be subject to the EIT at the rate of 25% on their global incomes, except that the dividends distributed by our PRC subsidiaries may be exempt from the EIT to the extent such dividends are deemed “dividends among qualified resident enterprises.” For more information on related risks, please see “Risk Factors—Risks Related to Doing Business in China—We may be deemed a PRC resident enterprise under the EIT Law, which could subject us to PRC taxation on our global income, and which may have a material and adverse effect on our results of operations.”

Should our offshore entities be deemed as PRC resident enterprises, such changes could significantly increase our tax burden and materially and adversely affect our cash flow and profitability.

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PRC VAT in Lieu of Business Tax

All of our PRC entities have been subject to VAT since August 1, 2013. These entities are required to pay VAT instead of business tax for services that are deemed by the relevant tax authorities to be within the pilot industries at a rate of 6%. In addition, cultural business construction fee is imposed at the rate of 3% on revenues derived from our advertisement distribution services, and we are entitled to a 50% reduction of cultural business construction fee from July 1, 2019 to December 31, 2024 and an exemption of cultural business construction fee from January 1, 2020 to December 31, 2020.

PRC Urban Maintenance and Construction Tax and Education Surcharge

Any entity, foreign-invested or purely domestic, or individual that is subject to consumption tax, VAT and business tax is also required to pay PRC urban maintenance and construction tax. The rates of urban maintenance and construction tax are 7%, 5% or 1% of the amount of consumption tax, VAT and business tax actually paid depending on where the taxpayer is located. All entities and individuals who pay consumption tax, VAT and business tax are also required to pay education surcharge at a rate of 3%, and local education surcharges at a rate of 2%, of the amount of VAT, business tax and consumption tax actually paid.

Impact of COVID-19 on Our Operations

Our results of operations have been, and could continue to be adversely, and may be materially, affected, to the extent that the COVID-19 or any other epidemic harms the Chinese and global economy in general. Any potential impact to our results will depend on, to a large extent, future developments and new information that may emerge regarding the duration and severity of the COVID-19 and the actions taken by government authorities and other entities to contain the COVID-19 or treat its impact, almost all of which are beyond our control.

The potential downturn brought by and the duration of the COVID-19 pandemic may be difficult to assess or predict where actual effects will depend on many factors beyond our control. The extent to which the COVID-19 pandemic impacts our long-term results remains uncertain, and we are closely monitoring its impact on us. During the year ended December 31, 2020, our operations have been significantly affected by the COVID-19 pandemic. Our online marketing revenues declined compared to the prior period mainly due to weakness in online marketing demand as our customers in certain industries are negatively impacted by COVID-19. We have also provided additional allowance for credit losses for accounts receivable and contract assets, recognized impairment charges on our long-term investments and content assets, and recorded loss from equity method investments in the year ended December 31, 2020, due to the impact of COVID-19 and other factors. In addition, increased market volatility has contributed to larger fluctuations in the valuation of our equity investments. There are still significant uncertainties of COVID-19's future impact, and the extent of the impact will depend on a number of factors, including the duration and severity of COVID-19, possibility of new waves in China and other countries, the development and progress of distribution of COVID-19 vaccine and other medical treatment, the potential change in user behavior, especially on internet usage due to the prolonged impact of COVID-19, the actions taken by government authorities, particularly to contain the outbreak, stimulate the economy to improve business condition especially for SMEs, almost all of which are beyond our control. As a result, certain of our estimates and assumptions, including the allowance for credit losses, the valuation of certain debt and equity investments, long-term investments, content assets and long-lived assets subject to impairment assessments, require significant judgments and carry a higher degree of variabilities and volatilities that could result in material changes to our current estimates in future periods. See also “Risk Factors—Risks Related to

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Our Business and Industry—We face risks related to health epidemics, severe weather conditions and other outbreaks.”

Results of Operations

The following table sets forth a summary of our consolidated results of operations for the periods indicated. The period-to-period comparisons of results of operations should not be relied upon as indicative of future performance.

| | Year ended December 31, | | | |
|--|-------------------------|----------------|----------------|---------------|
| | 2018 | 2019 | 2020 | |
| | RMB | RMB | RMB | US\$ |
| | (in millions) | | | |
| Revenues: | | | | |
| Online marketing services | 81,912 | 78,093 | 72,840 | 11,163 |
| Others | 20,365 | 29,320 | 34,234 | 5,247 |
| Total revenues | 102,277 | 107,413 | 107,074 | 16,410 |
| Operating costs and expenses⁽¹⁾: | | | | |
| Cost of revenues | 51,744 | 62,850 | 55,158 | 8,454 |
| Selling, general and administrative | 19,231 | 19,910 | 18,063 | 2,769 |
| Research and development | 15,772 | 18,346 | 19,513 | 2,989 |
| Total operating costs and expenses | 86,747 | 101,106 | 92,734 | 14,212 |
| Operating profit | 15,530 | 6,307 | 14,340 | 2,198 |
| Total other income (loss), net | 11,795 | (6,647) | 8,750 | 1,341 |
| Income (loss) before income taxes | 27,325 | (340) | 23,090 | 3,539 |
| Income taxes | 4,743 | 1,948 | 4,064 | 623 |
| Net income (loss) | 22,582 | (2,288) | 19,026 | 2,916 |
| Less: Net loss attributable to non-controlling interests | (4,991) | (4,345) | (3,446) | (528) |
| Net income attributable to Baidu, Inc. | 27,573 | 2,057 | 22,472 | 3,444 |

Note:

(1) Share-based compensation expenses are allocated in operating costs and expenses as follows:

| | | | | |
|---|--------------|--------------|--------------|--------------|
| Cost of revenues | 224 | 327 | 360 | 55 |
| Selling, general and administrative | 1,725 | 1,768 | 1,897 | 290 |
| Research and development | 2,727 | 3,531 | 4,471 | 686 |
| Total | 4,676 | 5,626 | 6,728 | 1,031 |

Year Ended December 31, 2020 Compared to Year Ended December 31, 2019

Consolidated revenues. Our total revenues in 2020 were RMB107.1 billion (US\$16.4 billion), which was basically flat from 2019.

Our online marketing revenues for Baidu Core in 2020 were RMB66.3 billion (US\$10.2 billion), decreasing by 5% from 2019.

Our online marketing revenues for iQIYI in 2020 were RMB6.8 billion (US\$1.0 billion), decreasing by 18% from 2019.

Other revenues in 2020 were RMB34.2 billion (US\$5.2 billion), increasing by 17% from 2019.

For a detailed description, see “Segment Revenues.”

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Consolidated operating costs and expenses. Our total operating costs and expenses decreased by RMB8.4 billion, or 8%, from RMB101.1 billion 2019 to RMB 92.7 billion (US\$14.2 billion) in 2020.

Cost of revenues. Our cost of revenues decreased by RMB7.7 billion from RMB62.9 billion in 2019 to RMB55.2 billion (US\$8.5 billion) in 2020, primarily due to the following factors:

- A decrease of RMB2.7 billion in traffic acquisition costs, which reflected decreasing union revenues, as we focused on growing in-app search and optimizing profitability over union revenue growth.
- A decrease of RMB1.7 billion in sales tax and surcharges, which resulted from an exemption of cultural business construction fee for 2020.
- A decrease of RMB1.6 billion in content cost, which related to less recorded expense of produced content, more shorter-length content with less total costs to satisfy diversified users demand, as well as revisions to accounting estimates of future viewership consumption patterns and useful lives of content assets.

Selling, general and administrative expenses. Our selling, general and administrative expenses decreased by RMB1.8 billion from RMB19.9 billion in 2019 to RMB18.1 billion (US\$2.8 billion) in 2020, primarily due to a decrease of RMB2.1 billion in channel spending and promotional marketing which reflected our effort to optimize marketing spending during COVID-19 pandemic, especially for the first half of 2020.

Research and development expenses. Our research and development expenses increased by RMB1.2 billion from RMB18.3 billion in 2019 to RMB19.5 billion (US\$3.0 billion) in 2020, primarily due to an increase of RMB1.5 billion in personnel-related expenses, which was in line with the growth in research and development headcount as we continue to strengthen our research and development effort.

Operating profit. As a result of the foregoing, we generated an operating profit of RMB14.3 billion (US\$2.2 billion) in 2020, a 127% increase from RMB6.3 billion in 2019.

Total other income (loss), net. Our total other income, net was RMB8.8 billion (US\$1.3 billion) in 2020, which included fair value gain of RMB11.6 billion from long-term investments. Total other loss, net was RMB6.6 billion for 2019, which included a non-cash impairment loss of RMB8.9 billion from investment in Trip.com.

Income taxes. Our income tax expenses was RMB4.1 billion (US\$623 million) in 2020, compared to RMB1.9 billion in 2019.

Net income attributable to Baidu, Inc. As a result of the foregoing, net income attributable to Baidu, Inc. increased from RMB2.1 billion in 2019 to RMB22.5 billion (US\$3.4 billion) in 2020.

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

Consolidated revenues. Our total revenues in 2019 were RMB107.4 billion, growing by 5% from 2018.

Online marketing revenues for Baidu Core in 2019 were RMB70.0 billion decreasing by 4% from 2018.

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Online marketing revenues for iQIYI in 2019 were RMB8.3 billion, decreasing by 11% from 2018.

Other revenues in 2019 were RMB29.3 billion, increasing by 44% from 2018.

For a detailed description, see “Segment Revenues.”

Consolidated operating costs and expenses. Our consolidated operating costs and expenses in 2019 were RMB101.1 billion, increasing by RMB14.4 billion, or 17%, from RMB86.7 billion 2018. This increase was primarily due to the expansion of our business.

Cost of revenues. Our cost of revenues in 2019 were RMB62.9 billion, increasing by RMB11.2 billion from RMB51.7 billion 2018, primarily due to the following factors:

- An increase of RMB3.3 billion in depreciation and bandwidth costs, resulted from increased investment in infrastructure.
- An increase of RMB3.1 billion in cost of goods sold, which was in line with the growth in sales of Xiaodu smart devices.
- An increase of RMB2.0 billion in content costs, resulted from iQIYI’s higher content costs recorded relating to licensed copyrights and produced content as iQIYI continued to invest in comprehensive and diversified content library.
- An increase of RMB1.5 billion in traffic acquisition costs, resulted from increasing TAC prices.

Selling, general and administrative expenses. Our selling, general and administrative expenses increased slightly by RMB679 million from RMB19.2 billion in 2018 to RMB19.9 billion in 2019.

Research and Development Expenses. Our research and development expenses increased by RMB2.5 billion from RMB15.8 billion in 2018 to RMB18.3 billion in 2019, primarily due to an increase of RMB2.3 billion in research and development personnel related expenses, which was in line with the growth in research and development headcount.

Operating profit. As a result of the foregoing, we generated an operating profit of RMB6.3 billion in 2019, a 59% decrease from RMB15.5 billion in 2018.

Total other income (loss), net. Our total other loss, net was RMB6.6 billion in 2019, compared to total other income, net of RMB11.8 billion in 2018. Total other loss, net in 2019 mainly comprises non-cash impairment loss on equity investment arising from other-than-temporary decline. In 2019, the market value of the shares of Trip.com declined, and the continuing low market price caused us to recognize a non-cash impairment loss of RMB8.9 billion in the third quarter of 2019. In October 2019, we sold a portion of our holding in Trip.com, reducing the interest of outstanding shares of Trip.com from 19% to 12%. Total other income, net in 2018 mainly comprises gains from the disposal of Du Xiaoman (financial services business) and fair value gains on private company equity investments without readily determinable fair values in accordance with ASC 321.

Income taxes. Our income tax expense was RMB1.9 billion in 2019, a 59% decrease from RMB4.7 billion in 2018. The decrease in income tax expense was mainly due to lower profit before income tax from Baidu Core.

Net loss attributable to non-controlling interests. Net loss attributable to non-controlling interests was RMB4.3 billion in 2019, compared to RMB5.0 billion in 2018.

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Net income attributable to Baidu, Inc. As a result of the foregoing, net income attributable to Baidu, Inc. decreased from RMB27.6 billion in 2018 to RMB2.1 billion in 2019.

Segment Revenues

The following table sets forth our revenues by segment and the year-over-year change rate for the periods indicated, with each segment revenues including inter-segment revenues:

| | Year ended December 31, | | | | | |
|---|-----------------------------------|----------------|-----------|----------------|---------------|------------|
| | 2018 | 2019 | | 2020 | | |
| | RMB | RMB | YoY% | RMB | US\$ | YoY% |
| | (In millions, except percentages) | | | | | |
| Baidu Core: | | | | | | |
| Online marketing services | 72,645 | 70,038 | (4) | 66,283 | 10,158 | (5) |
| Cloud services | 3,005 | 6,370 | 112 | 9,173 | 1,406 | 44 |
| Interest income earned from provision of financial services | 1,724 | — | (100) | — | — | — |
| Others | 897 | 3,303 | 268 | 3,228 | 495 | (2) |
| Subtotal | 78,271 | 79,711 | 2 | 78,684 | 12,059 | (1) |
| iQIYI: | | | | | | |
| Online advertising services | 9,329 | 8,271 | (11) | 6,822 | 1,046 | (18) |
| Membership services | 10,623 | 14,436 | 36 | 16,491 | 2,527 | 14 |
| Content distribution | 2,163 | 2,544 | 18 | 2,660 | 408 | 5 |
| Others | 2,874 | 3,743 | 30 | 3,734 | 572 | (0) |
| Subtotal | 24,989 | 28,994 | 16 | 29,707 | 4,553 | 2 |
| Intersegment eliminations | (983) | (1,292) | 31 | (1,317) | (202) | 2 |
| Total revenue | 102,277 | 107,413 | 5 | 107,074 | 16,410 | (0) |

Baidu Core

Baidu Core revenue was RMB78.7 billion (US\$12.1 billion) in 2020, decreasing by RMB1.0 billion, or 1%, from RMB79.7 billion in 2019.

Our online marketing revenues for Baidu Core in 2020 were RMB66.3 billion (US\$10.2 billion), decreasing by RMB3.7 billion, or 5%, compared to RMB70.0 billion in 2019, mainly due to weakness in online marketing services demand, as our customers in industries that were negatively impacted by the COVID-19 outbreak and other factors, including healthcare, franchising, travel, financial services and education, reduced their budgets on online marketing.

The number of our active online marketing customers decreased from approximately 528,000 in 2019 to approximately 505,000 in 2020, while the average revenue per customer decreased slightly from approximately RMB132,700 in 2019 to approximately RMB131,300 (US\$20,120) in 2020. The decrease of our active online marketing customers was primarily due to quarantines, travel restrictions, and the temporary closure of businesses and facilities and resulting impact to general economy brought by the COVID-19 pandemic.

Revenue from Baidu cloud services, interest income earned from provision of financial services, and others are included in “Other revenue” in the statements of comprehensive income (loss).

Baidu Core’s cloud services revenue in 2020 were RMB9.2 billion (US\$1.4 billion), increasing by RMB2.8 billion, or 44%, compared to RMB6.4 billion in 2019, due to the rapid adoption of our cloud service and products.

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Baidu Core’s other revenues were RMB3.2 billion (US\$495 million) in 2020, decreasing by RMB75 million, or 2%, compared to RMB3.3 billion in 2019.

Baidu Core revenue was RMB79.7 billion in 2019, increasing by RMB1.4 billion, or 2%, from RMB78.3 billion in 2018.

Online marketing revenues for Baidu Core in 2019 were RMB70.0 billion, decreasing by RMB2.6 billion, or 4%, from RMB72.6 billion in 2018, mainly due to weakness in healthcare, financial services and auto/logistics sectors, offset by strength in education, retail/e-commerce, travel and network services sectors. During 2019, we implemented an initiative in an attempt to require healthcare marketing customers to move their landing sites onto our Managed Page. Requiring healthcare customers to adopt our structured data solution allows us to better monitor the content they offer and increase consumer trust. In addition, certain sectors, such as financial services, were impacted by industry-specific policy changes and slowing macroeconomic environment. These changes dampened revenue growth, compared to the year before.

The number of our active online marketing customers increased from approximately 526,000 in 2018 to approximately 528,000 in 2019, while the average revenue per customer decreased from approximately RMB138,100 in 2018 to approximately RMB132,700 in 2019. In 2018, we began to wind down our local express business, which provided merchants with a turn-key solution to participate in our online marketing and transaction services, leading certain vendors discontinuing their business with us in 2018 and 2019. Excluding the impact of local express business, the number of our active online marketing customers increased from approximately 507,000 in 2018 to approximately 524,000 in 2019.

Our active customers of online marketing services in a given period are defined as those persons or entities that purchase at least one of Baidu Core’s online marketing services during the same period. The definition has been refined from the one used in 2017 annual report to better reflect how the management is evaluating our operating results. The number of our active online marketing customer and the average revenue per customer has been presented on a consistent basis in Track Record Period.

Baidu Core’s cloud services revenue in 2019 were RMB6.4 billion, increasing by RMB3.4 billion, or 112%, compared to RMB3.0 billion in 2018, due to the rapid adoption of our cloud services and products.

Interest income earned from provision of financial services were nil in 2019, decreased from RMB1.7 billion in 2018, as we divested our financial services business in August 2018.

Other revenues for Baidu Core in 2019 were RMB3.3 billion, increasing by RMB2.4 billion, or 268% from RMB897 million in 2018, primarily due to the increase in revenue from sales of our Xiaodu smart devices.

iQIYI

iQIYI revenue was RMB29.7 billion (US\$4.6 billion) in 2020, increasing by RMB713 million, or 2%, from RMB29.0 billion in 2019.

iQIYI online advertising services revenue are included in “Online marketing revenue” in the consolidated statements of comprehensive income (loss).

iQIYI’s online advertising revenues in 2020 were RMB6.8 billion (US\$1.0 billion), decreasing by RMB1.5 billion, or 18%, from RMB8.3 billion in 2019, as a result of the challenging macroeconomic

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environment in China, and the tightened advertising budget of advertisers and intensified competition in advertising business, as well as the tightened regulatory environment and the uncertainty of certain content scheduling in the early stage of COVID-19 pandemic in the first quarter of 2020. However, iQIYI’s online advertising services revenue has been rebounding since the second quarter of 2020 as iQIYI’s advertisers gradually recovered their advertising budgets. Average brand advertising revenue per brand advertiser increased by 11% from RMB5.9 million in 2019 to RMB6.6 million (US\$1.0 million) in 2020.

Revenue from iQIYI membership services, content distribution, and others are included in “Other revenue” in the statements of comprehensive income (loss).

Membership revenue of iQIYI in 2020 were RMB16.5 billion (US\$2.5 billion), increasing by RMB2.1 billion, or 14%, compared to RMB14.4 billion in 2019, primarily driven by (i) an increase in the average revenue per user due to the increase in the members’ willingness to pay for the premium content that iQIYI have been offering, and (ii) the relatively stable number of subscribing members of 101.7 million in 2020 as compared with 106.9 million in 2019.

iQIYI content distribution revenue increased by 5% from RMB2.5 billion in 2019 to RMB2.7 billion (US\$408 million) in 2020, primarily caused by the increase of high-quality content which fulfilled distribution to several platforms.

iQIYI other revenue for iQIYI was RMB3.7 billion (US\$572 million), which remained stable as compared to RMB3.7 billion in 2019.

iQIYI revenue was RMB29.0 billion in 2019, increasing by RMB4.0 billion, or 16% from RMB25.0 billion in 2018.

Online advertising revenues for iQIYI in 2019 were RMB8.3 billion, decreasing by RMB1.0 billion, or 11%, from RMB9.3 billion in 2018, primarily due to the challenging macroeconomic environment, the delay of certain content launches and intensified competition in the advertising business. Average brand advertising revenue per brand advertiser decreased by 12% from RMB6.7 million in 2018 to RMB5.9 million in 2019.

iQIYI membership services were RMB14.4 billion in 2019, increasing by RMB3.8 billion, or 36%, from RMB10.6 billion in 2018, which was primarily due to the growth of iQIYI subscribing members from 87.4 million in 2018 to 106.9 million in 2019.

iQIYI content distribution revenues were RMB2.5 billion in 2019, increasing by RMB381 million, or 18%, from RMB2.2 billion in 2018, primarily caused by an increased average transaction amount of premium content titles.

iQIYI other revenues were RMB3.7 billion in 2019, increasing by RMB869 million, or 30%, from RMB2.9 billion in 2018, primarily as a result of the growth of a number of business verticals, especially the growth of our game business after the acquisition of Skymoos.

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Segment Operating Costs and Expenses

The following table sets forth our operating costs and expenses by segment and the year-over-year change rate for the periods indicated, with each segment operating costs and expenses including inter-segment costs and expenses:

| | Year ended December 31, | | | | | |
|--------------------------------------|-----------------------------------|--------|------|--------|-------|------|
| | 2018 | 2019 | | 2020 | | |
| | RMB | RMB | YoY% | RMB | US\$ | YoY% |
| | (In millions, except percentages) | | | | | |
| Operating Costs and Expenses: | | | | | | |
| Baidu Core | 54,463 | 64,450 | 18 | 58,146 | 8,911 | (10) |
| iQIYI | 33,295 | 38,252 | 15 | 35,748 | 5,478 | (7) |

Baidu Core. Operating costs and expenses of Baidu Core mainly consist of personnel-related costs, traffic acquisition costs, marketing and promotion spending, depreciation expenses, costs of goods sold, content costs, bandwidth cost and sales tax and surcharges.

Cost of revenues

The cost of revenues of Baidu Core decreased by 17% from RMB34.0 billion in 2019 to RMB28.4 billion (US\$4.3 billion) in 2020, primarily due to a decrease in traffic acquisition costs, sales tax and surcharges and costs of goods sold.

The cost of revenues of Baidu Core increased by 34% from RMB25.4 billion in 2018 to RMB34.0 billion in 2019, primarily due to an increase in costs of goods sold, content costs, depreciation expenses, and traffic acquisition costs.

Selling, general and administrative expenses

The selling, general and administrative expenses of Baidu Core decreased by 12% from RMB14.7 billion in 2019 to RMB12.9 billion (US\$2.0 billion) in 2020, primarily due to a decrease in channel spending, promotional marketing and personnel-related expenses.

The selling, general and administrative expenses of Baidu Core decreased by 4% from RMB15.3 billion in 2018 to RMB14.7 billion in 2019, primarily due to a decrease in channel spending and personnel-related expenses, offset by an increase in promotional spending.

Research and development expenses

The research and development expenses of Baidu Core increased by 7% from RMB15.7 billion in 2019 to RMB16.8 billion (US\$2.6 billion) in 2020, primarily due to an increase in personnel-related expenses.

The research and development expenses of Baidu Core increased by 14% from RMB13.8 billion in 2018 to RMB15.7 billion in 2019, primarily due to an increase in personnel-related expenses.

iQIYI. Operating costs and expenses of iQIYI mainly consist of content costs, personnel-related costs, bandwidth costs, marketing and promotion spending, and payment platform charges.

Cost of revenues

The cost of revenues of iQIYI decreased by 8% from RMB30.3 billion in 2019 to RMB27.9 billion (US\$4.3 billion) in 2020, primarily due to lower content costs and bandwidth cost.

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The cost of revenues of iQIYI increased by 12% from RMB27.1 billion in 2018 to RMB30.3 billion in 2019, primarily due to higher content costs and other cost items.

Selling, general and administrative expenses

The selling, general and administrative expenses of iQIYI were RMB5.2 billion (US\$795 million) in 2020, which was basically flat from 2019.

The selling, general and administrative expenses of iQIYI increased by 26% from RMB4.2 billion in 2018 to RMB5.2 billion in 2019, primarily due to increased sales and marketing expenses related to certain iQIYI apps and its game business, as well as higher personnel-related compensation expenses.

Research and development expenses

The research and development expenses of iQIYI were RMB2.7 billion (US\$410 million) in 2020, which was basically flat from 2019.

The research and development expenses of iQIYI increased by 34% from RMB2.0 billion in 2018 to RMB2.7 billion in 2019, primarily due to an increase in personnel-related costs.

Liquidity and Capital Resources

As of December 31, 2020, we had RMB162.9 billion (US\$25.0 billion) of cash, cash equivalents, restricted cash and short-term investments. Our cash and cash equivalents consist of cash on hand and investments in interest bearing demand deposit accounts, time deposits, money market funds and other liquid investments which have original maturities of three months or less. The short-term investments primarily consist of fixed-rate and adjustable-rate debt investments with original maturity of less than one year. We believe that our current cash, cash equivalents, restricted cash and short-term investments and anticipated cash flow from operations will be sufficient to meet our anticipated cash needs, including our cash needs for working capital, capital expenditures and debt repayment, for at least the next 12 months. We may, however, require additional cash due to changing business conditions or other future developments, including any investments or acquisitions we may decide to pursue, and we may incur additional indebtedness (such as loans, convertible senior notes and notes payable) in the future.

Furthermore, cash transfers from our PRC subsidiaries to their parent companies outside of China are subject to PRC government control of currency conversion. Shortages in the availability of foreign currency may restrict the ability of our PRC subsidiaries and consolidated affiliated entities to remit sufficient foreign currency to pay dividends or other payments to their parent companies outside of China or our company, or otherwise satisfy their foreign currency denominated obligations. See “Risk Factors—Risks Related to Doing Business in China—Governmental control of currency conversion may affect the value of your [REDACTED].” As of December 31, 2020, our PRC subsidiaries and consolidated affiliated entities held RMB134.1 billion (US\$20.6 billion) of cash, cash equivalents, restricted cash, and short-term investments, RMB875 million (US\$134 million) of which were in the form of foreign currencies.

The total outstanding balance of our short-term loans as of December 31, 2019 and 2020 amounted to RMB2.6 billion and RMB3.0 billion (US\$462 million) respectively, which consisted of RMB denominated borrowings made by our subsidiaries from financial institutions in the PRC and were repayable within one year.

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The repayment of substantially all short-term loans is guaranteed by the subsidiaries and VIEs of iQIYI and either collateralized by an office building of one of iQIYI’s VIEs or collateralized by restricted cash or other receivables. As of December 31, 2019 and 2020, the weighted average interest rates for the outstanding borrowings were 4.05% and 4.30%, respectively, and the aggregate amounts of unused lines of credit for short-term loans were RMB1.6 billion and RMB840 million (US\$129 million), respectively.

We have entered into the following long-term loan transactions with commercial banks:

- In June 2016, we entered into a five-year term and revolving facility agreement with a group of 21 syndicated bankers, pursuant to which we are entitled to borrow an unsecured US\$ denominated floating rate loan of US\$1.0 billion with a term of five years and to borrow an unsecured US\$ denominated revolving loan of US\$1.0 billion for five years. The facility was priced at 110 basis points over LIBOR and is intended for our general working capital. In June 2016, we drew down two tranches of US\$250 million each under the facility commitment. In November 2016, we drew down two tranches of US\$250 million each under the facility commitment. In connection with the facility agreements, we entered into four interest rate swap agreements, pursuant to which the loans would be settled with a fixed annual interest rate of 2.11%, 2.10%, 2.78% and 2.78% respectively, during the respective term of the loans.
- iQIYI has other bank borrowings of RMB909 million (US\$139 million) as of December 31, 2020, primarily used for working capital purposes, see Note 12 to the Historical Financial Information in Appendix IA.

In February 2021, we entered into a non-binding term sheet for a term and revolving facility with a group of five mandated lead arrangers, bookrunners and underwriters, pursuant to which we are entitled to borrow an unsecured US\$ denominated floating rate term loan of US\$1.5 billion with a term of 5 years and to borrow an unsecured US\$ denominated revolving loan of US\$1.5 billion for 5 years. The facility is intended to finance the general corporate purposes and pay all transaction related fees and expenses.

We have issued the following rounds of debt securities, which remain outstanding as of the Latest Practicable Date:

- In November 2012, we issued US\$750 million senior unsecured notes due in 2017, with stated annual interest rates of 2.25%, and US\$750 million senior unsecured notes due in 2022 (“2022 Ten-year Notes”), with stated annual interest rates of 3.50%. The net proceeds from the sale of the notes were used for general corporate purposes. In November 2017, notes with carrying value of US\$750 million were fully repaid when they became due. As of December 31, 2020, the total carrying value and estimated fair value of these notes were US\$750 million and US\$786 million, respectively. The estimated fair value was based on quoted prices for our publicly-traded debt securities as of December 31, 2020. We are not subject to any financial covenants or other significant restrictions under the notes. In 2020, we paid an aggregate of US\$26 million in interest payments related to these notes.
- In June 2015, we issued an aggregate of US\$750 million senior unsecured notes due in 2020 (“2020 Notes”), with stated annual interest rate of 3.00%, and an aggregate of US\$500 million senior unsecured notes due in 2025 (“2025 Ten-year Notes”), with stated annual interest rate of 4.13%. The net proceeds from the sale of the notes were used for general corporate purposes. In June 2020, notes with carrying value of US\$750 million were fully repaid when they became due. As of December 31, 2020, the total carrying value and estimated fair value were US\$500 million and US\$559 million, respectively, with respect to the 2025 Notes. The estimated fair values were

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based on quoted prices for our publicly-traded debt securities as of December 31, 2020. We are not subject to any financial covenants or other significant restrictions under the notes. In 2020, we paid an aggregate of US\$32 million in interest payments related to these notes.

- In July 2017, we issued an aggregate of US\$900 million senior unsecured notes due in 2022 (“2022 Five-year Notes”), with stated annual interest rate of 2.88%, and an aggregate of US\$600 million senior unsecured notes due in 2027 (“2027 Notes”), with stated annual interest rate of 3.63%. The net proceeds from the sale of the notes were used to repay existing indebtedness and for general corporate purposes. As of December 31, 2020, the total carrying value and estimated fair value were US\$900 million and US\$926 million, respectively, with respect to the 2022 Five-year Notes, and US\$600 million and US\$663 million, respectively, with respect to the 2027 Notes. The estimated fair values were based on quoted prices for our publicly-traded debt securities as of December 31, 2020. We are not subject to any financial covenants or other significant restrictions under the notes. In 2020, we paid an aggregate of US\$48 million in interest payments related to these notes.
- In March 2018, we issued an aggregate of US\$1.0 billion senior unsecured notes due in 2023 (“2023 Notes”), with stated annual interest rate of 3.88%, and an aggregate of US\$500 million senior unsecured notes due in 2028 (“2028 March Notes”), with stated annual interest rate of 4.38%. The net proceeds from the sale of the notes were used to repay existing indebtedness and for general corporate purposes. As of December 31, 2020, the total carrying value and estimated fair value were US\$1.0 billion and US\$1.1 billion, respectively, with respect to the 2023 Notes, and US\$500 million and US\$576 million, respectively, with respect to the 2028 March Notes. The estimated fair values were based on quoted prices for our publicly-traded debt securities as of December 31, 2020. We are not subject to any financial covenants or other significant restrictions under the notes. In 2020, we paid an aggregate of US\$61 million in interest payments related to these notes.
- In November 2018, we issued an aggregate of US\$600 million senior unsecured notes due in 2024 (“2024 November Notes”), with stated annual interest rate of 4.38%, and an aggregate of US\$400 million senior unsecured notes due in 2028 (“2028 November Notes”), with stated annual interest rate of 4.88%. In December 2018, we issued an aggregate of US\$250 million senior unsecured notes due in 2024 (“2024 December Notes”), with stated annual interest rate of 4.38%, which constitute a further issuance of, and be fungible with and be consolidated and form a single series with the 2024 November Notes. The net proceeds from the sale of the notes were used to repay existing indebtedness and for general corporate purposes. As of December 31, 2020, the total carrying value and estimated fair value were US\$600 million and US\$659 million, respectively, with respect to the 2024 November Notes, US\$400 million and US\$480 million, respectively, with respect to the 2028 November Notes, and US\$250 million and US\$275 million, respectively, with respect to the 2024 December Notes. The estimated fair values were based on quoted prices for our publicly-traded debt securities as of December 31, 2020. We are not subject to any financial covenants or other significant restrictions under the notes. In 2020, we paid an aggregate of US\$57 million in interest payments related to these notes.
- In April 2020, we issued an aggregate of US\$600 million senior unsecured notes due in 2025 (“2025 Five-year Notes”), with stated annual interest rate of 3.075%, and an aggregate of US\$400 million senior unsecured notes due in 2030 (“2030 April Notes”), with stated annual interest rate of 3.425%. The net proceeds from the sale of the notes were used to repay existing indebtedness and for general corporate purposes. As of December 31, 2020, the total carrying value and estimated fair value were US\$600 million and US\$642 million, respectively, with respect to the 2025 Five-Year Notes, and US\$400 million and US\$444 million, respectively, with

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respect to the 2030 April Notes. The estimated fair values were based on quoted prices for our publicly-traded debt securities as of December 31, 2020. We are not subject to any financial covenants or other significant restrictions under the notes.

- In October 2020, we issued an aggregate of US\$650 million senior unsecured notes due in 2026 (“2026 Notes”), with stated annual interest rate of 1.720%, and an aggregate of US\$300 million senior unsecured notes due in 2030 (“2030 October Notes”), with stated annual interest rate of 2.375%. The net proceeds from the sale of the notes are to be used to repay existing indebtedness. As of December 31, 2020, the total carrying value and estimated fair value were US\$650 million and US\$663 million, respectively, with respect to the 2026 Notes, and US\$300 million and US\$307 million, respectively, with respect to the 2030 October Notes. The estimated fair values were based on quoted prices for our publicly-traded debt securities as of December 31, 2020. We are not subject to any financial covenants or other significant restrictions under the notes.

iQIYI has issued the following convertible notes, which remain outstanding as of the Latest Practicable Date:

- In December 2018, iQIYI issued US\$750 million convertible senior notes due 2023 (“iQIYI 2023 Convertible Notes”). The iQIYI 2023 Convertible Notes are senior, unsecured obligations of iQIYI, and interest is payable semi-annually in cash at a rate of 3.75% per annum with a maturity date of December 1, 2023, unless previously repurchased, redeemed or converted prior to such date. The initial conversion rate of the iQIYI 2023 Convertible Notes is 37.1830 of iQIYI’s ADSs per US\$1,000 principal amount of the iQIYI 2023 Convertible Notes. Upon conversion, iQIYI will pay or deliver to such converting holders, as the case may be, cash, ADSs, or a combination of cash and ADSs, at its election.

Concurrently with the issuance of the iQIYI 2023 Convertible Notes, iQIYI purchased capped call options on iQIYI’s ADS with certain counterparties at a price of US\$68 million. The capped call exercise price is equal to the initial conversion price of the iQIYI 2023 Convertible Notes and the cap price is US\$38.42 per ADS, subject to certain adjustments under the terms of the capped call transaction. The cost of the capped call was recorded as a reduction of our additional paid-in capital and non-controlling interests on the consolidated balance sheets with no subsequent remeasurement to fair value.

As the conversion option may be settled entirely or partially in cash at iQIYI’s option, we separated the iQIYI 2023 Convertible Notes into liability and equity components in accordance with ASC Subtopic 470-20, *Debt with Conversion and Other Options*. The carrying amount of the liability component was calculated by measuring the fair value of a similar liability that does not have an associated conversion feature. The carrying amount of the equity component representing the conversion option was determined by deducting the fair value of the liability component from the initial proceeds and recorded as additional paid-in capital. Debt issuance costs were allocated to the liability and equity components based on the same proportion as the recognized amounts bifurcated based on gross proceeds from the iQIYI 2023 Convertible Notes. The difference between the principal amount of the iQIYI 2023 Convertible Notes and the liability component is considered debt discount and is amortized at an effective interest rate of 7.04% to accrete the discounted carrying value of the iQIYI 2023 Convertible Notes to its face value on December 1, 2021, the put date of the iQIYI 2023 Convertible Notes. The holders may require iQIYI to repurchase all or portion of the iQIYI 2023 Convertible Notes for cash on December 1, 2021, or upon a fundamental change, at a repurchase price equal to 100% of the principal amount, plus accrued and unpaid interest.

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- In March 2019, iQIYI issued US\$1.2 billion convertible senior notes due 2025 (“iQIYI 2025 Convertible Notes”). The iQIYI 2025 Convertible Notes are senior, unsecured obligations of iQIYI, and interest is payable semi-annually in cash at a rate of 2.00% per annum with a maturity date of April 1, 2025, unless previously repurchased, redeemed or converted prior to such date. The initial conversion rate of the iQIYI 2025 Convertible Notes is 33.0003 of iQIYI’s ADSs per US\$1,000 principal amount of the iQIYI 2025 Convertible Notes. Upon conversion, iQIYI will pay or deliver to such converting holders, as the case may be, cash, ADSs, or a combination of cash and ADSs, at its election.

Concurrently with the issuance of the iQIYI 2025 Convertible Notes, iQIYI purchased call options on iQIYI’s ADS with certain counterparties at a price of US\$85 million. The capped call exercise price is equal to the initial conversion price of the iQIYI 2025 Convertible Notes and the cap price is US\$40.02 per ADS, subject to certain adjustments under the terms of the capped call transaction. The cost of the capped call was recorded as a reduction of our additional paid-in capital and non-controlling interests on the consolidated balance sheets with no subsequent remeasurement to fair value.

The accounting of iQIYI 2025 Convertible Notes is similar to that of iQIYI 2023 Convertible Notes. The difference between the principal amount of the iQIYI 2025 Convertible Notes and the liability component is considered debt discount and is amortized at an effective interest rate of 6.01% to accrete the discounted carrying value of the iQIYI 2025 Convertible Notes to its face value on April 1, 2023, the put date of the Notes. The holders may require iQIYI to repurchase all or portion of the iQIYI 2025 Convertible Notes for cash on April 1, 2023, or upon a fundamental change, at a repurchase price equal to 100% of the principal amount, plus accrued and unpaid interest.

- In January 2021, iQIYI completed the issuance of US\$900 million convertible senior notes due 2026 (“iQIYI 2026 Convertible Notes”). The iQIYI 2026 Convertible Notes are senior, unsecured obligations of iQIYI, and interest is payable semi-annually in cash at a rate of 4.00% per annum with a maturity date of December 15, 2026, unless previously repurchased, redeemed or converted prior to such date. The initial conversion rate of the iQIYI 2026 Convertible Notes is 44.8179 ADSs of iQIYI per US\$1,000 principal amount of the iQIYI 2026 Convertible Notes. Upon conversion, iQIYI will pay or deliver to such converting holders, as the case may be, cash, iQIYI ADSs, or a combination of cash and iQIYI ADSs, at its election.

The iQIYI 2023 Convertible Notes, the iQIYI 2025 Convertible Notes and the iQIYI 2026 Convertible Notes are collectively referred to the Convertible Notes. As of December 31, 2019 and 2020, the principal amount of the liability component of the Convertible Notes were RMB13.6 billion and RMB18.0 billion (US\$2.8 billion), unamortized debt discount was RMB1.3 billion and RMB1.3 billion (US\$195 million), and the net carrying amount of the liability component were RMB12.3 billion and RMB16.7 billion (US\$2.6 billion), respectively. The carrying amount of the equity component of the Convertible Notes were RMB1.3 billion and RMB1.7 billion (US\$267 million), respectively. For the years ended December 31, 2018, 2019 and 2020, the amount of interest cost recognized relating to both the contractual interest coupon and amortization of the discount on the liability component were RMB24 million, RMB670 million and RMB799 million (US\$123 million), respectively. As of December 31, 2020, the liability component of the iQIYI 2023 Convertible Notes, the iQIYI 2025 Convertible Notes and the iQIYI 2026 Convertible Notes will be accreted up to the principal amount of RMB4.9 billion (US\$750 million), RMB7.8 billion (US\$1.2 billion) and RMB5.2 billion (US\$800 million) over a remaining period of 0.92 years, 2.25 years and 3.59 years, respectively.

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We may use the net proceeds from our issuance and sale of the notes to fund the operations of our PRC subsidiaries by making additional capital contributions to our existing PRC subsidiaries, injecting capital to establish new PRC subsidiaries and/or providing loans to our PRC subsidiaries. Such transfer of funds from Baidu, Inc. or any of our offshore subsidiaries to our PRC subsidiaries is subject to the PRC regulatory restrictions and procedures: (i) capital increase of the existing PRC subsidiaries and establishment of new PRC subsidiaries must be registered with the local branch of SAMR and reported to the Ministry of Commerce via the online enterprise registration system, and registered with local banks authorized by SAFE; and (ii) loans to any of our PRC subsidiaries must not exceed the statutory limit and must be filed with SAFE. See “Risk Factors—Risks Related to Doing Business in China—PRC regulation of loans to and direct investment in PRC entities by offshore holding companies and governmental control of currency conversion may delay or prevent us from making loans to our PRC subsidiaries or consolidated affiliated entities, or making additional capital contributions to our PRC subsidiaries, which could adversely affect our ability to fund and expand our business.”

As of December 31, 2019 and 2020, we had RMB51.9 billion and RMB55.8 billion (US\$8.6 billion) in long-term loans and notes payables (including current portion of RMB6.0 billion and RMB7.4 billion (US\$1.1 billion)), RMB12.3 billion and RMB16.7 billion (US\$2.6 billion) in long-term convertible notes (including current portion of nil and RMB4.8 billion (US\$728 million)) and had RMB2.6 billion and RMB3.0 billion (US\$462 million) in short-term loans, respectively. Our long-term loans and notes payable, long-term convertible notes and short-term loans include those of iQIYI hereinafter. As of December 31, 2019 and 2020, iQIYI had RMB1.6 billion and RMB909 million (US\$139 million) in long-term loans payables (including current portion of RMB737 million and RMB909 million (US\$139 million)), RMB12.3 billion and RMB16.7 billion (US\$2.6 billion) in long-term convertible notes (including current portion of nil and RMB4.8 billion (US\$728 million)) and had RMB2.6 billion and RMB3.0 billion (US\$455 million) in short-term loans, respectively.

Cash Flows

As of December 31, 2018, 2019 and 2020, we had RMB141.5 billion, RMB147.4 billion and RMB162.9 billion (US\$25.0 billion) in cash, cash equivalents, restricted cash and short-term investments.

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

| | Year ended December 31, | | | |
|---|-------------------------|----------|----------|---------|
| | 2018 | 2019 | 2020 | |
| | RMB | RMB | RMB | US\$ |
| | (in millions) | | | |
| Net cash provided by operating activities | 35,967 | 28,458 | 24,200 | 3,709 |
| Net cash used in investing activities | (34,460) | (19,974) | (27,552) | (4,223) |
| Net cash provided by (used in) financing activities | 15,082 | (3,873) | 5,665 | 869 |
| Effect of exchange rate changes on cash, cash equivalents and restricted cash | 1,902 | 1 | (212) | (32) |
| Net increase in cash, cash equivalents and restricted cash | 18,491 | 4,612 | 2,101 | 323 |
| Cash, cash equivalents and restricted cash at beginning of the year | 11,336 | 29,827 | 34,439 | 5,278 |
| Cash, cash equivalents and restricted cash at end of the year | 29,827 | 34,439 | 36,540 | 5,601 |

Operating Activities

Net cash provided by operating activities decreased to RMB24.2 billion (US\$3.7 billion) in 2020 from RMB28.5 billion in 2019. This decrease was primarily due to an addition of RMB10.5 billion

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(US\$1.6 billion) in licensed copyrights resulting from reclassification of cash outflows for costs incurred to acquire licensed contents from investing activities to operating activities due to the adoption of ASU 2019-02, an increase of RMB9.7 billion (US\$1.5 billion) in investment and interest income and a decrease of RMB7.8 billion (US\$1.2 billion) in impairment of other assets, partially offset by an increase of RMB21.3 billion (US\$3.3 billion) in net income.

Net cash generated from operating activities decreased to RMB28.5 billion in 2019 from RMB36.0 billion in 2018. This decrease was primarily due to a decrease of RMB24.9 billion in net income, partially offset by an increase of RMB9.5 billion in impairment of other assets and a decrease of RMB6.1 billion in gain on disposal of subsidiaries.

Investing Activities

Net cash used in investing activities was RMB27.6 billion (US\$4.2 billion) in 2020, consisting primarily of RMB159.2 billion (US\$24.4 billion) in purchase of held-to-maturity investments, RMB133.0 billion (US\$20.4 billion) in purchase of available-for-sale investments, RMB134.3 billion (US\$20.6 billion) in maturities of held-to-maturity investments, RMB135.6 billion (US\$20.8 billion) in sales and maturities of available-for-sale investments, and RMB4.5 billion (US\$685 million) in purchase of other long-term investments offset by RMB6.5 billion (US\$1.0 billion) in proceeds from disposal of long-term investments.

Net cash used in investing activities was RMB20.0 billion in 2019, consisting primarily of RMB12.2 billion for acquisition of licensed copyrights, RMB6.4 billion for acquisition of fixed assets, RMB120.2 billion in purchase of held-to-maturity investments, RMB218.2 billion in purchase of available-for-sale investments, offset by RMB46.6 billion in maturities of held-to-maturity investments and RMB291.2 billion in sales and maturities of available-for-sale investments, and RMB6.3 billion in purchase of other long-term investments offset by RMB7.5 billion in proceeds from disposal of long-term investments.

Net cash used in investing activities was RMB34.5 billion in 2018, consisting primarily of RMB13.1 billion for the acquisition of licensed copyrights, RMB27.6 billion in purchase of held-to-maturity investments, RMB284.1 billion in purchase of available-for-sale investments and RMB9.9 billion in purchase of long-term investments, offset by RMB49.0 billion in maturities of held-to-maturity investments and RMB239.9 billion in sales and maturities of available-for sale investments, and RMB10.8 billion in our net cash inflow relating to the financial services business we divested in 2018.

We have adopted ASU 2019-02 on January 1, 2020 which the FASB issued in March 2019, and report cash flows related to the acquisition of licensed copyrights as “operating activities” in the statement of cash flows, beginning with the period of adoption, as opposed to “investing activities.”

Financing Activities

Net cash provided by financing activities was RMB5.7 billion (US\$869 million) in 2020, consisting primarily of RMB13.3 billion (US\$2.0 billion) from our issuance of long-term notes, RMB5.2 billion (US\$789 million) from the issuance by iQIYI of convertible notes, and RMB4.7 billion (US\$715 million) from issuance of iQIYI’s shares, offset by RMB13.1 billion (US\$2.0 billion) used to repurchase our shares and repayment of RMB5.4 billion (US\$824 million) for long-term notes.

Net cash used in financing activities was RMB3.9 billion in 2019, consisting primarily of our repayment of RMB6.9 billion for long-term notes and RMB5.0 billion used to repurchase our shares, offset by RMB7.9 billion of net proceeds from the issuance by iQIYI of convertible notes.

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Net cash generated from financing activities was RMB15.1 billion in 2018, consisting primarily of RMB18.1 billion of net proceeds from issuance of long-term notes and RMB15.7 billion of proceeds from issuance of shares by our subsidiaries, which was primarily due to the initial public offering of iQIYI’s ADSs in 2018, offset by net cash outflow of RMB21.3 billion relating to the financial services business we divested in 2018.

Certain Balance Sheet Items

Long-term investments

The following table sets forth a breakdown of our long-term investments by accounting treatment as of the dates indicated:

| | As of December 31, | | | |
|---|----------------------|----------------------|----------------------|----------------------|
| | 2018 | 2019 | 2020 | |
| | RMB | RMB | RMB | US\$ |
| | (In millions) | | | |
| Equity investments at fair value with readily determinable fair value | 4,428 | 11,334 | 12,978 | 1,989 |
| Available-for-sale debt investment | 1,167 | 3,970 | 2,607 | 400 |
| Equity investments without readily determinable fair value | 29,269 | 24,686 | 24,603 | 3,770 |
| Equity method investments | 44,133 | 27,105 | 24,067 | 3,688 |
| Investments accounted for at fair value | 1,457 | 1,819 | 2,238 | 343 |
| Long-term held-to-maturity investments | — | 496 | 9,740 | 1,493 |
| Total long-term investments | <u>80,454</u> | <u>69,410</u> | <u>76,233</u> | <u>11,683</u> |

Equity investments at fair value with readily determinable fair value represent investments in the equity securities of publicly listed companies, for which we do not have significant influence. Equity investments at fair value with readily determinable fair value are reported at fair value and changes in fair value are recognized in earnings.

Equity investments without readily determinable fair value mainly represents our investments in companies without observable market price in the form of preferred shares or common stock for which we do not have significant influence. For these investments, we elected to use the measurement alternative to measure such investments at cost, less any impairment, plus or minus changes resulting from observable price changes in orderly transactions for identical or similar investments of the same issuer, if any.

We recognized a net gain of RMB4.4 billion, RMB17 million, and RMB2.0 billion (US\$304 million) related to equity securities without readily determinable fair value as “others, net” in our consolidated statements of comprehensive income for the years ended December 31, 2018, 2019 and 2020, respectively.

During the Track Record Period, our significant equity method investees primarily included Trip.com with carrying amount of RMB30.5 billion, RMB14.1 billion and RMB12.6 billion as of December 31, 2018, 2019 and 2020, respectively. We recognized impairment of RMB167 million, RMB9.2 billion and RMB297 million (US\$46 million) related to equity method investments for the years ended December 31, 2018, 2019 and 2020, respectively.

Long-term held-to-maturity securities were mainly deposits in commercial banks with maturities of greater than one year and wealth management products issued by commercial banks and other financial institutions for which we have the positive intent and ability to hold those securities to maturity.

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Short-term investments

As of December 31, 2018, 2019 and 2020, our short-term investments comprised of only debt securities. Short-term held-to-maturity securities were mainly deposits in commercial banks with maturities of less than one year and wealth management products issued by commercial banks and other financial institutions for which we have the positive intent and ability to hold those securities to maturity. The short-term available-for-sale securities include wealth management products issued by commercial banks and other financial institutions which are not classified as trading securities or as held-to-maturity securities.

Accounts Receivable, net

Our accounts receivable mainly consists of those due from our online marketing customers, cloud services customers and other services customers, and are recognized and carried at the original invoiced amount less an allowance for credit losses. Our accounts receivable, net increased by 17% from RMB7.4 billion as of December 31, 2019 to RMB8.7 billion (US\$1.3 billion) as of December 31, 2020, primarily due to an increase from online marketing and cloud services. Our accounts receivable increased by 23% from RMB6.0 billion as of December 31, 2018 to RMB7.4 billion as of December 31, 2019, primarily due to our business development on Xiaodu smart products and cloud services.

Accounts Payable and Accrued Liabilities

Our accounts payable and accrued liabilities primarily include those related to content acquisition costs, traffic acquisition costs, bandwidth costs, accrued payroll and welfare and accrued other operating expenses. Our accounts payable and accrued liabilities increased by 12% from RMB32.7 billion as of December 31, 2019 to 36.7 billion (US\$5.6 billion) as of December 31, 2020, primarily due to an increase in payables to non-controlling shareholder related to their withdrawal of equity from our subsidiary. Our accounts payable and accrued liabilities decreased by 8% from RMB35.4 billion as of December 31, 2018 to RMB32.7 billion as of December 31, 2019 primarily due to a decrease in content acquisition related payables.

Customer Deposits and Deferred Revenue

Our customer deposits and deferred revenue mainly consist of deposits received from certain customers of our online marketing services. Our customer deposits and deferred revenue increased by 14% from RMB11.1 billion as of December 31, 2019 to RMB12.6 billion (US\$1.9 billion) as of December 31, 2020, primarily due to an increase in deposits and consideration received from customers of online marketing services and iQIYI membership services. Our customer deposits and deferred revenue increased by 20% from RMB9.2 billion as of December 31, 2018 to RMB11.1 billion as of December 31, 2019, primarily due to an increase in deposits and consideration received from online marketing services customers.

Total Shareholders' Equity

Our total Baidu, Inc. shareholders' equity increased by 12% from of RMB163.6 billion as of December 31, 2019 to RMB182.7 billion (US\$28.0 billion) as of December 31, 2020, primarily due to net income attributable to Baidu, Inc of RMB22.5 billion (US\$3.4 billion), share-based compensation of RMB5.7 billion (US\$881 million) and issuance of shares by our subsidiaries to non-controlling interest of RMB2.3 billion, and partially offset by repurchase of ordinary shares of RMB13.1 billion (US\$2.0 billion) for the year ended December 31, 2020. Our total shareholders' equity slightly

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increased from of RMB162.9 billion as of December 31, 2018 to RMB163.6 billion as of December 31, 2019, primarily due to net income attributable to Baidu, Inc of RMB2.1 billion and share-based compensation of RMB5.0 billion, and offset by other comprehensive loss of RMB1.6 billion and repurchase and retirement of ordinary shares of RMB5.0 billion in 2019.

Goodwill

The carrying amount of goodwill for each of Baidu Core and iQIYI as of December 31, 2018, 2019 and 2020 was as follows.

| | As of December 31, | | |
|--------------------|--------------------|---------------|---------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| Baidu Core | | | |
| —91 Wireless | 9,845 | 9,845 | 9,845 |
| —Others | 4,803 | 4,517 | 8,515 |
| | <u>14,648</u> | <u>14,362</u> | <u>18,360</u> |
| iQIYI | 3,888 | 3,888 | 3,888 |
| | <u>18,536</u> | <u>18,250</u> | <u>22,248</u> |

In October 2013, we acquired 100% of the outstanding ordinary shares of 91 Wireless Websoft Limited (“91 Wireless”), a leading Chinese mobile application marketplaces and mobile games operator, with which we expected to enhance its ability and market share in mobile online marketing business. The total purchase consideration was RMB11.2 billion, and we recognized goodwill of RMB9.8 billion.

The carrying amount of goodwill for iQIYI reporting unit mainly represents business combinations of iQIYI, Inc. (formerly known as “Qiyi.com, Inc.”) completed in 2012 and PPStream Inc. (“PPS”) completed in 2013.

Except for 91 Wireless, iQIYI and PPS, we completed over 30 business combinations since establishment, from which we expected to achieve significant synergies as the acquired businesses complement our existing businesses. The acquired entities were considered insignificant individually as of the acquisition date.

As of December 31, 2018, 2019 and 2020, we had two reporting units, consisting of Baidu Core and iQIYI. We have the option to assess qualitative factors first to determine whether it is necessary to perform the quantitative test in accordance with ASC Subtopic 350-20, *Intangibles — Goodwill and Other: Goodwill* (“ASC 350-20”). In the qualitative assessment, we consider primary factors such as industry and market considerations, overall financial performance of the reporting unit, and other specific information related to the operations. If we believe, as a result of the qualitative assessment, that it is more-likely-than-not that the fair value of the reporting unit is less than its carrying amount, the quantitative impairment test described above is required. Otherwise, no further testing is required. The quantitative impairment test compares the fair value of the reporting unit with its carrying amount, including goodwill. If the carrying amount of a reporting unit exceeds its fair value, an impairment loss shall be recognized in an amount equal to that excess.

We performed qualitative assessments for the reporting unit of Baidu Core as of December 31, 2018, 2019 and 2020. Based on the requirements of ASC 350-20, we evaluated all relevant factors including,

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but not limited to, macroeconomic conditions, industry and market conditions, financial performance, and our share price. We weighed all factors in their entirety and concluded that it was not more-likely-than-not the fair value of the Baidu Core reporting unit was less than its carrying amount. Therefore, further impairment testing was unnecessary as of December 31, 2018, 2019 and 2020.

We elected to choose to bypass the qualitative assessment and proceed directly to perform quantitative test for the reporting unit of iQIYI. Subsequent to iQIYI’s IPO, we primarily considered the quoted market price of iQIYI’s share to determine the fair value of the reporting unit. As of December 31, 2018, 2019 and 2020, the fair value of iQIYI exceeded its carrying amount, therefore, goodwill related to the iQIYI reporting unit was not impaired and we were not required to perform further testing.

Intangible assets — Trademarks and Others

Our intangible assets included trademarks, technology, intellectual property rights, online literature and others. The estimated useful lives of trademarks range from 2 to 22 years. Others mainly include customer relationships, software, domain names and user lists that have estimated useful lives ranging from 1 to 22 years. The estimated useful lives of intangible assets are determined by considering several factors, including the expected use of the asset by us, our own historical experience in renewing or extending similar arrangements, the effect of demand, competition and other economic factors, etc.. For each major intangible asset class, the weighted average useful lives from the date of purchase for trademarks and others are 10 years and 8 years, respectively.

Level 3 fair value measurements

We use valuation methodologies, primarily the market approach, which requires management to unobservable inputs (level 3) such as selection of comparable companies and multiples, volatility, discount for lack of marketability and probability of exit events as it relates to redemption preferences when applicable.

Other non-financial assets, intangible assets, licensed copyrights and produced content, would be measured at fair value whenever events or changes in circumstances indicate the carrying value of an asset may not be recoverable. The fair values of these non-financial long-lived assets were measured under income approach, based on our best estimation. Significant inputs used in the income approach primarily included future estimated cash flows and discount rate.

Our Directors oversee the valuation process by ensuring the management selecting a qualified financial reporting team, maintaining robust processes and internal controls, and overseeing significant valuations. Under the supervision of our Directors, the management conducts the estimation of fair values of such non-financial assets, including evaluation and selection of appropriate valuation methodologies and significant unobservable inputs of such non-recurring fair value measurements (level 3), with the assistance of our valuation specialists for those valuations that are significant to the financial statements. Based on the above procedures, our Directors are of the view that the valuation analysis performed by the Company is fair and reasonable, and the level 3 fair value measurements in the financial statements of our Company are properly prepared.

Details of the fair value measurement of financial assets categorized within Level 3, particularly the fair value hierarchy, the valuation techniques and key inputs, including significant unobservable inputs, and reconciliation of level 3 measurements are disclosed in Note 25 to the Historical Financial Information in Appendix IA.

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In relation to the fair value measurement of financial assets categorized within Level 3, the Joint Sponsors have conducted relevant due diligence work, including but not limited to, reviewing relevant disclosure and understanding, through the Company, the valuation work performed, including the valuation techniques adopted, procedures performed for impairment testing and the internal control process undertaken by the Company for the valuation of the financial assets. Having considered the work done by the Company’s management and Directors and the relevant due diligence conducted by the Joint Sponsors, nothing material has come to the Joint Sponsors’ attention to disagree with the Company in respect of the valuation of such financial assets.

Critical Accounting Policies

We prepare financial statements in accordance with U.S. GAAP, which requires us to make judgments, estimates and assumptions that affect the reported amounts of our assets and liabilities and the disclosure of our contingent assets and liabilities at the end of each fiscal period and the reported amounts of revenues and expenses during each fiscal period. We continually evaluate these judgments and estimates based on our own historical experience, knowledge and assessment of current business and other conditions, our expectations regarding the future based on available information and assumptions that we believe to be reasonable, which together form our basis for making judgments about matters that are not readily apparent from other sources. Since the use of estimates is an integral component of the financial reporting process, our actual results could differ from those estimates. Some of our accounting policies require a higher degree of judgment than others in their application.

The selection of critical accounting policies, the judgments and other uncertainties affecting application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors that should be considered when reviewing our financial statements. For further information on our critical accounting policies, see Note 2 to the Accountants’ Report in Appendix IA. We believe the following accounting policies involve the most significant judgments and estimates used in the preparation of our financial statements.

Consolidation of Affiliated Entities

In order to comply with PRC laws and regulations limiting foreign ownership of or imposing conditions on internet content, advertising, audio and video services, and mobile app distribution businesses, we operate our websites and conduct our internet content, advertising, audio and video services, and mobile app distribution businesses through our affiliated entities in China by means of contractual arrangements. We have entered into certain exclusive agreements with the affiliated entities directly or through our subsidiaries, which obligate us to absorb losses of the VIEs’ that could potentially be significant to the VIEs or entitle the Primary Beneficiaries to receive economic benefits from the VIEs that could potentially be significant to the VIEs. In addition, we have entered into certain agreements with the affiliated entities and the nominee shareholders of affiliated entities directly or through our subsidiaries, which enable us to direct the activities that most significantly affect the economic performance of the affiliated entities. Based on these contractual arrangements, we consolidate the affiliated entities as required by ASC Topic 810, *Consolidation*, because we hold all the variable interests of the affiliated entities directly or through the subsidiaries, which are the primary beneficiaries of the affiliated entities. We will reconsider the initial determination of whether a legal entity is a consolidated affiliated entity upon certain events listed in ASC 810-10-35-4 occurring. We will also continuously reconsider whether we are the primary beneficiaries of our affiliated entities as facts and circumstances change. See “Risk Factors—Risks Related to Our Corporate Structure.”

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Segment Reporting

As of December 31, 2018, 2019 and 2020, we had two reportable segments, Baidu Core and iQIYI. Baidu Core mainly provides search-based, feed-based, and other online marketing services, as well as products and services from our new AI initiatives. iQIYI is an online entertainment service provider that offers original, professionally produced and partner-generated content on its platform. In early April 2018, iQIYI completed its initial public offering (IPO) on the Nasdaq Global Market.

Our chief executive officer, who has been identified as the chief operating decision maker, (“CODM”), reviews the operating results of Baidu Core and iQIYI, to allocate resources and assess our performance. Accordingly, the financial statements include segment information which reflects the current composition of the reportable segments in accordance with ASC Topic 280, *Segment Reporting*.

Revenue Recognition

We adopted ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* (“ASU 2014-09”), codified in ASC Topic 606, *Revenue from Contracts with Customers* (“ASC 606”) from January 1, 2018, using the modified retrospective method.

Revenue is recognized when control of promised goods or services is transferred to our customers in an amount of consideration to which an entity expects to be entitled to in exchange for those goods or services. Revenue is recorded net of valued added taxes (“VAT”).

Performance-based online marketing services

Cost-per-click (“CPC”)

Our auction-based P4P platform enables customers to bid for priority placement of paid sponsored links and reach users who search for information related to their products or services. P4P online marketing customers can choose from search-based and feed-based online marketing services, and select criteria for their inventory purchase, such as daily spending limit and user profile targeted, including, but not limited to, users from specific regions in China and users online during specific time period. Revenue is recognized when all of the revenue recognition criteria are met, which is generally when a user clicks on one of the customer-sponsored links or feed-based marketing.

Other performance-based online marketing services

To the extent the we provide online marketing services based on performance criteria other than cost-per-click, such as the number of downloads (and user registration) of mobile apps and the pre-determined ratios of completed transaction volumes, revenue is recognized when the specified performance criteria are met along with the satisfaction of other applicable revenue recognition criteria.

Online display advertising services

We provide online display advertising services to its customers by integrating text description, image and/or video, and displaying the advertisement in the search result, in Baidu Feed or on other properties. We recognize revenue on a pro-rata basis over the contractual term for cost per time advertising arrangements, commencing on the start date of the display advertisement, or based on the number of times that the advertisement has been displayed for cost per thousand impressions advertising arrangements.

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Baidu Union online marketing services

Baidu Union is a program through which we expand distribution of its customers’ sponsored links or advertisements by leveraging the traffic of Baidu Union partners’ online properties. We acquire traffic from Baidu Union partners and is responsible for service fulfillment, pricing and bearing inventory risks. The services which we provided to customers through Baidu Union partners’ online properties include CPC, other performance-based online marketing services and online display advertising services. These services are provided in the same way to our customers as those through Baidu’s own platforms or properties. As principal, we recognize revenue from Baidu Union on a gross basis, based on customer billing. Payments made to Baidu Union partners are recorded as traffic acquisition costs, which are included in “cost of revenues” in the consolidated statements of comprehensive income (loss).

Certain online marketing services customers are required to pay a deposit before using our services. Once their account balance falls below a designated amount, they will receive an automated notice from us to replenish their accounts. Customer deposit is deducted when a user clicks on the customer’s link in the search result or when other performance criteria other than CPC have been satisfied. We offer payment terms to certain customers based on their credit history with us and other credit factors. We may also offer payment terms to certain agencies, as is common in the industry.

Collection

Certain customers of online marketing services are required to pay a deposit before using our services and are sent automated reminders to replenish their accounts when the balance falls below a designated amount. The deposits received are recorded as “customer deposits and deferred revenue” on the consolidated balance sheets. The amounts due to us are deducted from the deposited amounts when users click on the paid sponsored links in the search results or other performance criteria have been satisfied. In addition, we offer payment terms to some customers based on their historical marketing placements and credibility. We also offer longer payment terms to certain online payment agencies, consistent with industry practice.

Payment terms and conditions vary by customer and are based on the billing schedule established in our contracts or purchase orders with customers, but we generally provide credit terms to customers within one year; therefore, we have determined that our contracts do not include a significant financing component.

Sales incentives

We provide sales incentives to third-party agents that entitle them to receive price reduction on the online marketing services by meeting certain cumulative consumption requirements. We account for these incentives granted to customers as variable consideration and net them against revenue. Amounts of variable consideration is measured based on the most likely amount of incentives to be provided to customers.

Membership services

We offers membership services to subscribing members with various privileges, which primarily include access to exclusive and ad-free streaming of premium content 1080P/4K high definition video, Dolby Audio, and accelerated downloads and others, or personal cloud services, in exchange for non-refundable upfront membership fees. When the receipt of membership fees is for services to be delivered over a period of time, the receipt is initially recorded as “customer deposits and deferred

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revenue” and revenue is recognized ratably over the membership period as services are rendered. Membership services revenue also includes fees earned from subscribing members for on-demand content purchases and early access to premium content. We are the principal in its relationships where partners, including consumer electronics manufacturers (TVs and cell phones), mobile operators, internet service providers and online payment agencies, provide access to the membership services or payment processing services as we retain control over its service delivery to its subscribing members. Typically, payments made to the partners, are recorded as cost of revenues. For the sale of the right to other membership services through strategic cooperation with other parties, we recognize revenue on a net basis when we do not control the specified services before they are transferred to the customer.

Content distribution

We generate revenues from sub-licensing content licensed from vendors for cash or through nonmonetary exchanges mainly with other online video broadcasting companies. The exclusive licensing agreements we enter into with the vendors have a specified license period and provide us rights to sub-license these contents to other parties. We enter into a non-exclusive sub-license agreement with a sub-licensee for a period that falls within the original exclusive license period. For cash sub-licensing transactions, we are entitled to receive the sub-license fee under the sub-licensing arrangements and do not have any future obligation once we have provided the underlying content to the sub-licensee (which is provided at or before the beginning of the sub-license period). The sub-licensing of content represents a license of functional intellectual property that grants a right to use our licensed copyrights, and is recognized at the point in time when the licensed copyright is made available for the customer’s use and benefit.

We also enter into nonmonetary transactions to exchange online broadcasting rights of licensed copyrights with other online video broadcasting companies from time to time. The exchanged licensed copyrights provide rights for each party to broadcast the licensed copyrights received on its own website only. Each transferring party retains the right to continue broadcasting the exclusive content on its own website and/or sublicense the rights to the content it surrendered in the exchange. We account for these nonmonetary exchanges based on the fair value of the asset received. Barter sublicensing revenue are recognized in accordance with the same revenue recognition criteria above. We estimate the fair value of the licensed copyrights received using a market approach based on various factors, including the purchase price of similar non-exclusive and/or exclusive contents, broadcasting schedule, cast and crew, theme, and box office. The transaction price of barter sublicensing revenues is calculated on the individual content asset basis. For a significant barter sublicensing transaction, the Company further reviews the fair value by analyzing against the cost of the licensed copyrights bartered out and/or engages a third-party valuation firm to assess the reasonableness of its fair value. The attributable cost of sublicensing transactions, whether for cash or through nonmonetary exchanges, is recognized as cost of revenues through the amortization of the sublicensing right component of the exclusive licensed copyright.

Financial services

Before the divestiture of Du Xiaoman in August 2018, we offer financial services which include provision of installment payment services to consumers and wealth management services to third-party investors. Interest income earned from provision of financial services is reported as “Other revenues” and reported on a net basis after deduction of related interest costs incurred.

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Cloud services

We provide public cloud services, which include computing database, storage and other services and allow customers to use hosted software over the contract period without taking possession of the software, generally on either a subscription or consumption basis. We also provide proprietary cloud services which mainly include hardware, software licensing and software installation service. Revenue related to cloud services provided on a subscription basis is recognized ratably over the contract period. Revenue related to cloud services provided on a consumption basis, such as the amount of storage used in a period, is recognized based on the customer utilization of such resources.

Cloud service revenue is recognized over time if one of the following three criteria is met: (i) the customer simultaneously receives and consumes the benefits as we perform; (ii) our performance creates or enhances an asset that the customer controls as the asset is created or enhanced; (iii) the asset delivered has no alternative use and we have an enforceable right to payment for performance completed to date. Otherwise, revenue is recognized at a point in time only upon customer acceptance of the cloud services.

Sales of hardware

We sell hardware products via third-party agents or directly to end customers. Revenue from the sales of hardware is recognized when control of the goods is transferred to customers, which generally occurs when the products are delivered and accepted by our customers. Revenue is recorded net of sales incentives and return allowance.

Other revenue recognition related policies

For arrangements that include multiple performance obligations, primarily for advertisements to be displayed in different spots, placed under different forms and displayed at different times and proprietary cloud services which mainly include hardware, software licensing and software installation service, we would evaluate all of the performance obligations in the arrangement to determine whether each performance obligation is distinct. Consideration is allocated to each performance obligation based on its standalone selling price at contract inception. We generally determine standalone selling prices based on the prices charged to customers on a standalone basis or estimates it using an expected cost plus margin approach. If a promised good or service does not meet the criteria to be considered distinct, it is combined with other promised goods or services until a distinct bundle of goods or services exists.

Timing of revenue recognition may differ from the timing of invoicing to customers. For certain services customers are required to pay before the services are delivered to the customer. When either party to a revenue contract has performed, we recognize a contract asset or a contract liability on the consolidated balance sheet, depending on the relationship between the entity’s performance and the customer’s payment. Contract liabilities were mainly related to fees for membership services to be provided over the membership period, which were presented as “Customer deposits and deferred revenue” on the consolidated balance sheets. Contract assets mainly represent unbilled amounts related to our rights to consideration for advertising services and cloud services delivered and were included in “Other current assets, net” on the consolidated balance sheets.

We do not disclose the value of unsatisfied performance obligations for (i) contracts with an original expected length of one year or less and (ii) contracts for which we recognize revenue at the amount to which it has the right to invoice for services performed.

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Share-based Compensation

We account for share-based compensation in accordance with ASC Topic 718, *Compensation-Stock Compensation*, (“ASC 718”). We have elected to recognize share-based compensation using the straight-line method for all share-based awards issued with no performance conditions. For awards with performance conditions, compensation cost is recognized on an accelerated basis if it is probable that the performance condition will be achieved.

Forfeitures are estimated based on historical experience and are periodically reviewed. Cancellation of an award accompanied by the concurrent grant of a replacement award is accounted for as a modification of the terms of the cancelled award (“modified awards”). The compensation costs associated with the modified awards are recognized if either the original vesting condition or the new vesting condition is achieved. Total recognized compensation cost for the awards is at least equal to the fair value of the awards at the grant date unless at the date of the modification the performance or service conditions of the original awards are not expected to be satisfied. The incremental compensation cost is measured as the excess of the fair value of the replacement award over the fair value of the cancelled award at the cancellation date. Therefore, in relation to the modified award, we recognize share-based compensation over the vesting periods of the replacement award, which comprises (i) the amortization of the incremental portion of share-based compensation over the remaining vesting term, and (ii) any unrecognized compensation cost of the original award, using either the original term or the new term, whichever results in higher expenses for each reporting period.

We adopted ASU No. 2018-07, *Compensation-Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting* to simplify the accounting for share-based payments to nonemployees (“ASU 2018-07”) on January 1, 2019 using the modified retrospective method. Subsequent to the adoption, the Company measures equity-classified nonemployee awards using their fair value on grant date.

Income Taxes

We recognize income taxes under the liability method. Deferred income taxes are recognized for differences between the financial reporting and tax bases of assets and liabilities at enacted tax rates in effect for the years in which the differences are expected to reverse. We record a valuation allowance against the amount of deferred tax assets that we determine is not more-likely-than-not to be realized. The effect on deferred taxes of a change in tax rates is recognized in earnings in the period that includes the enactment date. For reconciliation of tax computed by applying the respective statutory income tax rate to pre-tax income, please see “Income taxes” under Note 14 to the Accountant’s Report in Appendix IA.

Deferred income taxes are recognized on the undistributed earnings of subsidiaries, which are presumed to be transferred to the parent company and are subject to withholding taxes, unless there is sufficient evidence to show that the subsidiary has invested or will invest the undistributed earnings indefinitely or that the earnings will be remitted in a tax-free liquidation.

We apply the provisions of ASC Topic 740, *Income Taxes*, (“ASC 740”), in accounting for uncertainty in income taxes. ASC 740 clarifies the accounting for uncertainty in income taxes by prescribing the recognition threshold a tax position is required to meet before being recognized in the financial statements. We have elected to classify interest and penalties related to an uncertain tax position (if and when required) as part of income tax expense in the consolidated statements of comprehensive income (loss).

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Long-term investments

Our long-term investments consist of equity investments with readily determinable fair value, equity method investments, held-to-maturity debt investments, available-for-sale debt investments, equity investments without readily determinable fair value, and other investments accounted for at fair value.

We adopted ASU No. 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities (“ASU 2016-01”), codified in ASC Topic 321, Investments—Equity Securities (“ASC 321”), from January 1, 2018 and the cumulative effect of RMB1.9 billion representing the unrealized gains of available-for-sale equity securities before the adoption was recorded as an adjustment to the opening retained earnings. Pursuant to ASU 321, equity investments, except for those accounted for under the equity method, those that result in consolidation of the investee and certain other investments, are measured at fair value, and any changes in fair value are recognized in earnings. For equity securities without readily determinable fair value and do not qualify for the existing practical expedient in ASC Topic 820, *Fair Value Measurements and Disclosures* (“ASC 820”) to estimate fair value using the net asset value per share (or its equivalent) of the investment, we elected to use the measurement alternative to measure those investments at cost, less any impairment, plus or minus changes resulting from observable price changes in orderly transactions for identical or similar investments of the same issuer, if any. Significant judgments are required to determine (i) whether observable price changes are orderly transactions and identical or similar to an investment held by the Company and (ii) the selection of appropriate valuation methodologies and underlying assumptions, including expected volatility and the probability of exit events as it relates to liquidation and redemption features used to measure the price adjustments for the difference in rights and obligations between instruments. Equity securities with readily determinable fair values are measured at fair value, and any changes in fair value are recognized in “Others, net.” in the consolidated statements of comprehensive income (loss).

For equity investments measured at fair value with changes in fair value recorded in earnings, we do not assess whether those securities are impaired. For equity investments that we elect to use the measurement alternative, we make a qualitative assessment considering impairment indicators to evaluate whether investments are impaired at each reporting date. Impairment indicators considered include, but are not limited to, a significant deterioration in the earnings performance or business prospects of the investee, including factors that raise significant concerns about the investee’s ability to continue as a going concern, a significant adverse change in the regulatory, economic, or technologic environment of the investee and a significant adverse change in the general market condition of either the geographical area or the industry in which the investee operates. If a qualitative assessment indicates that the investment is impaired, we estimate the investment’s fair value in accordance with the principles of ASC 820. If the fair value is less than the investment’s carrying value, we recognize an impairment loss in net income equal to the difference between the carrying value and fair value.

Investments in entities in which we can exercise significant influence but does not own a majority equity interest or control are accounted for using the equity method of accounting in accordance with ASC Topic 323, *Investments-Equity Method and Joint Ventures* (“ASC 323”). Under the equity method, we initially record its investment at cost and the difference between the cost of the equity investee and the amount of the underlying equity in the net assets of the equity investee is accounted for as if the investee were a consolidated subsidiary. We subsequently adjust the carrying amount of its investment to recognize our proportionate share of each equity investee’s net income or loss into earnings. We will discontinue applying the equity method if an investment (plus additional financial support provided to the investee, if any) has been reduced to zero. When we have other investments in

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the equity-method investee and we are not required to advance additional funds to the investee, we would continue to report its share of equity method losses in its statement of comprehensive (loss)income after our equity-method investment in ordinary shares has been reduced to zero, to the extent of and as an adjustment to the adjusted basis of our other investments in the investee. Such losses are first applied to those investments of a lower liquidation preference before being further applied to the investments of a higher liquidation preference. We adopted a one-quarter lag in reporting for its share of equity income (loss) in all of its equity method investees.

We evaluate the equity method investments for impairment at each reporting date, or more frequently if events or changes in circumstances indicate that the carrying amount of the investment might not be recoverable. Factors considered by us when determining whether an investment has been other-than-temporarily-impaired, includes, but are not limited to, the length of the time and the extent to which the market value has been less than cost, the financial performance and near-term prospect of the investee, and our intent and ability to retain the investment until the recovery of its cost. An impairment loss on the equity method investments is recognized in earnings when the decline in value is determined to be other-than-temporary and is allocated to the individual net assets underlying equity method investments in the following order: 1) reduce any equity method goodwill to zero; 2) reduce the individual basis differences related to the investee’s long-lived assets pro rata based on their amounts relative to the overall basis difference at the impairment date and 3) reduce the individual basis difference of the investee’s remaining assets in a systematic and rational manner.

In accordance with ASC Subtopic 946-320, *Financial Services—Investment Companies, Investments—Debt and Equity Securities*, we account for long-term equity investments in unlisted companies held by consolidated investment companies at fair value. These investments were initially recorded at their transaction price net of transaction costs, if any. Fair value of these investments are re-measured at each reporting date in accordance with ASC 820.

Available-for-sale debt investments are convertible debt instruments issued by private companies and investment in preferred shares that is redeemable at our option, which are measured at fair value. Interest income is recognized in earnings. All other changes in the carrying amount of these debt investments are recognized in other comprehensive income (loss).

Licensed Copyrights, net

Licensed copyrights consist of professionally-produced content such as films, television series, variety shows and other video content acquired from external parties. The license fees are capitalized and, unless prepaid, a corresponding liability is recorded when the cost of the content is known, the content is accepted by us in accordance with the conditions of the license agreement and the content is available for its first showing on our websites. Licensed copyrights are presented on the consolidated balance sheets as current and non-current, based on estimated time of usage.

Our licensed copyrights include the right to broadcast and in some instances, the right to sublicense. The broadcasting right, refers to the right to broadcast the content on its own websites and the sublicensing right, refers to the right to sublicense the underlying content to external parties. When licensed copyrights include both broadcasting and sublicensing rights, the content costs are allocated to these two rights upon initial recognition, based on the relative proportion of the estimated total revenues that will be generated by each right over its estimated useful lives.

For the right to broadcast the contents on its own websites that generates online advertising and membership services revenues, based on factors including historical and estimated future viewership

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patterns, the content costs are amortized using an accelerated method by content categories over the shorter of each content’s contractual period or estimated useful lives within ten years, beginning with the month of first availability. Content categories accounting for most of our content include newly released drama series, newly released movies, animations, library drama series and library movies. Estimates of future viewership consumption patterns and economic useful lives are reviewed periodically, at least on an annual basis and revised, if necessary. Revisions to the amortization patterns are accounted for as a change in accounting estimate prospectively in accordance with ASC Topic 250, *Accounting Changes and Error Corrections* (“ASC 250”).

For the right to sublicense the content to external parties that generates direct content distribution revenues, the content costs are amortized based on its estimated usage pattern and recorded as cost of revenues.

Produced Content, net

We produce original content in-house and collaborates with external parties. Produced content primarily consists of films, episodic series, variety shows and animations. The costs incurred in the physical production of original content includes direct production costs, production overhead and acquisition costs. Production costs for original content that are predominantly monetized in a film group are capitalized and reported separately as non-current assets with caption of “Produced content, net” on the consolidated balance sheets. Production costs for original content predominantly monetized on its own are capitalized to the extent that they are recoverable from total revenues expected to be earned (“ultimate revenue”), otherwise, they are expensed as cost of revenues. Ultimate revenue estimates include revenue expected to be earned from all sources, including exhibition, licensing, or exploitation of produced content if we have demonstrated a history of earning such revenue. We estimate ultimate revenue to be earned during the economic useful lives of produced content based on anticipated release patterns and historical results of similar produced content, which are identified based on various factors, including cast and crew, target audience and popularity. Produced content also includes cash expenditures made to acquire a proportionate share of certain rights to films including profit sharing, distribution and/or other rights. Exploitation costs are expensed as incurred.

Based on factors including historical and estimated future viewership consumption patterns, we amortize film costs for produced content that is predominantly monetized in a film group. For produced content that is monetized on its own, we consider historical and estimated usage patterns to determine the pattern of amortization for film costs. Based on the estimated patterns, we amortize produced content using an accelerated method over its estimated useful lives within ten years, beginning with the month of first availability and such costs are included in “Cost of revenues” in the consolidated statement of comprehensive income(loss).

Impairment of licensed copyrights and produced content

Our business model is mainly subscription and advertising based, as such the majority of our content assets (licensed copyrights and produced content) are predominantly monetized with other content assets, whereas a smaller portion of our content assets are predominantly monetized at a specific title level such as variety shows and investments in a proportionate share of certain rights to films including profit sharing, distribution and/or other rights. Because the identifiable cash flows related to content launched on our Mainland China platform are largely independent of the cash flows of other content launched on our overseas platform, we have identified two separate film groups. We review our film groups and individual content for impairment when there are events or changes in circumstances that indicate the fair value of a film group or individual content may be less than its unamortized costs.

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Examples of such events or changes in circumstances include, a significant adverse change in technological, regulatory, legal, economic, or social factors, that could affect the fair value of the film group or the public’s perception of a film or the availability of a film for future showings, a significant decrease in the number of subscribers or forecasted subscribers, or the loss of a major third-party agent, a change in the predominant monetization strategy of a film that is currently monetized on its own, actual costs substantially in excess of budgeted costs, substantial delays in completion or release schedules, or actual performance subsequent to release failing to meet expectations set before release such as a significant decrease in the amount of ultimate revenue expected to be recognized.

When such events or changes in circumstances are identified, we assess whether the fair value of an individual content (or film group) is less than its unamortized film costs, determines the fair value of an individual content (or film group) and recognizes an impairment charge for the amount by which the unamortized capitalized costs exceed the individual content’s (or film group’s) fair value. We mainly use an income approach to determine the fair value of an individual content or film group, for which the most significant inputs include forecasted future revenues, costs and operating expenses attributable to the film group and the discount rate. An impairment loss attributable to a film group is allocated to individual licensed copyrights and produced content within the film group on a pro rata basis using the relative carrying values of those assets as we cannot estimate the fair value of individual contents in the film group without undue cost and effort.

Business Combinations

We account for our business combinations using the purchase method of accounting in accordance with ASC Topic 805, *Business Combinations*. The purchase method of accounting requires that the consideration transferred to be allocated to the assets, including separately identifiable assets and liabilities we acquired, based on their estimated fair values. The consideration transferred in an acquisition is measured as the aggregate of the fair values at the date of exchange of the assets given, liabilities incurred, and equity instruments issued as well as the contingent considerations as of the acquisition date. The costs directly attributable to the acquisition are expensed as incurred. Identifiable assets, liabilities and contingent liabilities acquired or assumed are measured separately at their fair value as of the acquisition date, irrespective of the extent of any noncontrolling interests. The excess of (i) the total of cost of acquisition, fair value of the noncontrolling interests and acquisition date fair value of any previously held equity interest in the acquiree over (ii) the fair value of the identifiable net assets of the acquiree, is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in earnings.

In a business combination achieved in stages, we re-measured our previously held equity interest in the acquiree immediately before obtaining control at its acquisition-date fair value and the re-measurement gain or loss, if any, is recognized in earnings.

The determination and allocation of fair values to the identifiable assets acquired, liabilities assumed and noncontrolling interests is based on various assumptions and valuation methodologies requiring considerable judgment from management. The most significant variables in these valuations are discount rates and the number of years on which to base the cash flow projections, as well as the assumptions and estimates used to determine the cash inflows and outflows. We determine discount rates to be used based on the risk inherent in the related activity’s current business model and industry comparisons.

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Recently Issued And Adopted Accounting Pronouncements

Please refer to Note 2 to the Accountants’ Report in Appendix IA.

Recently Issued But Not Yet Adopted Accounting Pronouncements

Please refer to Note 2 to the Accountants’ Report in Appendix IA.

Capital Expenditures

We made capital expenditures of RMB8.8 billion, RMB6.4 billion and RMB5.1 billion (US\$779 million) in 2018, 2019 and 2020, representing 9%, 6% and 5% of our total revenues, respectively. In the years of 2018, 2019 and 2020, our capital expenditures were primarily attributable to the purchase of servers, network equipment and other computer hardware to increase our network infrastructure capacity. We funded our capital expenditures primarily with net cash flows generated from operating activities.

Our capital expenditures may increase in the future as our business continues to grow, in connection with the expansion and improvement of our network infrastructure and the construction of additional office buildings and cloud-computing based data centers. We currently plan to fund these expenditures with our current cash, cash equivalents, restricted cash, short-term investments and anticipated cash flow generated from our operating activities.

Holding Company Structure

Baidu, Inc. is a holding company with no operations of its own. We conduct our operations in China primarily through our subsidiaries and consolidated affiliated entities in China. As a result, although other means are available for us to obtain financing at the holding company level, Baidu, Inc.’s ability to pay dividends to the shareholders and to service any debt it may incur may depend upon dividends paid by our PRC subsidiaries and license and service fees paid by our PRC consolidated affiliated entities. If any of our subsidiaries incurs debt on its own behalf in the future, the instruments governing such debt may restrict its ability to pay dividends to Baidu, Inc. In addition, our PRC subsidiaries and consolidated affiliated entities are required to make appropriations to certain statutory reserve funds, which are not distributable as cash dividends except in the event of a solvent liquidation of the companies.

Our PRC subsidiaries, being foreign-invested enterprises established in China, are required to make appropriations to certain statutory reserves, namely, a general reserve fund, an enterprise expansion fund, a staff welfare fund and a bonus fund, all of which are appropriated from net profit as reported in their PRC statutory accounts. Each of our PRC subsidiaries is required to allocate at least 10% of its after-tax profits to a general reserve fund until such fund has reached 50% of its respective registered capital. Appropriations to the enterprise expansion fund and staff welfare and bonus funds are at the discretion of the board of directors of the PRC subsidiaries.

Our consolidated affiliated entities must make appropriations from their after-tax profits as reported in their PRC statutory accounts to non-distributable reserve funds, namely a statutory surplus fund, a statutory public welfare fund and a discretionary surplus fund. Each of our consolidated affiliated entities is required to allocate at least 10% of its after-tax profits to the statutory surplus fund until such fund has reached 50% of its respective registered capital. Appropriations to the statutory public welfare fund and the discretionary surplus fund are at the discretion of our consolidated affiliated entities.

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Under PRC laws and regulations, our PRC subsidiaries and consolidated affiliated entities are subject to certain restrictions with respect to paying dividends or otherwise transferring any of their net assets to us. The amounts restricted include the paid-up capital and the statutory reserve funds of our PRC subsidiaries and the net assets of our consolidated affiliated entities in which we have no legal ownership, totaling RMB25.7 billion, RMB40.8 billion and RMB45.0 billion (US\$6.9 billion) as of December 31, 2018, 2019 and 2020, respectively.

Working Capital

We recorded net current assets of RMB98.2 billion, RMB108.2 billion and RMB115.0 billion (US\$17.6 billion), respectively, as of December 31, 2018 and 2019 and 2020. The following table sets forth a breakdown of our current assets and liabilities as of the dates indicated.

| | As of December 31, | | | |
|--|--------------------|----------------|----------------|---------------|
| | 2018 | 2019 | 2020 | |
| | RMB | RMB | RMB | US\$ |
| | (in millions) | | | |
| Current assets: | | | | |
| Cash and cash equivalents | 27,638 | 33,443 | 35,782 | 5,484 |
| Restricted cash | 2,189 | 996 | 758 | 117 |
| Short-term investments, net | 111,626 | 112,924 | 126,402 | 19,372 |
| Accounts receivable, net | 6,015 | 7,416 | 8,668 | 1,328 |
| Amounts due from related parties | 785 | 1,594 | 726 | 111 |
| Other current assets, net | 6,841 | 9,189 | 11,006 | 1,687 |
| Total current assets | 155,094 | 165,562 | 183,342 | 28,099 |
| Current liabilities | | | | |
| Short-term loans | 3,046 | 2,618 | 3,016 | 462 |
| Accounts payable and accrued liabilities | 35,381 | 32,701 | 36,716 | 5,627 |
| Customer deposits and deferred revenue | 9,221 | 11,062 | 12,626 | 1,935 |
| Deferred income | 523 | 529 | 158 | 24 |
| Long-term loans, current portion | 84 | 737 | 7,427 | 1,138 |
| Notes payable, current portion | 6,871 | 5,219 | — | — |
| Convertible senior note, current portion | — | — | 4,752 | 728 |
| Amounts due to related parties | 1,727 | 2,231 | 1,324 | 203 |
| Operating lease liabilities | — | 2,283 | 2,366 | 364 |
| Total current liabilities | 56,853 | 57,380 | 68,385 | 10,481 |
| Net current assets | 98,241 | 108,182 | 114,957 | 17,618 |

For a detailed discussion on our cash position, being the balance sheet item that has material impact on our liquidity, as well as material changes in the various working capital items, see “—Liquidity and Capital Resources.”

Taking into account our current cash, cash equivalents, restricted cash and short-term investments, anticipated cash flow from operations and the estimated [REDACTED] available to us from the [REDACTED], our directors believe that we have sufficient working capital for our present requirements and for at least the next 12 months from the date of this document.

Off-Balance Sheet Arrangements

We have not entered into any financial guarantees or other commitments to guarantee the payment obligations of any third parties. We have not entered into any off-balance sheet derivative instruments. Furthermore, we do not have any retained or contingent interest in assets transferred to an

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unconsolidated entity that serves as credit, liquidity or market risk support to such entity. We do not have any variable interest in any unconsolidated entity that provides financing, liquidity, market risk or credit support to us or engages in leasing, hedging or research and development services with us.

Contractual Obligations

The following table sets forth our contractual obligations by specified categories as of December 31, 2020:

| | Payment Due by Period | | | | |
|--|-----------------------|---------------------|---------------|---------------|----------------------|
| | Total | Less Than 1 Year | 1-3 Years | 3-5 Years | More Than 5 Years |
| | (In RMB millions) | | | | |
| Long-term debt obligations ⁽¹⁾ | 84,842 | 9,807 | 26,366 | 22,953 | 25,716 |
| Operating lease obligations ⁽²⁾ | 7,839 | 2,430 | 3,289 | 1,496 | 624 |
| Purchase obligations for fixed assets | 754 | 729 | 13 | 5 | 7 |
| Purchase obligations for bandwidth and property management fees | 1,373 | 742 | 458 | 126 | 47 |
| Purchase obligations for video content ⁽³⁾ | 21,771 | 10,480 | 9,660 | 1,631 | — |
| Investment commitment obligations ⁽⁴⁾ | 1,454 | NA | NA | NA | NA |
| Total | 118,033 | 24,188 | 39,786 | 26,211 | 26,394 |

Notes:

- (1) Including estimated interest payments of RMB10.9 billion in total (RMB2.4 billion, RMB4.2 billion, RMB2.4 billion and RMB1.9 billion over the periods of less than one year, one to three years, three to five years and more than five years from December 31, 2020, respectively). Please see “Loans Payable” under Note 12, “Notes Payable” under Note 13 and “Convertible Notes” under Note 14 to the Historical Financial Information in Appendix IA.
- (2) Operating lease obligations represent our obligations for leasing internet data center facilities and office premises, which include all future cash outflows under ASC Topic 842, *Leases*. Please see “Leases” under Note 15 to the Historical Financial Information in Appendix IA.
- (3) Purchase obligations for video content consist primarily of expenditures for video content under non-cancelable agreements for licensed copyrights and produced content.
- (4) Our investment commitments primarily relate to capital contributions obligation under certain arrangements which do not have contractual maturity date.

Other than the contractual obligations set forth above, we do not have any contractual obligations that are long-term debt obligations, operating lease obligations, purchase obligations, investment commitment obligations or other long-term liabilities reflected on our consolidated balance sheet.

Material Related Party Transactions

For details relating to our related party transactions, see “Related Party Transactions”. Our Directors believe that our transactions with related parties during the Track Record Period were conducted on an arm’s length basis, and they did not distort our results of operations or make our historical results not reflective of our future performance.

Dividend Policy

Baidu, Inc., our holding company in the Cayman Islands, has never declared or paid any dividends on our ordinary shares, nor do we have any present plan to pay any cash dividends on our ordinary shares in the foreseeable future. We currently intend to retain most, if not all, of our available funds and any future earnings to operate and expand our business.

Our board of directors has complete discretion as to whether to distribute dividends, subject to Cayman Islands law. Even if our board of directors decides to pay dividends, the form, frequency and amount of

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our dividends will depend upon our future operations and earnings, capital requirements and surplus, financial condition, contractual restrictions and other factors that our board of directors may deem relevant. If we pay any dividends, our depositary will distribute such dividends to our ADS holders to the same extent as holders of our ordinary shares, subject to the terms of the deposit agreement, including the fees and expenses payable thereunder. Cash dividends on our ordinary shares, if any, will be paid in U.S. dollars.

Quantitative and Qualitative Disclosures about Market

Interest Rate Risk

Our exposure to interest rate risk primarily relates to excess cash invested in short-term instruments with original maturities of less than a year and bank borrowings that have a floating rate of interest.

Investments in both fixed rate and floating rate interest earning instruments carry a degree of interest rate risk. Fixed rate securities may have their fair market value adversely impacted due to a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may fall short of expectations due to changes in interest rates, or we may suffer losses in principal if we have to sell securities which have declined in market value due to changes in interest rates. For example, as of December 31, 2020, we had RMB126.4 billion (US\$19.4 billion) short-term investments, with a weighted average duration of 0.5 year. A hypothetical one percentage point (100 basis-point) increase in interest rates would have resulted in a decrease of RMB552 million (US\$85 million) in the fair value of our short-term investments as of December 31, 2020. We have not been, and do not expect to be, exposed to material interest rate risks relating to our investment in short-term instruments, and therefore have not used any derivative financial instruments to manage such interest risk exposure.

Our exposure to interest rate risk also arises from our bank borrowings that have a floating rate of interest. The costs of floating rate borrowings may be affected by the fluctuations in the interest rates. We manage this risk by maintaining an appropriate mix between fixed and floating rate borrowings and through the use of interest rate swap contracts. In connection with the loan facilities entered into in June 2016, we entered into four interest rate swap agreements, which effectively convert the term loans from a variable interest rate to a fixed rate, thereby managing our exposure to changes in market interest rates under the term loans.

Foreign Exchange Risk

Most of our revenues and costs are denominated in RMB, while a portion of our cash and cash equivalents, restricted cash, short-term financial assets, long-term investments, long-term loans payable, notes payable and convertible senior notes are denominated in U.S. dollars. Any significant revaluation of RMB against the U.S. dollar may materially affect our cash flows, revenues, earnings and financial position, and the value of, and any dividends payable on, our ADS in U.S. dollars. See “Risk Factors—Risks Related to Doing Business in China—Fluctuation in exchange rates could have a material and adverse effect on our results of operations and the value of your [REDACTED]” In addition, we commenced operation in Japan in late 2007. To the extent we need to make capital injections into our Japan operation by converting U.S. dollars into Japanese Yen, we will be exposed to the fluctuations in the exchange rate between the U.S. dollar and the Japanese Yen. We have not used any derivative financial instruments to hedge exposure to foreign exchange risk. The value of your [REDACTED] in our ADSs will be affected by the exchange rate between U.S. dollar and Renminbi because the value of our business is effectively denominated in RMB, while our ADSs will be traded in U.S. dollars.

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The conversion of Renminbi into foreign currencies, including U.S. dollars, is based on rates set by the People’s Bank of China. The Renminbi has fluctuated against the U.S. dollar, at times significantly and unpredictably. It is difficult to predict how market forces or PRC or U.S. government policy may impact the exchange rate between Renminbi and the U.S. dollar in the future.

To the extent that we need to convert U.S. dollars into Renminbi for our operations, appreciation of the Renminbi against the U.S. dollar would have an adverse effect on the RMB amount we receive from the conversion. Conversely, if we decide to convert Renminbi into U.S. dollars for the purpose of making payments for dividends on our ordinary shares or ADSs, repay indebtedness denominated in U.S. dollars, or for other business purposes, appreciation of the U.S. dollar against the Renminbi would have a negative effect on the U.S. dollar amounts available to us.

As of December 31, 2019, we had RMB-denominated cash and cash equivalents, restricted cash and short-term investments of RMB122.0 billion, and U.S. dollar-denominated cash and cash equivalents, restricted cash and short-term investments of US\$2.8 billion. Assuming we had converted RMB122.0 billion into U.S. dollars at the exchange rate of RMB 6.9618 per US\$1.00 as of the end of 2019, our U.S. dollar cash balance would have been US\$20.3 billion. If the RMB had depreciated by 10% against the U.S. dollar, our U.S. dollar cash balance would have been US\$18.7 billion instead. In addition, we had U.S. dollar-denominated long-term loans payable, notes payable and convertible senior notes of US\$9.2 billion as of December 31, 2019. If the RMB had depreciated by 10% against the U.S. dollar, we would have experienced an increase of RMB6.4 billion in the value of our U.S. dollar-denominated long-term loans payable and notes payable as of December 31, 2019.

As of December 31, 2020, we had RMB-denominated cash and cash equivalents, restricted cash and short-term investments of RMB143.9 billion, and U.S. dollar-denominated cash and cash equivalents, restricted cash and short-term investments of US\$2.8 billion. Assuming we had converted RMB143.9 billion into U.S. dollars at the exchange rate of RMB6.5250 for US\$1.00 as of December 31, 2020, our U.S. dollar cash balance would have been US\$24.9 billion. If the RMB had depreciated by 10% against the U.S. dollar, our U.S. dollar cash balance would have been US\$22.6 billion instead. In addition, we had U.S. dollar-denominated short-term borrowings, long-term loans payable (including current portion), notes payable and convertible senior notes (including current portion) of US\$11.2 billion as of December 31, 2020. A hypothetical 10% increase in the exchange rate of the U.S. dollar against the RMB would have resulted in an increase of RMB7.3 billion (US\$1.1 billion) in the value of our U.S. dollar-denominated short-term borrowings, long-term loans payable (including current portion) notes payable and convertible senior notes (including current portion) as of December 31, 2020.

Credit Risk

Financial instruments that potentially subject us to significant concentration of credit risk primarily consist of cash and cash equivalents, restricted cash, debt investments, accounts receivable, contract assets, receivables from online payment agencies and amounts due from related parties. As of December 31, 2019, we had RMB147.4 billion in cash and cash equivalents, restricted cash and debt investments, 92% and 8% of which are held by financial institutions in the PRC and international financial institutions outside of the PRC, respectively. Our total cash and cash equivalents, restricted cash and debt investments held at three financial institutions in the PRC exceeded 10%, representing 24%, 21% and 18% of our total cash and cash equivalents, restricted cash, debt investments, as of December 31, 2019, respectively. As of December 31, 2020, we had RMB172.7 billion in cash and cash equivalents, restricted cash and debt investments, 90% and 10% of which are held by financial institutions in the PRC and international financial institutions outside of the PRC, respectively. Our

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total cash and cash equivalents, restricted cash and debt investments held at four financial institutions in the PRC exceeded 10%, representing 30%, 21%, 16% and 11% of our total cash and cash equivalents restricted cash, and debt investments as of December 31, 2020, respectively.

Accounts receivable and contract assets are typically unsecured and derived from revenue earned from customers and third-party agents in China, which are exposed to credit risk. The risk is mitigated by credit evaluations we perform on its customers and its ongoing monitoring process of outstanding balances. We maintain allowance for estimated and expected credit losses. As of December 31, 2018, 2019 and 2020, we had no single customer with a receivable balance exceeding 10% of the total accounts receivable balance. Amounts due from related parties are typically unsecured and we maintain allowance for estimated and expected credit losses.

Inflation

Inflation in China has not materially impacted our results of operations. According to the National Bureau of Statistics of China, the annual average percent changes in the consumer price index in China for 2018, 2019 and 2020 were 2.1%, 2.9% and 2.5%, respectively. The year-over-year percent change in the consumer price index for January 2019, 2020 and 2021 was an increase of 1.7%, an increase of 5.4% and a decrease of 0.3%, respectively. Although we have not been materially affected by inflation in the past, we can provide no assurance that we will not be affected in the future by higher rates of inflation in China. For example, certain operating costs and expenses, such as employee compensation and office operating expenses may increase as a result of higher inflation. Additionally, because a substantial portion of our assets consists of cash and cash equivalents and short-term investments, high inflation could significantly reduce the value and purchasing power of these assets. We are not able to hedge our exposure to higher inflation in China.

No Material Adverse Change

After due and careful consideration, our Directors confirm that except as disclosed in “—Impact of COVID-19 on Our Operations” and elsewhere in this document, up to the date of this document, there has been no material adverse change in our financial or trading position or prospects since December 31, 2020, and there has been no event since December 31, 2020 which would materially affect the information shown in our consolidated financial statements included in the Accountants’ Report in Appendix IA to this document.

Financial Information of YY Live

Baidu (Hong Kong) Limited, our wholly-owned subsidiary, and JOYY entered into a share purchase agreement on November 16, 2020, and subsequently amended the share purchase agreement on February 7, 2021. Pursuant to the agreement, we agreed to acquire JOYY’s domestic video-based entertainment live streaming business in China which is referred to as YY Live, for an aggregate purchase price of approximately US\$3.6 billion in cash, subject to certain adjustments. Approximately US\$2.0 billion of the purchase price would be payable to JOYY at the closing of the acquisition, subject to certain adjustments. After the closing, subject to certain conditions and adjustments, approximately US\$1.0 billion would be payable no later than the later of the closing and April 30, 2021, and approximately US\$300 million would be paid no later than the later of the closing of the acquisition and June 30, 2021, and a maximum amount of US\$300 million would be payable subject to the achievement of certain conditions. The acquisition has been substantially completed, with certain customary matters remaining to be completed in the near future. See “Recent Developments—Business Updates.”

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YY Live is a video-based live streaming platform in China offering content such as music and dance shows, talk shows, outdoor activities, sports and anime. Users of YY Live may enjoy the live streaming services on YY Live platform through YY mobile app, YY.com website and PC YY. Users access content on the platform free of charge, but are charged for purchases of virtual items. YY Live generates revenue from the sales of in-channel virtual items used on its platform as tips for live streaming hosts. We may be subject to a variety of risks associated with the online live streaming business of YY Live. See “Risk Factors—Risks Related to Our Business and Industry—We face risks associated with our proposed acquisition of YY Live and its online live streaming business.”

Selected Statements of Operations items

Revenues. YY Live generates (i) live streaming revenue from the sales of in-channel virtual items used on its live streaming platform and (ii) other revenue mainly from memberships services and advertising revenue.

Cost of revenues. Cost of revenues of YY Live consists primarily of (i) revenue sharing fees and content costs including payments to various talent agencies and performers, and content providers, (ii) bandwidth costs, (iii) payment handling costs, (iv) salaries and benefits, (v) technical service fee, (vi) depreciation and amortization expense for servers, other equipment and intangibles directly related to operating the platform, (vii) share-based compensation, (viii) other taxes and surcharges and (ix) other costs.

Sales and marketing expenses. Sales and marketing expenses of YY Live consist primarily of (i) advertising and promotion expenses and (ii) salaries and benefits for sales and marketing personnel.

Research and development expenses. Research and development expenses of YY Live consist primarily of (i) salary and welfare for research and development personnel, (ii) share-based compensation for research and development personnel, (iii) depreciation of office premise and servers utilized by research and development personnel, and (iv) rental expenses..

General and administrative expenses. General and administrative expenses of YY Live consist primarily of (i) share-based compensation for management and administrative personnel, (ii) salary and welfare for general and administrative personnel, (iii) impairment charge, and (iv) professional service fees.

Other income. Other income of YY Live primarily consists of government grants in connection with its contributions to tax refund.

Taxation

PRC

YY Live’s consolidated entities in China are governed by the Enterprise Income Tax Law (“EIT Law”), which became effective on January 1, 2008. Pursuant to the EIT Law and its implementation rules, enterprises in China are generally subject to tax at a statutory rate of 25%. Certified High and New Technology Enterprises (“HNTE”) are entitled to a favorable tax rate of 15%, but need to re-apply every three years. During this three-year period, an HNTE must conduct a qualification self-review each year to ensure it meets the HNTE criteria and is eligible for the 15% preferential tax rate for that year. If an HNTE fails to meet the criteria for qualification in any year, the enterprise cannot enjoy the preferential tax rate in that year, and must instead use the regular 25% EIT rate. Enterprises qualified as software enterprises can enjoy an income tax exemption for two years beginning with their

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first profitable year and a 50% tax reduction to the applicable tax rate for the subsequent three years. An entity that qualifies as a “Key National Software Enterprise” (a “KNSE”) is entitled to a further reduced preferential income tax rate of 10%. A number of YY Live’s consolidated entities qualified as HNTE or KNSE and enjoyed preferential income tax rates for the periods reported.

According to a policy promulgated by the State Tax Bureau of the PRC and effective from 2008 onwards, enterprises engaged in research and development activities are entitled to claim an additional tax deduction amounting to 50% of the qualified research and development expenses incurred in determining its tax assessable profits for that year. The additional tax deducting amount of the qualified research and development expenses have been increased from 50% to 75%, effective from 2018 to 2020, according to a new tax incentives policy promulgated by the State Tax Bureau of the PRC in September 2018 (“Super Deduction”). A number of YY Live’s consolidated entities claimed the Super Deduction in ascertaining the tax assessable profits for the periods reported.

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Results of Operations

The following table sets forth a summary of YY Live’s results of operations for the periods indicated. The period-to-period comparisons of results of operations should not be relied upon as indicative of future performance. The financial statements of YY Live were prepared on a carve-out basis and the presentation may not necessarily reflect the financial position, the results of operation or the cash flows of YY Live had it actually existed on a stand-alone basis during the years presented. For more details of the preparation basis of the financial statements of YY Live, please refer to note 1(c) to Appendix IB Accountant’s Report of YY Live.

| | Year ended December 31, | | | |
|--|-------------------------|--------------------|--------------------|------------------|
| | 2018 | 2019 | 2020 | |
| | RMB | RMB | RMB | US\$ |
| | (in thousands) | | | |
| Net revenues: | | | | |
| Live streaming | 10,073,347 | 10,721,295 | 9,664,816 | 1,481,198 |
| Others | 199,349 | 241,243 | 285,470 | 43,750 |
| Total net revenues | 10,272,696 | 10,962,538 | 9,950,286 | 1,524,948 |
| Cost of revenues ⁽¹⁾ | (5,357,786) | (5,703,255) | (5,342,372) | (818,754) |
| Gross profit | 4,914,910 | 5,259,283 | 4,607,914 | 706,194 |
| Operating expenses⁽¹⁾ : | | | | |
| Sales and marketing expenses | (498,211) | (506,605) | (581,091) | (89,056) |
| Research and development expenses | (412,046) | (393,100) | (362,406) | (55,541) |
| General and administrative expense | (203,678) | (198,450) | (152,866) | (23,428) |
| Total operating expenses | (1,113,935) | (1,098,155) | (1,096,363) | (168,025) |
| Other income | 67,018 | 203,408 | 166,272 | 25,482 |
| Operating income | 3,867,993 | 4,364,536 | 3,677,823 | 563,651 |
| Interest income and investment income | 1,565 | 2,455 | 2,899 | 444 |
| Income before income tax expenses | 3,869,558 | 4,366,991 | 3,680,722 | 564,095 |
| Income tax expenses | (580,935) | (666,311) | (539,435) | (82,672) |
| Net income | 3,288,623 | 3,700,680 | 3,141,287 | 481,423 |

Note:

(1) Share-based compensation expenses was allocated in cost of revenues and operating expenses as follows:

| | | | | |
|---|--------|--------|--------|-------|
| Cost of revenues | 17,494 | 8,655 | 11,241 | 1,723 |
| Research and development expenses | 97,945 | 56,960 | 45,861 | 7,029 |
| Sales and marketing expenses | 2,473 | 1,799 | 1,276 | 196 |
| General and administrative expenses | 75,284 | 72,913 | 34,344 | 5,263 |

Year Ended December 31, 2020 Compared to Year Ended December 31, 2019

Total net revenues. YY Live’s total net revenues decreased by 9% from RMB10,962.5 million in 2019 to RMB9,950.3 million (US\$1,524.9 million) in 2020.

Live streaming revenue. Live streaming revenue of YY Live decreased by 10% from RMB10,721.3 million in 2019 to RMB9,664.8 million (US\$1,481.2 million) in 2020, due to the combined effect of increase in number of paying users from 9.4 million in 2019 to 10.3 million in 2020 and decrease of ARPU from RMB1,138 in 2019 to RMB937 in 2020 due to COVID-19’s impact. YY Live’s number of paying users during a given period is the cumulative number of registered user accounts that have purchased virtual items or other products and services on YY Live at least once

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during the relevant period. YY Live’s ARPU is calculated by dividing total live streaming revenue during a given period by the number of paying users for that period.

Other revenue. Other revenue of YY Live increased by 18% from RMB241.2 million in 2019 to RMB285.5 million (US\$43.8 million) in 2020, which was primarily due to an increase in membership fees.

Cost of revenues. Cost of revenues of YY Live decreased by 6% from RMB5,703.3 million in 2019 to RMB5,342.4 million (US\$818.8 million) in 2020. This decrease was primarily due to the decrease of revenue sharing fees resulting from the decreased revenue.

Sales and marketing expenses. Sales and marketing expenses of YY Live increased by 15% from RMB506.6 million in 2019 to RMB581.1 million (US\$89.1 million) in 2020. This increase was primarily due to increase of promotional expenses for user acquisition.

Research and development expenses. Research and development expenses of YY Live decreased by 8% from RMB393.1 million in 2019 to RMB362.4 million (US\$55.5 million) in 2020, primarily due to the decrease of share-based compensation related to research and development personnel resulted from less new grants made.

General and administrative expenses. General and administrative expenses of YY Live decreased by 23% from RMB198.5 million in 2019 to RMB152.9 million (US\$23.4 million) in 2020, primarily due to the decrease of share-based compensation resulted from less grant made.

Other income. Other income of YY Live was RMB166.3 million (US\$25.5 million) in 2020, compared to an other income of RMB203.4 million in 2019, primarily attributable to the decrease of government grants received.

Income tax expenses. Income tax expenses of YY Live decreased by 19% from RMB666.3 million in 2019 to RMB539.4 million (US\$82.7 million) in 2020, primarily due to lowered taxable income.

Net income. As a result of the foregoing, YY Live generated a net income of RMB3,141.3 million (US\$481.4 million) in 2020, representing a 15% decrease from RMB3,700.7 million in 2019.

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

Total net revenues. YY Live’s total net revenues increased by 7% from RMB10,272.7 million in 2018 to RMB10,962.5 million in 2019, primarily due to the growth in live streaming revenues.

Live streaming revenue. YY Live’s live streaming revenue increased by 6% from RMB10,073.3 million in 2018 to RMB10,721.3 million in 2019, due to the combined effect of increase in the number of paying users on YY Live from 8.6 million in 2018 to 9.4 million in 2019 and decrease of ARPU from RMB1,170 in 2018 to RMB1,138 in 2019.

Other revenue. YY Live’s other revenues increased by 21% from RMB199.3 million in 2018 to RMB241.2 million in 2019, which was primarily due to an increase in membership fees.

Cost of revenues. Cost of revenues of YY Live increased by 6% from RMB5,357.8 million in 2018 to RMB5,703.3 million in 2019, which was largely in line with the increase in total revenues.

Sales and marketing expenses. Sales and marketing expenses of YY Live increased by 2% from RMB498.2 million in 2018 to RMB506.6 million in 2019.

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Research and development expenses. Research and development expenses of YY Live decreased by 5% from RMB412.0 million in 2018 to RMB393.1 million in 2019, primarily due to the decrease of share-based compensation related to research and development personnel resulted from less new grants made.

General and administrative expenses. General and administrative expenses of YY Live decreased by 3% from RMB203.7 million in 2018 to RMB198.5 million in 2019.

Other income. Other income of YY Live was RMB203.4 million in 2019, increasing by 204% from RMB67.0 million in 2018, primarily due to an increase in government grants received.

Income tax expenses. Income tax expenses of YY Live increased by 15% from RMB580.9 million in 2018 to RMB666.3 million in 2019, in line with the taxable income growth.

Net income. As a result of the foregoing, YY Live generated a net income of RMB3,700.7 million in 2019, representing a 13% increase from RMB3,288.6 million in 2018.

Liquidity and Capital Resources

As of December 31, 2020, YY Live had RMB206.2 million (US\$31.6 million) cash and cash equivalents. YY Live’s cash and cash equivalents consist of cash on hand and investments in interest bearing liquid investments. During the Track Record Period, YY Live have financed its operations primarily through cash flows from operations.

Cash Flows

The following table sets forth a summary of YY Live’s cash flows for the periods indicated:

| | Year ended December 31, | | | |
|--|-------------------------|---------------|----------------|---------------|
| | 2018 | 2019 | 2020 | |
| | RMB | RMB | RMB | US\$ |
| | (in thousands) | | | |
| Net cash provided by operating activities | 3,787,985 | 3,815,151 | 3,093,275 | 474,066 |
| Net cash (used in) provided by investing activities | (26,404) | (192,783) | 45,208 | 6,928 |
| Net cash used in financing activities | (3,723,605) | (3,600,884) | (3,002,014) | (460,079) |
| Net increase in cash and cash equivalents | 37,976 | 21,484 | 136,469 | 20,915 |
| Cash and cash equivalents at the beginning of the year | 10,262 | 48,238 | 69,722 | 10,685 |
| Cash and cash equivalents at the end of the year | <u>48,238</u> | <u>69,722</u> | <u>206,191</u> | <u>31,600</u> |

Operating Activities

Net cash provided by operating activities amounted to RMB3,093.3million (US\$474.1 million) in 2020. The difference between net cash provided by operating activities and net income of RMB3,141.3million (US\$481.4 million) was primarily due to an increase in accounts receivable of RMB128.0 million (US\$19.6 million) and a decrease in deferred revenue of RMB58.3 million (US\$8.9 million), partially offset by a non-cash item adjustment in share-based compensation of RMB92.7 million (US\$14.2 million).

Net cash provided by operating activities amounted to RMB3,815.2 million in 2019. The difference between net cash provided by operating activities and net income of RMB3,700.7 million was primarily due to a non-cash item adjustment in share-based compensation of RMB140.3 million, partially offset by a decrease in accrued liabilities and other current liabilities of RMB31.7 million.

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Net cash provided by operating activities amounted to RMB3,788.0 million in 2018. The difference between net cash provided by operating activities and net income of RMB3,288.6 million was primarily due to a non-cash item adjustment in share-based compensation of RMB193.2 million and an increase in accrued liabilities and other current liabilities of RMB208.6 million, partially offset by a decrease in deferred revenue of RMB23.4 million.

Investing Activities

Net cash provided by investing activities amounted to RMB45.2 million (US\$6.9 million) in 2020. Net cash provided by investing activities primarily resulted from maturities of short-term investments of RMB130.0 million (US\$19.9 million), partially offset by placement of short-term investments of RMB60 million (US\$9.2 million).

Net cash used in investing activities amounted to RMB192.8 million in 2019. Net cash used in investing activities primarily resulted from placement of short-term investments of RMB121.8 million and purchase of property and equipment of RMB72.7 million.

Net cash used in investing activities amounted to RMB26.4 million in 2018. Net cash used in investing activities primarily resulted from purchase of property and equipment of RMB27.2 million.

Financing Activities

Net cash used in financing activities was RMB3,002.0 million (US\$460.1 million) in 2020, attributable to contribution to JOYY.

Net cash used in financing activities was RMB3,600.9 million in 2019, attributable to contribution to JOYY.

Net cash used in financing activities was RMB3,723.6 million in 2018, attributable to contribution to JOYY.

For more discussion on how the contributions to JOYY in the cash flows were derived, please refer to note 1(c) to Appendix IB Accountant’s Report of YY Live.

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Working Capital

The following table sets forth a breakdown of YY Live’s current assets and liabilities as of the dates indicated.

| | As of December 31, | | | |
|---|--------------------|------------------|------------------|----------------|
| | 2018 | 2019 | 2020 | |
| | RMB | RMB | RMB | US\$ |
| | (in thousands) | | | |
| Current assets: | | | | |
| Cash and cash equivalents | 48,238 | 69,722 | 206,191 | 31,600 |
| Short-term investments | — | 70,327 | — | — |
| Accounts receivable, net | 74,253 | 79,430 | 206,580 | 31,660 |
| Amounts due from related parties | 1,537 | 1,087 | 456 | 70 |
| Prepayments and other current assets | 25,785 | 39,205 | 45,001 | 6,897 |
| Total current assets | 149,813 | 259,771 | 458,228 | 70,227 |
| Current liabilities | | | | |
| Income taxes payable | — | 3,459 | 21,014 | 3,221 |
| Accrued liabilities and other current liabilities | 936,667 | 904,918 | 907,692 | 139,110 |
| Advances from customers | 80,504 | 97,928 | 80,761 | 12,377 |
| Deferred revenue | 425,226 | 355,549 | 326,702 | 50,069 |
| Total current liabilities | 1,442,397 | 1,361,854 | 1,336,169 | 204,777 |

YY Live recorded net current liabilities of RMB1,292.6 million, RMB1,102.1 million and RMB877.9 million (US\$134.6 million) as of December 31, 2018, 2019 and 2020, respectively, primarily due to accrued liabilities and other current liabilities and deferred revenue.

Certain Balance Sheet Items

Accrued liabilities and other current liabilities

YY Live’s accrued liabilities and other current liabilities primarily include accrued revenue sharing fees, accrued salaries and welfare and accrued promotion expenses. YY Live’s accrued liabilities and other current liabilities increased by 0.3% from RMB904.9 million as of December 31, 2019 to RMB907.7 million (US\$139.1 million) as of December 31, 2020. YY Live’s accrued liabilities and other current liabilities decreased by 3.4% from RMB936.7 million as of December 31, 2018 to RMB904.9 million as of December 31, 2019, primarily due to the decrease of revenue sharing payable to live streaming talent agencies and performers.

Deferred revenue, current

YY Live’s deferred revenue primarily consists of prepaid subscriptions under membership program and unamortized revenue from virtual items. YY Live’s current deferred revenue decreased by 8% from RMB355.5 million as of December 31, 2019 to RMB326.7 million (US\$50.1 million) as of December 31, 2020, primarily due to decrease in live streaming revenue. YY Live’s current deferred revenue decreased by 16% from RMB425.2 million as of December 31, 2018 to RMB355.5 million as of December 31, 2019, primarily due to one upfront recharge promotion activity conducted in 2018 year end and no such activity in 2019 year end.

Advances from customers

YY Live’s advances from customers primarily consist of prepayments from users in the form of virtual currency that are not yet consumed or converted into virtual items. YY Live’s advances from

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customers decreased by 18% from RMB97.9 million as of December 31, 2019 to RMB80.8 million (US\$12.4 million) as of December 31, 2020, primarily due to the decrease of live streaming revenue. YY Live’s advances from customers increased by 22% from RMB80.5 million as of December 31, 2018 to RMB97.9 million as of December 31, 2019, primarily due to the increase of live streaming revenue.

Accounts Receivable, net

YY Live’s accounts receivable, net mainly consist of amounts due from live streaming service users to be collected from payment platforms. YY Live’s accounts receivable, net increased by 160% from RMB79.4 million as of December 31, 2019 to RMB206.6 million (US\$31.7 million) as of December 31, 2020, primarily due to delayed withdrawal from third party online payment platforms. YY Live’s accounts receivable, net increased by 7% from RMB74.3 million as of December 31, 2018 to RMB79.4 million as of December 31, 2019, which was largely in line with the increase in total revenues.

Listing Expenses

We expect to incur listing expenses of up to approximately RMB[REDACTED] million (assuming that the [REDACTED] is conducted at the indicative [REDACTED] per [REDACTED] of HK\$[REDACTED] for both [REDACTED] and [REDACTED] and the [REDACTED] is not exercised). We expect to recognize RMB[REDACTED] million as general and administrative expenses in the fiscal year ending December 31, 2021 and RMB[REDACTED] million as a deduction in equity directly.

Unaudited Pro Forma Adjusted Net Tangible Assets

The following unaudited pro forma adjusted net tangible assets prepared in accordance with Rule 4.29 of the Hong Kong Listing Rules are set out below for the purpose of illustrating the effect of the [REDACTED] on the consolidated net tangible assets attributable to the ordinary shareholders of the Company as at December 31, 2020 as if the [REDACTED] had taken place on that date.

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The unaudited pro forma adjusted net tangible assets has been prepared for illustrative purposes only and because of its hypothetical nature, it may not give a true picture of the consolidated net tangible assets of the Company, had the [REDACTED] been completed as of December 31, 2020 or at any future dates. It is prepared based on the consolidated net tangible assets attributable to ordinary shareholders of the Company as of December 31, 2020 as derived from the Company’s consolidated financial statements for the year ended December 31, 2020 included in Appendix IA, and adjusted as described below.

| | Unaudited consolidated net tangible assets attributable to ordinary shareholders of the Company as of December 31, 2020 | Estimated [REDACTED] from the [REDACTED] | Unaudited pro forma adjusted net tangible assets attributable to ordinary shareholders of the Company as of December 31, 2020 | Unaudited pro forma adjusted net tangible assets per Share | Unaudited pro forma adjusted net tangible assets per ADS | Unaudited pro forma adjusted net tangible assets per Share | Unaudited pro forma adjusted net tangible assets per ADS |
|--|---|--|---|--|--|--|--|
| | (in millions of RMB) (Note 1) | (in millions of RMB) (Note 2) | (in millions of RMB) | RMB (Note 3) | RMB (Note 4) | HK\$ (Note 5) | HK\$ (Note 5) |
| Based on an indicative [REDACTED] of HK\$[REDACTED] per [REDACTED] . . . | 158,426 | [REDACTED] | [REDACTED] | [REDACTED] | [REDACTED] | [REDACTED] | [REDACTED] |

Notes:

- (1) The unaudited consolidated net tangible assets attributable to ordinary shareholders of the Company as of December 31, 2020 is arrived at after deducting Intangible assets, net of RMB2,022 million and Goodwill of RMB22,248 million from the Total Baidu, Inc. shareholders’ equity of RMB182,696 million as of December 31, 2020, as shown in the Accountants’ Report as set out in Appendix IA to the [REDACTED]. For the avoidance of doubt, “Licensed copyrights, net” and “Produced content, net” were not deducted for the purpose of calculating the unaudited consolidated net tangible assets attributable to ordinary shareholders of the Company.
[REDACTED]
- (3) The unaudited pro forma adjusted net tangible assets attributable to ordinary shareholders of the Company per Share is calculated based on a total of [REDACTED] Shares that will be in issue assuming that the [REDACTED] have been completed on December 31, 2020, and after having accounted for the Share Subdivision but do not take into account any [REDACTED] of [REDACTED] upon exercise of the [REDACTED], the Shares to be issued pursuant to the Share Incentive Plans, including pursuant to the exercise of options or other awards that have been or may be granted from time to time and any issuance or repurchase of Shares by the Company.
- (4) The unaudited pro forma adjusted net tangible assets attributable to ordinary shareholders of the Company per ADS is calculated based on that eight Shares equals one ADS.
- (5) The unaudited pro forma adjusted net tangible assets per Share and the unaudited pro forma adjusted net tangible assets per ADS are converted into Hong Kong dollars at an exchange rate of RMB0.8416 to HK\$1.00.
- (6) Assuming the Company’s acquisition of YY Live (as defined in the [REDACTED]) had been completed on December 31, 2020, the unaudited pro forma adjusted net tangible assets per Share and the unaudited pro forma adjusted net tangible assets per ADS would have been RMB[REDACTED] or HK\$[REDACTED] and RMB[REDACTED] or HK\$[REDACTED], respectively. No adjustment has been made to reflect any trading result, or other transactions of the Group entered into subsequent to December 31, 2020.

RELATIONSHIP WITH THE CONTROLLING SHAREHOLDERS

CONTROLLING SHAREHOLDERS

Immediately following the [REDACTED], Mr. Robin Yanhong Li, our chairman and chief executive officer, will be interested in and will control through: (i) 3,013,200 Class A Ordinary Shares directly held by Mr. Robin Yanhong Li on record, (ii) 2,232,000 Class A ordinary shares in the form of ADSs held by Mr. Robin Yanhong Li in the brokerage account of the administrator of our employee stock option program, (iii) 342,320 Class A Ordinary Shares issuable to Mr. Robin Yanhong Li upon exercise of options within 60 days after the Latest Practicable Date, (iv) 14,560 Class A Ordinary Shares issuable to Mr. Robin Yanhong Li upon vesting of restricted shares within 60 days after the Latest Practicable Date, (v) 439,200,000 Class B Ordinary Shares held on record by Handsome Reward Limited, a British Virgin Islands company wholly owned by Mr. Robin Yanhong Li, (vi) 5,772,720 Class A ordinary shares in the form of ADSs held by Handsome Reward Limited in the brokerage account of the administrator of our employee stock option program, (vii) 6,916,480 Class A Ordinary Shares issuable to Handsome Reward Limited upon exercise of options within 60 days after the Latest Practicable Date. See “Directors and Senior Management—Compensation—Share Incentive Plans” for details of our employee share incentive plan.

Without taking into account (i) any allotment and issuance of Class A ordinary shares upon exercise of the [REDACTED], (ii) the Class A ordinary shares to be issued pursuant to the Share Incentive Plans, including pursuant to the exercise of options or other awards that have been or may be granted from time to time to grantees other than Mr. Robin Yanhong Li and Handsome Reward Limited and (iii) any issuance or repurchase of Shares and/or ADSs that we may make, Mr. Li’s aggregated shareholding will be approximately [REDACTED] of our issued share capital and he will hold approximately [REDACTED] of the voting rights in the Company through shares beneficially owned by him and capable of being exercised on resolutions in general meetings. Therefore, Mr. Li will be a Controlling Shareholder after the Listing. For more information on Mr. Li’s shareholding, please see “Major Shareholders”.

INDEPENDENCE FROM CONTROLLING SHAREHOLDERS

Having considered the following factors, our directors are satisfied that we are capable of carrying on our business independently of our controlling shareholders and their close associates after the Listing.

Management independence

Our business is managed and conducted by our board and senior management. Our board consists of five directors, of whom four are independent directors unrelated to our Controlling Shareholders. For more information, please see “Directors and Senior Management.”

Our directors consider that our board and senior management will function independently of our controlling shareholders because:

- (a) each director is aware of his/her fiduciary duties as a director, which require, among other things, that he/she acts for the benefit, and in the interests, of our Company and does not allow any conflict between his/her duties as a director and his/her personal interests;
- (b) our daily management and operations are carried out by our senior management, all of whom have substantial experience in our Group’s business and/or the industry in which we operate, and will be able to make decisions that are in the best interest of our Group;
- (c) we have four independent directors and certain matters of our Company will always be referred to them for review and/or approval;

RELATIONSHIP WITH THE CONTROLLING SHAREHOLDERS

- (d) in the event that there is a potential conflict of interest arising out of any transaction to be entered into between our Group and our directors or their respective associates, the interested director(s) is required to declare the nature of his/her interest before voting at the relevant meeting(s) in respect of that transaction; and
- (e) we have adopted a series of corporate governance measures to manage conflicts of interest, if any, between our Group and our Controlling Shareholders that would support our independent management; see “—Corporate Governance Measures” in this section.

Operational Independence

Our Group is not operationally dependent on our controlling shareholders. Our Group holds all material licenses and owns all relevant intellectual properties and research and development facilities necessary to carry on our business. We have sufficient capital, facilities, equipment and employees to operate our business independently of our controlling shareholders. Our access to, and relationship with, our customers and suppliers are independent of our Controlling Shareholders, and we have an independent management team that operates our business.

Financial Independence

We have independent internal control and accounting systems. We also have an independent finance department responsible for discharging the treasury function, and an audit committee comprising solely of independent directors to oversee our accounting and financial reporting processes. We are capable of obtaining financing from third parties, if necessary, without reliance on our Controlling Shareholders.

No loans or guarantees provided by, or granted to, our Controlling Shareholders or their respective associates will be outstanding as of the Latest Practicable Date.

Based on the above, our directors believe that our board as a whole and together with our senior management team are able to manage, operate and carry on our business independently of, and do not place undue reliance on, our Controlling Shareholders and their respective close associates.

DISCLOSURE UNDER RULE 8.10 OF THE HONG KONG LISTING RULES

Our Controlling Shareholders and/or our directors may, from time to time, make minority investments or hold non-executive board positions in entities that operate in, or have subsidiaries that operate in, the broader industries in which all of our business segments also operate. As our Controlling Shareholders and/or directors have no executive or shareholding control over any of these entities, and these entities have separate businesses with separate management and shareholder bases that control their entities, our controlling shareholders will not inject any of their interested entities into our Group; and to the extent our directors hold non-executive board positions or make minority investments in these entities, we believe that this strengthens the experience and diversity of our directors, as a group, and signifies their passion for the industries in which we operate.

Our Controlling Shareholders and directors confirm that as of the Latest Practicable Date, they did not have any interest in a business, apart from the business of our Group, which competes or is likely to compete, directly or indirectly, with our principal business that would require disclosure under Rule 8.10 of the Hong Kong Listing Rules.

RELATIONSHIP WITH THE CONTROLLING SHAREHOLDERS

CORPORATE GOVERNANCE MEASURES

Our directors recognize the importance of good corporate governance in protecting our shareholders’ interests. We have adopted the following measures to ensure good corporate governance standards and to avoid potential conflicts of interest between our Group and our Controlling Shareholders:

- (a) where our directors reasonably request the advice of independent professionals, such as financial advisors, the appointment of such independent professionals will be made at our Company’s expense;
- (b) we have appointed Somerley Capital Limited as our compliance advisor to provide advice and guidance to us in respect of compliance with the applicable laws, as well as the Hong Kong Listing Rules, including various requirements relating to corporate governance; and
- (c) we have established our audit committee, compensation committee, and corporate governance and nominating committee with written terms of reference in compliance with the rules of Nasdaq. All of the members of our audit committee, including the chairman, are independent directors.

Based on the above, our directors are satisfied that we have sufficient corporate governance measures in place to manage conflicts of interest that may arise between our Group and our Controlling Shareholders, and to protect our minority shareholders’ interests after the Listing.

DIRECTORS AND SENIOR MANAGEMENT

OVERVIEW

The following table sets forth information regarding our directors and senior management.

| Name | Age | Position/Title | Date of appointment | Year of joining our Group |
|---------------------------------------|-----|--|---------------------|---------------------------|
| <i>Directors⁽¹⁾</i> | | | | |
| Robin Yanhong Li | 52 | Chairman of the board of directors and Chief Executive Officer | January 2000 | 2000 |
| James Ding | 55 | Independent director ⁽²⁾ | August 2005 | 2005 |
| Brent Callinicos | 55 | Independent director ⁽²⁾ | October 2015 | 2015 |
| Yuanqing Yang | 56 | Independent director ⁽²⁾ | October 2015 | 2015 |
| Jixun Foo | 52 | Independent director ⁽²⁾ | July 2019 | 2019 |
| <i>Senior Management</i> | | | | |
| Herman Yu | 50 | Chief Financial Officer | September 2017 | 2017 |
| Haifeng Wang | 49 | Chief Technology Officer | May 2019 | 2010 |
| Dou Shen | 41 | Executive Vice President | May 2019 | 2012 |
| Shanshan Cui | 45 | Senior Vice President | May 2019 | 2000 |
| Victor Zhixiang Liang | 47 | Senior Vice President ⁽³⁾ | June 2011 | 2005 |

Notes:

- (1) Our board consists of five directors, including four independent directors. See “—Board Practices” for the functions and duties of our board. Our board is responsible for exercising other powers, functions and duties in accordance with the Articles of Association, and all applicable laws, including the Hong Kong Listing Rules.
- (2) Our independent directors under applicable U.S. regulations are also independent non-executive directors for the purpose of the Hong Kong Listing Rules. We have determined that Brent Callinicos qualifies as an “audit committee financial expert” under the applicable rules of the SEC and has the appropriate professional accounting or financial management experience.
- (3) Subsequent to the end of the fiscal year ended December 31, 2020, we determine that Mr. Victor Zhixiang Liang, our senior vice president, is an executive officer of our Company.

Save as disclosed below, none of our directors held any other directorships in any other company listed in Hong Kong or overseas during the three years immediately preceding the date of this document and there are no family relationships among any of the directors or executive officers of our Company. See “Major Shareholders” for disclosure of interests of the directors and executive officers. There is no material matter relating to our directors that needs to be brought to the attention of our shareholders and the information of our directors disclosed in this document comply with the requirements under Rule 13.51(2) of the Hong Kong Listing Rules in all material respects.

BIOGRAPHIES

Our Directors

Mr. Yanhong Li, also known as Mr. Robin Yanhong Li, is our co-founder, chief executive officer and chairman of our Board of Directors, overseeing our overall strategy and business operations. Mr. Li has been serving as the chairman since our inception in January 2000 and as our chief executive officer since February 2004. Mr. Li served as our president from February 2000 to December 2003. Prior to founding our company, Mr. Li worked as an engineer for Infoseek, a pioneer in the search industry, and as a senior consultant for IDD Information Services. Mr. Li currently serves on the board of New Oriental Education & Technology Group Inc., a private educational services provider in China (NYSE: EDU; SEHK: 9901), Trip.com, an online travel agency in China (NASDAQ: TCOM) and iQIYI (NASDAQ: IQ).

DIRECTORS AND SENIOR MANAGEMENT

Mr. Li received a bachelor’s degree in information science from Peking University and a master’s degree in computer science from the State University of New York at Buffalo.

Mr. Jian Ding, also known as Mr. James Ding, has served as our independent director since our initial public offering in August 2005. Mr. Ding brings a deep understanding of the internet and artificial intelligence industry, which is relevant to and continuously supported the growth and evolution of our principal business since his appointment. He also brings extensive experience as a high tech entrepreneur and CEO of a Nasdaq-listed company. Mr. Ding is a valuable member of the Company’s board of directors and continues to make important contribution to the Company. He is also a member of our Audit Committee and Corporate Governance and Nominating Committee, and the Chairman of our Compensation Committee. Mr. Ding is currently a managing director of GSR Ventures, which focuses on early stage companies in the artificial intelligence, big data, information technology related healthcare, virtual reality/augmented reality and new media sectors. Prior to that, Mr. Ding served as a co-chairman of the board of directors of AsiaInfo-Linkage Inc., a former NASDAQ-listed company, from July 2010 to January 2014. Mr. Ding also served as the chairman of the board of AsiaInfo from April 2003 to July 2010, and has served as a member of the board since AsiaInfo’s inception in 1993. Mr. Ding served as the chief executive officer and president of AsiaInfo from 1999 to 2003 and as senior vice president and chief technology officer of AsiaInfo from 1993 to 1999. Mr. Ding currently serves as director of the board of AsiaInfo (which is currently listed on the Hong Kong Stock Exchange as AsiaInfo Technologies Limited with stock code 1675). Mr. Ding received a master’s degree in information science from the University of California, Los Angeles and a bachelor’s degree in chemistry from Peking University in China.

Mr. Brent Callinicos has served as our independent director since October 2015, and as the chairman of our audit committee since April 2016. Mr. Callinicos served as the chief operating officer and the chief financial officer of Virgin Hyperloop One from January 2017 to January 2018. Prior to that, Mr. Callinicos served as the chief financial officer of Uber Technologies Inc. from September 2013 to March 2015, and then as an advisor for 18 additional months. Prior to joining Uber, he worked at Google from January 2007 to September 2013, where he last served as vice president, treasurer and chief accountant. He also led green energy investments and financial services at Google Inc. From 1992 to 2007, he served in a variety of increasingly senior roles at Microsoft Corporation, where he last served as corporate vice-president and divisional chief financial officer of the Platforms and Services Division, and oversaw Microsoft’s Worldwide Licensing and Pricing and Microsoft Financing. He currently serves on the board of directors of PVH Corp. (NYSE: PVH), and Rubicon, a private company. Mr. Callinicos is a certified public accountant. Mr. Callinicos received a bachelor’s degree from the University of North Carolina at Chapel Hill and an M.B.A. degree from the Kenan-Flagler School of Business at Chapel Hill.

Mr. Yuanqing Yang has served as our independent director since October 2015. Mr. Yang is currently the chairman and chief executive officer of Lenovo Group Limited (SEHK: 992), a director of Sureinvest Holdings Limited and Taikang Insurance Group. He also serves as a member of the International Advisory Council of the Brookings Institution. Mr. Yang joined Lenovo in 1989 and has led the company from the initial China-based PC maker to a diversified global technology leader. In 2011, FinanceAsia named Mr. Yang the Best CEO in China. In 2004 and 2012, Mr. Yang was named one of the “CCTV China Annual Economic Figures.” He was on Barron’s list of Best CEOs in 2013, 2014 and 2015. In 2014, Mr. Yang won an Edison Achievement Award for Innovation. Mr. Yang holds a master’s degree in computer science from the University of Science and Technology of China and a bachelor’s degree in computer science and engineering from Shanghai Jiao Tong University.

Mr. Ji-xun Foo, also known as Mr. Jixun Foo, has served as our independent director since July 2019. Mr. Foo has served as managing partner at GGV Capital since 2006, working with entrepreneurs in the

DIRECTORS AND SENIOR MANAGEMENT

travel, transportation, social media, e-commerce and enterprise services sectors in China. Prior to joining GGV Capital, Mr. Foo was a director at Draper Fisher Jurvetson ePlanet Ventures, where he led investments in Asia. Mr. Foo also previously led investments under the finance and investment division of the National Science and Technology Board of Singapore and served as an R&D project group leader at Hewlett Packard. Mr. Foo currently serves on the board of XPeng Inc. (NYSE: XPEV) and on the boards of a number of private companies, including Hello and Boss Zhipin. Mr. Foo received a First-Class Honors bachelor’s degree in engineering and a master’s degree in the management of technology from the National University of Singapore.

Our Senior Management

Mr. Herman Yu has served as our chief financial officer since September 2017, overseeing our finance and purchasing functions. Prior to joining Baidu, Mr. Yu served as the chief financial officer of Weibo Corporation, a social media company (NASDAQ: WB) from 2015 to 2017. Prior to Weibo, Mr. Yu worked at SINA Corporation, a portal (NASDAQ: SINA) from 2004 to 2015, beginning as a Vice President, Finance, and in 2006 became the chief financial officer. Mr. Yu currently serves on the board of directors of ZTO Express Inc., an express delivery company (NYSE: ZTO; SEHK:2057), and iQIYI (NASDAQ: IQ). Mr. Yu, a California Certified Public Accountant, received his bachelor’s degree in economics from the University of California, Santa Cruz, and master in accountancy (MAcc) from the University of Southern California.

Mr. Haifeng Wang has served as our chief technology officer since May 2019, overseeing our AI lab, systems & technology and cloud group. Dr. Wang joined Baidu in 2010 and was promoted to vice president in 2013. Dr. Wang oversaw our core search products from 2014 to 2017. He was promoted to senior vice president in 2018. Prior to Baidu, Dr. Wang served as the chief research scientist at Toshiba’s R&D Center. Dr. Wang is the president of National Engineering Laboratory for Deep Learning Technology and Applications. Dr. Wang was a fellow (and former president) of the Association for Computational Linguistics (ACL) and the founding chair of ACL’s Asia-Pacific chapter. Dr. Wang obtained his bachelor’s, master’s, and Ph.D. degrees in computer science from the Harbin Institute of Technology.

Mr. Dou Shen has served as executive vice president since May 2019. Previously, Dr. Shen served as senior vice president of Baidu’s mobile products, overseeing the development of Baidu App, Haokan short video app and Smart Mini Program. Dr. Shen joined Baidu in 2012 and has served in various management roles, including web search, display advertising and the financial services group. Prior to Baidu, Dr. Shen worked in the adCenter group at Microsoft and sold Buzzlabs, a social media monitoring and analysis platform company that he co-founded, to IAC-owned CityGrid Media. Dr. Shen currently serves on the board of directors of Trip.com, an online travel agency in China (NASDAQ: TCOM). Dr. Shen received a bachelor’s degree in engineering from North China Electric Power University, a master’s degree in engineering from Tsinghua University, and a Ph.D. in computer science from the Hong Kong University of Science and Technology.

Ms. Shanshan Cui currently serves as our senior vice president in charge of human resources and administrative functions since May 2019. Ms. Cui joined us in January 2000 overseeing the search technology group, and is a founding member of the company. Ms. Cui left Baidu in July 2010 to pursue personal interests and rejoined Baidu in December 2017, initially serving as Secretary General to our Organizational Culture Committee. In this capacity, Ms. Cui oversaw employee culture and organization effectiveness, implementing initiatives, such as OKR (objectives & key results) management, throughout the company. Ms. Cui received a bachelor’s degree in computer science from Beijing Institute of Technology and a master’s degree in computer science from the University of Chinese Academy of Sciences.

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Mr. Victor Zhixiang Liang joined Baidu in June 2005, and became senior vice president and general counsel in June 2011. Mr. Liang leads our legal and government relations functions. Mr. Liang also served as an executive assistant to the CEO from January 2013 to February 2018. Prior to joining Baidu, he worked at the legislative affairs office of the State Council of the People’s Republic of China and Davis Polk & Wardwell LLP, as a visiting attorney at their New York Office. Mr. Liang received an LL.M. degree from Yale Law School and law degrees from the University of New South Wales and Peking University.

COMPENSATION

Compensation of Directors and Executive Officers

For the three fiscal years 2018, 2019 and 2020, we paid an aggregate of RMB85 million, RMB22 million, and RMB16 million (US\$2 million), respectively, in cash compensation, and granted options to purchase an aggregate of 1,207,200 Class A ordinary shares and 1,798,160 restricted Class A ordinary shares, 2,197,280 Class A ordinary shares and 2,942,800 restricted Class A ordinary shares, and 277,680 Class A ordinary shares and 2,529,920 restricted Class A ordinary shares, respectively, to our executive officers that are in office as of the date of filing of our annual reports on Form 20-F (for the three fiscal years 2018, 2019 and 2020). During the same period, we also paid an aggregate of RMB452,000, RMB487,000, and RMB666,550 (US\$102,000), respectively, in cash compensation, and granted an aggregate of 1,067,280 restricted Class A ordinary shares, 12,080 restricted Class A ordinary shares, and 153,680 restricted Class A ordinary shares, respectively, to our non-executive directors as a group. The number of shares has been retrospectively adjusted for the Share Subdivision. Our PRC subsidiaries and consolidated affiliated entities are required by law to make contributions equal to certain percentages of each employee’s salary for his or her pension insurance, medical insurance, housing fund, unemployment insurance and other statutory benefits. Other than the above-mentioned statutory contributions mandated by applicable PRC law, we have not set aside or accrued any amount to provide pension, retirement or other similar benefits to our executive officers and directors. No executive officer is entitled to any severance benefits upon termination of his or her employment with our company except as required under applicable PRC law.

Employment Agreements and Indemnification Agreements

Each of our executive officers and key employees has entered into an employment agreement with us, containing confidentiality and non-competition provisions. In addition, the Company entered into separate indemnification agreements with each director and each executive officer of the Company that provide for indemnification of these directors and officers under similar circumstances and under additional circumstances.

Share Incentive Plans

Our board of directors and shareholders approved the issuance of up to 403,200,000 ordinary shares (taking into account the Share Subdivision) upon exercise of awards granted under our 2000 option plan. Our 2000 option plan terminated in January 2010 upon the expiration of its ten-year term.

At the annual general meeting held on December 16, 2008, our shareholders approved a 2008 share incentive plan (the “**2008 Share Incentive Plan**”), which has reserved an additional 274,302,160 Class A ordinary shares (taking into account the Share Subdivision) for awards to be granted pursuant to its terms. Our 2008 Share Incentive Plan terminated in December 2018 upon the expiration of its ten-year term.

On July 20, 2018, our board of directors approved a 2018 share incentive plan (the “**2018 Share Incentive Plan**”), which has reserved an additional 275,516,000 Class A ordinary shares (taking into account the Share Subdivision) for awards to be granted pursuant to its terms.

DIRECTORS AND SENIOR MANAGEMENT

2008 Share Incentive Plan

The following paragraphs summarize the key terms of our 2008 Share Incentive Plan.

Types of Awards. We may grant the following types of awards under our 2008 Share Incentive Plan:

- options (incentive share options, or “ISO”);
- restricted shares;
- restricted share units; and
- any other form of awards granted to a participant pursuant to the 2008 plan.

Plan Administration. The compensation committee of our board of directors administers our 2008 Share Incentive Plan, but may delegate to a committee of one or more members of our board of directors the authority to grant or amend awards to participants other than independent directors and executive officers. The compensation committee will determine the provisions and terms and conditions of each award grant, including, but not limited to, the exercise price, the grant price or purchase price, any restrictions or limitations on the award, any schedule for lapse of forfeiture restrictions or restrictions on the exercisability of an award, and accelerations or waivers thereof, any provisions related to non-competition and recapture of gain on an award, based in each case on such considerations as the committee in its sole discretion determines. The compensation committee has the sole power and discretion to cancel, forfeit or surrender an outstanding award (whether or not in exchange for another award or combination of awards).

Award Agreement. Awards granted under our 2008 Share Incentive Plan are evidenced by an award agreement that sets forth the terms, conditions and limitations for each award which may include the term of an award, the provisions applicable in the event the participant’s employment or service ends, and our authority to unilaterally or bilaterally amend, modify, suspend, cancel or rescind an award.

Eligibility. We may grant awards to employees, directors and consultants of our company or any of our related entities, which include our subsidiaries or any entities in which we hold a substantial ownership interest. However, we may grant ISOs only to our employees and employees of our majority-owned subsidiaries.

Acceleration of Awards upon Corporate Transactions. The outstanding awards will accelerate (i) upon occurrence of a change-of-control corporate transaction where any person acquires at least 50% of the total combined voting power of our outstanding securities or the incumbent board members no longer constitute at least 50% of our board, or (ii) upon occurrence of any other change-of-control corporate transaction in which the successor entity does not assume our outstanding awards under our 2008 Share Incentive Plan, provided that the plan participant remains an employee, consultant or member of our board of directors on the effective date of the corporate transaction. In such event, each outstanding award will become fully exercisable and all forfeiture restrictions on such award will lapse immediately prior to the specified effective date of the corporate transaction.

If the successor entity assumes our outstanding awards and later terminates the grantee’s employment or service without cause within 12 months of the corporate transaction, or if the grantee resigns voluntarily with good reason, the outstanding awards automatically will become fully vested and exercisable. The compensation committee may also, in its sole discretion, upon or in anticipation of a corporate transaction, accelerate awards, purchase the awards from the plan participants, replace the awards, or provide for the payment of the awards in cash.

DIRECTORS AND SENIOR MANAGEMENT

Exercise Price and Term of Awards. The exercise price per share subject to an option may be amended or adjusted in the absolute discretion of the compensation committee, the determination of which shall be final, binding and conclusive. To the extent not prohibited by applicable laws or exchange rules, a downward adjustment of the exercise prices of options mentioned in the preceding sentence shall be effective without the approval of our shareholders or the approval of the affected grantees. If we grant an ISO to an employee, who, at the time of that grant, owns shares representing more than 10% of the voting power of all classes of our share capital, the exercise price cannot be less than 110% of the fair market value of our ordinary shares on the date of that grant. The compensation committee will determine the time or times at which an option may be exercised in whole or in part, including exercise prior to vesting. The term may not exceed ten years from the date of the grant, except that five years is the maximum term of an ISO granted to an employee who holds more than 10% of the voting power of our share capital.

Restricted Shares and Restricted Share Units. The compensation committee is also authorized to make awards of restricted shares and restricted share units. Except as otherwise determined by the compensation committee at the time of the grant of an award or thereafter, upon termination of employment or service during the applicable restriction period, restricted shares that are at the time subject to restrictions shall be forfeited or repurchased in accordance with the respective award agreements.

Vesting Schedule. The compensation committee determines, and the award agreement specifies, the vesting schedule of options and other awards granted. The compensation committee determines the time or times at which an option may be exercised in whole or in part, including exercise prior to vesting, and also determines any conditions that must be satisfied before all or part of an option may be exercised. At the time of grant for restricted share units, the compensation committee specifies the date on which the restricted share units become fully vested and non-forfeitable, and may specify such conditions to vesting as it deems appropriate.

Amendment and Termination. With the approval of our board of directors, the compensation committee may at any time amend, suspend or terminate our 2008 Share Incentive Plan. Amendments to our 2008 Share Incentive Plan are subject to shareholder approval, to the extent required by law, or by stock exchange rules or regulations. Any amendment, suspension or termination of our 2008 Share Incentive Plan must not adversely affect in any material way awards already granted without written consent of the recipient of such awards. Unless terminated earlier, our 2008 Share Incentive Plan shall continue in effect for a term of ten years from the date of adoption.

2018 Share Incentive Plan

The following paragraphs summarize the key terms of our 2018 Share Incentive Plan.

Types of Awards. We may grant the following types of awards under our 2018 Share Incentive Plan:

- options;
- restricted shares;
- restricted share units; and
- any other form of awards granted to a participant pursuant to the 2018 plan.

Plan Administration. The compensation committee of our board of directors administers our 2018 Share Incentive Plan, but may delegate to a committee of one or more members of our board of

DIRECTORS AND SENIOR MANAGEMENT

directors the authority to grant or amend awards to participants other than independent directors and executive officers. The compensation committee will determine the provisions and terms and conditions of each award grant, including, but not limited to, the exercise price, the grant price or purchase price, any restrictions or limitations on the award, any schedule for lapse of forfeiture restrictions or restrictions on the exercisability of an award, and accelerations or waivers thereof, any provisions related to non-competition and recapture of gain on an award, based in each case on such considerations as the committee in its sole discretion determines. The compensation committee has the sole power and discretion to cancel, forfeit or surrender an outstanding award (whether or not in exchange for another award or combination of awards).

Award Agreement. Awards granted under our 2018 Share Incentive Plan are evidenced by an award agreement that sets forth the terms, conditions and limitations for each award which may include the term of an award, the provisions applicable in the event the participant's employment or service ends, and our authority to unilaterally or bilaterally amend, modify, suspend, cancel or rescind an award.

Eligibility. We may grant awards to employees, directors and consultants of our company or any of our related entities, which include our subsidiaries or any entities in which we hold a substantial ownership interest. However, we may grant ISOs only to our employees and employees of our majority-owned subsidiaries.

Acceleration of Awards upon Corporate Transactions. The outstanding awards will accelerate (i) upon occurrence of a change-of-control corporate transaction where any person acquires at least 50% of the total combined voting power of our outstanding securities or the incumbent board members no longer constitute at least 50% of our board, or (ii) upon occurrence of any other change-of-control corporate transaction in which the successor entity does not assume our outstanding awards under our 2018 Share Incentive Plan, provided that the plan participant remains an employee, consultant or member of our board of directors on the effective date of the corporate transaction. In such event, each outstanding award will become fully exercisable and all forfeiture restrictions on such award will lapse immediately prior to the specified effective date of the corporate transaction.

If the successor entity assumes our outstanding awards and later terminates the grantee's employment or service without cause within 12 months of the corporate transaction, or if the grantee resigns voluntarily with good reason, the outstanding awards automatically will become fully vested and exercisable. The compensation committee may also, in its sole discretion, upon or in anticipation of a corporate transaction, accelerate awards, purchase the awards from the plan participants, replace the awards, or provide for the payment of the awards in cash.

Exercise Price and Term of Awards. The exercise price per share subject to an option may be amended or adjusted in the absolute discretion of the compensation committee, the determination of which shall be final, binding and conclusive. To the extent not prohibited by applicable laws or exchange rules, a downward adjustment of the exercise prices of options mentioned in the preceding sentence shall be effective without the approval of our shareholders or the approval of the affected grantees. If we grant an ISO to an employee, who, at the time of that grant, owns shares representing more than 10% of the voting power of all classes of our share capital, the exercise price cannot be less than 110% of the fair market value of our ordinary shares on the date of that grant. The compensation committee will determine the time or times at which an option may be exercised in whole or in part, including exercise prior to vesting. The term may not exceed ten years from the date of the grant, except that five years is the maximum term of an ISO granted to an employee who holds more than 10% of the voting power of our share capital.

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Restricted Shares and Restricted Share Units. The compensation committee is also authorized to make awards of restricted shares and restricted share units. Except as otherwise determined by the compensation committee at the time of the grant of an award or thereafter, upon termination of employment or service during the applicable restriction period, restricted shares that are at the time subject to restrictions shall be forfeited or repurchased in accordance with the respective award agreements.

Vesting Schedule. The compensation committee determines, and the award agreement specifies, the vesting schedule of options and other awards granted. The compensation committee determines the time or times at which an option may be exercised in whole or in part, including exercise prior to vesting, and also determines any conditions that must be satisfied before all or part of an option may be exercised. At the time of grant for restricted share units, the compensation committee specifies the date on which the restricted share units become fully vested and non-forfeitable, and may specify such conditions to vesting as it deems appropriate.

Amendment and Termination. With the approval of our board of directors, the compensation committee may at any time amend, suspend or terminate our 2018 Share Incentive Plan. To the extent the Company decides to follow home country practice, amendments to our 2018 Share Incentive Plan are subject to shareholder approval, to the extent required by law, or by stock exchange rules or regulations. Any amendment, suspension or termination of our 2018 Share Incentive Plan must not adversely affect in any material way awards already granted without written consent of the recipient of such awards. Unless terminated earlier, our 2018 Share Incentive Plan shall continue in effect for a term of ten years from the date of adoption.

Grants under the 2008 and 2018 Share Incentive Plans

As of December 31, 2020, options to purchase an aggregate of 50,634,400 Class A ordinary shares and an aggregate of 246,747,920 restricted Class A ordinary shares had been granted under the 2008 and 2018 share incentive plans (taking into account the Share Subdivision).

The following table summarizes, as of December 31, 2020, the outstanding options and restricted Class A ordinary shares that we had granted to our current directors and executive officers and to other individuals as a group. Each ADS represents eight Class A ordinary shares. The number of shares has been retrospectively adjusted for the Share Subdivision.

| <u>Name</u> | <u>Ordinary Shares Underlying Outstanding Options</u> | <u>Exercise Price (US\$/Share)</u> | <u>Grant Date</u> | <u>Expiry Date</u> |
|----------------------------|---|--|-------------------|--------------------|
| Robin Yanhong Li | 342,320 | 17.729 | February 16, 2012 | February 16, 2022 |
| | 847,840 | 13.538 | January 31, 2013 | January 31, 2023 |
| | 193,200 | 21.566 | February 24, 2014 | February 24, 2024 |
| | 958,160 | 26.834 | February 11, 2015 | February 11, 2025 |
| | 3,512,320 | 25.863 | April 16, 2015 | April 16, 2025 |
| | 211,040 | 19.778 | February 25, 2016 | February 25, 2026 |
| | 724,800 | 21.888 | October 27, 2016 | October 27, 2026 |
| | 469,120 | 23.251 | February 22, 2017 | February 22, 2027 |
| | 110,400 ⁽¹⁾ | — | February 22, 2017 | N/A |
| | 397,280 ⁽¹⁾ | — | February 9, 2018 | N/A |
| | 786,240 ⁽¹⁾ | — | February 18, 2019 | N/A |
| | 212,560 ⁽¹⁾ | — | May 23, 2019 | N/A |
| | 1,317,760 ⁽¹⁾ | — | February 5, 2020 | N/A |

DIRECTORS AND SENIOR MANAGEMENT

| Name | Ordinary Shares Underlying Outstanding Options | Exercise Price (US\$/Share) | Grant Date | Expiry Date |
|----------------------------------|--|--------------------------------|-------------------|-------------------|
| Herman Yu | * | 0.001 | February 9, 2018 | February 9, 2028 |
| | * | 0.001 | February 18, 2019 | February 18, 2029 |
| | * | 0.001 | May 23, 2019 | May 23, 2029 |
| | * | 0.001 | February 5, 2020 | February 5, 2030 |
| Dou Shen | *(1) | — | February 22, 2017 | N/A |
| | *(1) | — | July 26, 2017 | N/A |
| | *(1) | — | February 9, 2018 | N/A |
| | *(1) | — | February 18, 2019 | N/A |
| | *(1) | — | May 23, 2019 | N/A |
| | * | 12.486 | August 8, 2019 | August 8, 2029 |
| | *(1) | — | August 8, 2019 | N/A |
| | *(1) | — | October 28, 2019 | N/A |
| | *(1) | — | February 5, 2020 | N/A |
| | Haifeng Wang | *(1) | — | February 22, 2017 |
| * | | 23.483 | April 27, 2017 | April 27, 2027 |
| *(1) | | — | April 27, 2017 | N/A |
| *(1) | | — | February 9, 2018 | N/A |
| *(1) | | — | July 21, 2018 | N/A |
| *(1) | | — | February 18, 2019 | N/A |
| *(1) | | — | May 23, 2019 | N/A |
| * | | 12.486 | August 8, 2019 | August 8, 2029 |
| *(1) | | — | February 5, 2020 | N/A |
| Shanshan Cui | | *(1) | — | February 9, 2018 |
| | *(1) | — | February 18, 2019 | N/A |
| | *(1) | — | May 23, 2019 | N/A |
| | *(1) | — | February 5, 2020 | N/A |
| Victor Zhixiang Liang | * | 26.834 | February 11, 2015 | February 11, 2025 |
| | * | 23.251 | February 22, 2017 | February 22, 2027 |
| | *(1) | — | February 22, 2017 | N/A |
| | *(1) | — | February 9, 2018 | N/A |
| | *(1) | — | February 18, 2019 | N/A |
| | *(1) | — | May 23, 2019 | N/A |
| | *(1) | — | February 5, 2020 | N/A |
| Jixun Foo | *(1) | — | February 5, 2020 | N/A |
| James Ding | *(1) | — | February 5, 2020 | N/A |
| Brent Callinicos | *(1) | — | February 5, 2020 | N/A |
| Yuanqing Yang | *(1) | — | February 5, 2020 | N/A |
| Other individuals as a group . . | 137,893,360 | — | — | — |

Note:

* The options and restricted shares in aggregate held by each of these directors and officers represent less than 1% of our total outstanding shares.

The options held by these directors and officers represent less than 1% of our total outstanding shares.

(1) Restricted shares

DIRECTORS AND SENIOR MANAGEMENT

BOARD PRACTICES

Board of Directors

Our board of directors has five directors. A director is not required to hold any shares in the company by way of qualification. A director may vote with respect to any contract, proposed contract or arrangement in which he is materially interested. A director may exercise all the powers of the company to borrow money, mortgage its undertakings, property and uncalled capital, and issue debentures or other securities whenever money is borrowed or as security for any obligation of the company or of any third party. The remuneration to be paid to the directors is determined by the board of directors. There is no age limit requirement for directors.

Code of Ethics

In July 2005, our board of directors adopted a code of business conduct and ethics that applies to our directors, officers, employees and advisors. We have posted a copy of our code of business conduct and ethics on our website.

Committees of the Board of Directors

We have three committees under the board of directors: an audit committee, a compensation committee and a corporate governance and nominating committee. We have adopted a charter for each of the three committees.

Audit Committee

Our audit committee consists of Brent Callinicos, James Ding and Yuanqing Yang, all of whom satisfy the “independence” requirements of Rule 5605(a)(2) of the Nasdaq Stock Market Rules and Rule 10A-3 under the Exchange Act. Our board of directors has determined that Mr. Callinicos is an audit committee financial expert as defined in the instructions to Item 16A of the Form 20-F. The audit committee oversees our accounting and financial reporting processes and the audits of the financial statements of our company. The audit committee is responsible for, among other things:

- appointing, retaining and overseeing the work of the independent auditors, including resolving disagreements between the management and the independent auditors relating to financial reporting;
- pre-approving all auditing and non-auditing services permitted to be performed by the independent auditors;
- reviewing annually the independence and quality control procedures of the independent auditors;
- reviewing and approving all proposed related party transactions;
- discussing the annual audited financial statements with the management;
- meeting separately with the independent auditors to discuss critical accounting policies, management letters, recommendations on internal controls, the auditor’s engagement letter and independence letter and other material written communications between the independent auditors and the management;
- attending to such other matters that are specifically delegated to our audit committee by our board of directors from time to time; and
- reviewing investor feedback sent to the investor relations function of the Company and attending to management reports on investor relations.

Compensation Committee

Our compensation committee consists of James Ding, Yuanqing Yang and Jixun Foo, all of whom satisfy the “independence” requirements of Rule 5605(a)(2) of the Nasdaq Stock Market Rules. The

DIRECTORS AND SENIOR MANAGEMENT

compensation committee assists the board in reviewing and approving our compensation structure, including all forms of compensation relating to our directors and executive officers. Our chief executive officer may not be present at any committee meeting while his compensation is deliberated. The compensation committee is responsible for, among other things:

- reviewing and approving, or recommending to the board for its approval, the compensation for our chief executive officer and other executive officers;
- reviewing and recommending to the board for determination with respect to the compensation of our non-employee directors;
- reviewing periodically and approving any incentive compensation or equity plans, programs or similar arrangements; and
- selecting compensation consultant, legal counsel or other adviser only after taking into consideration all factors relevant to that person’s independence from management.

Corporate Governance and Nominating Committee

Our corporate governance and nominating committee consists of James Ding and Yuanqing Yang, both of whom satisfy the “independence” requirements of Rule 5605(a) (2) of the Nasdaq Stock Market Rules. The corporate governance and nominating committee assists the board of directors in selecting individuals qualified to become our directors and in determining the composition of the board and its committees. The corporate governance and nominating committee is responsible for, among other things:

- recommending to the board nominees for election or re-election to the board or for appointments to fill any vacancies;
- reviewing annually the performance of each incumbent director in determining whether to recommend such director for an additional term;
- overseeing the board in the board’s annual review of its own performance and the performance of the management; and
- considering, preparing and recommending to the board such policies and procedures with respect to corporate governance matters as may be required or required to be disclosed under the applicable laws or otherwise considered to be material.

Terms of Directors and Executive Officers

All directors hold office until their successors have been duly elected and qualified. None of our directors is subject to a fixed term of office. In addition, the service agreements between us and the directors do not provide benefits upon termination of their services. Director nomination is subject to the approval of our corporate governance and nominating committee. Our shareholders may remove any director by ordinary resolution and may in like manner appoint another person in his stead. A valid ordinary resolution requires a majority of the votes cast at a shareholder meeting that is duly constituted and meets the quorum requirement. Officers are elected by and serve at the discretion of the board of directors.

MAJOR SHAREHOLDERS

Except as otherwise noted, the following table sets forth information with respect to the beneficial ownership of our ordinary shares as of the Latest Practicable Date by:

- each of our directors and executive officers; and
- each person known to us to own beneficially more than 5% of our total outstanding shares.

The calculations in the table below are based on 2,685,023,744 ordinary shares, consisting of 2,125,123,424 Class A ordinary shares and 559,900,320 Class B ordinary shares issued and outstanding as of the Latest Practicable Date.

Beneficial ownership is determined in accordance with the rules and regulations of the SEC. In computing the number of shares beneficially owned by a person and the percentage ownership of that person, we have included shares that the person has the right to acquire within 60 days, including through the exercise of any option, warrant or other right or the conversion of any other security. These shares, however, are not included in the computation of the percentage ownership of any other person.

| | Ordinary Shares Beneficially Owned | | | Percentage of total ordinary shares | Percentage of aggregate voting power |
|---|------------------------------------|-------------------------|-----------------------|-------------------------------------|--------------------------------------|
| | Class A ordinary shares | Class B ordinary shares | Total ordinary shares | | |
| Directors and Executive Officers:** | | | | | |
| Robin Yanhong Li ⁽¹⁾ | 18,291,280 | 439,200,000 | 457,491,280 | 17.0% | 57.0% |
| Herman Yu | * | — | * | * | * |
| Dou Shen | * | — | * | * | * |
| Haifeng Wang | * | — | * | * | * |
| Shanshan Cui | * | — | * | * | * |
| Victor Zhixiang Liang | * | — | * | * | * |
| James Ding | * | — | * | * | * |
| Brent Callinicos | * | — | * | * | * |
| Yuanqing Yang | * | — | * | * | * |
| Jixun Foo | * | — | * | * | * |
| All Directors and Executive Officers as a Group | 20,209,280 | 439,200,000 | 459,409,280 | 17.1% | 57.1% |
| Principal Shareholders: | | | | | |
| Handsome Reward Limited ⁽²⁾ | 12,689,200 | 439,200,000 | 451,889,200 | 16.8% | 57.0% |

Notes:

† For each person and group included in this column, percentage of voting power is calculated by dividing the voting power beneficially owned by such person or group by the voting power of all of our Class A ordinary shares and Class B ordinary shares as a single class. Holders of Class A ordinary shares are entitled to one vote per share, while holders of Class B ordinary shares are entitled to ten votes per share. Holders of our Class B ordinary shares may choose to convert their Class B ordinary shares into the same number of Class A ordinary shares at any time.

* Less than 1% of our total outstanding ordinary shares.

(1) Includes (i) 3,013,200 Class A Ordinary Shares directly held by Mr. Robin Yanhong Li on record, (ii) 2,232,000 Class A ordinary shares in the form of ADSs held by Mr. Robin Yanhong Li in the brokerage account of the administrator of our employee stock option program, (iii) 342,320 Class A Ordinary Shares issuable to Mr. Robin Yanhong Li upon exercise of options within 60 days after the Latest Practicable Date, (iv) 14,560 Class A Ordinary Shares issuable to Mr. Robin Yanhong Li upon vesting of restricted shares within 60 days after the Latest Practicable Date, (v) 439,200,000 Class B Ordinary Shares held on record by Handsome Reward Limited, a British Virgin Islands company wholly owned by Mr. Robin Yanhong Li, (vi) 5,772,720 Class A ordinary shares in the form of ADSs held by Handsome Reward Limited in the brokerage account of the administrator of our employee stock option program, (vii) 6,916,480 Class A Ordinary Shares issuable to Handsome Reward Limited upon exercise of options within 60 days after the date of the Latest Practicable Date, (viii) excludes 116,600,000 Class B Ordinary Shares owned by Ms. Melissa Ma, Mr. Robin Yanhong Li’s wife, who also had owned an aggregate of 50,000 ADSs, an additional 25,645 ADSs in the brokerage account of the administrator of our employee stock option program and the right to acquire 575 ADSs upon the vesting of restricted share units granted under our share incentive plan within 60 days after the Latest Practicable Date of which Mr. Robin Yanhong Li disclaims beneficial ownership. The voting power of the shares beneficially owned by Mr. Robin Yanhong Li represented 57.0% of the total outstanding voting power of our company as of the Latest Practicable Date.

MAJOR SHAREHOLDERS

- (2) Includes (i) 439,200,000 Class B ordinary shares held by Handsome Reward Limited, a British Virgin Islands company wholly owned and controlled by Mr. Robin Yanhong Li, (ii) 5,772,720 Class A ordinary shares in the form of ADSs held by Handsome Reward Limited in the brokerage account of the administrator of our employee stock option program, (iii) 6,916,480 Class A Ordinary Shares issuable to Handsome Reward Limited upon exercise of options within 60 days after the Latest Practicable Date.

As of the Latest Practicable Date, to our knowledge, approximately 78.4% of our total outstanding ordinary shares were held by three record shareholders in the United States, including approximately 78.3% held by The Bank of New York Mellon, the depository of our ADS program. The number of beneficial owners of ADSs in the United States is likely to be much larger than the number of record holders of our ordinary shares in the United States.

RELATED PARTY TRANSACTIONS

We are seeking a listing on the Hong Kong Stock Exchange pursuant to Chapter 19C of the Hong Kong Listing Rules. Pursuant to Rule 19C.11 of the Hong Kong Listing Rules, Chapter 14A of the Hong Kong Listing Rules, governing connected transactions, does not apply to us. The following discussion of related party transactions has been prepared pursuant to the requirements of Form 20-F of the SEC, and is included in this document for disclosure purposes only.

CONTRACTUAL ARRANGEMENTS

Please refer to “History and Corporate Structure—Contractual Arrangements” for a summary of the contractual arrangements and the variable interest entity structure adopted by the Company.

Our subsidiaries, consolidated affiliated entities, and the subsidiaries of the consolidated affiliated entities have engaged, during the ordinary course of business, in a number of customary transactions with each other. All of these inter-company balances have been eliminated in consolidation.

AMOUNTS DUE FROM RELATED PARTIES

As of December 31, 2018, 2019 and 2020, we had RMB5.1 billion, RMB5.2 billion and RMB4.2 billion (US\$638 million), respectively, due from related parties. The decrease of the balance from December 31, 2019 to December 31, 2020 was primarily due to the repayment of loans from certain related parties including Du Xiaoman and the acquisition of Investee A.

AMOUNTS DUE TO RELATED PARTIES

As of December 31, 2018, 2019 and 2020, we had RMB6.1 billion, RMB6.1 billion and RMB4.9 billion (US\$746 million), respectively, due to related parties. The decrease of the balance from December 31, 2019 to December 31, 2020 was primarily due to payment of unsettled payments to Du Xiaoman and the acquisition of Investee A.

TRANSACTIONS WITH RELATED PARTIES

Trip.com

In 2018, 2019 and 2020, related party transactions with Trip.com mainly comprised the online marketing services that we provided to Trip.com, which were in the total amount of RMB774 million, RMB627 million and RMB204 million (US\$31 million), respectively.

Du Xiaoman

In August 2018, we completed the divestiture of Du Xiaoman, following which we recognized our non-controlling equity interest in Du Xiaoman as an equity method investment and Du Xiaoman became a related party.

For the years ended December 31, 2018, 2019 and 2020, related party transactions with Du Xiaoman comprised the online marketing services, cloud service and other services that we provided to Du Xiaoman, which were in the total amount of RMB256 million, RMB731 million and RMB678 million (US\$104 million), respectively.

In 2018, we provided multiple short-term loans to Du Xiaoman in the amount of RMB12.0 billion with interest rates ranging from 5.00% to 7.00%. As of December 31, 2018, all short-term loans extended to Du Xiaoman had been repaid in full.

RELATED PARTY TRANSACTIONS

In 2018, we provided three term loans to Du Xiaoman in the amount of RMB3.8 billion with terms ranging from two to five years, which are intended for working capital purposes. These loans bear interest rates ranging from 4.28% to 5.00% in 2018, and 0% to 5.00% since 2019. Du Xiaoman repaid one term loan in the principal amount of RMB500 million in October 2020. The principal amount outstanding as of February 28, 2021 was RMB3.3 billion (US\$513 million).

In 2018, Du Xiaoman provided us with two term loans in the amount of RMB3.4 billion with terms of three and five years, which are intended for general corporate purposes. These loans bear interest rates ranging from 3.78% to 4.28% in 2018, and were revised to 0% since 2019, based on the re-entered agreements. The principal amount outstanding as of February 28, 2021 was RMB3.2 billion (US\$487 million).

The background of the above loan arrangements with Du Xiaoman is that, our cash is mainly onshore due to our extensive business operation within the PRC, and had offshore cash needs; Du Xiaoman had considerable cash resources offshore due to its equity financing, and had onshore spending needs. To meet both company’s needs, we and Du Xiaoman entered into several loan agreements (including onshore loan agreements and offshore loan agreements) in 2018, under which certain of our onshore subsidiaries lent RMB loans to one of Du Xiaoman’s onshore affiliates inside the PRC, and Du Xiaoman lent USD loans to one of our subsidiaries outside the PRC, respectively. Our PRC Legal Adviser is of the opinion that these loan agreements were executed for actual business purposes of us and Du Xiaoman, and these agreements did not expressly provide that the loan under one agreement constitutes collateral to guarantee repayment of the loan under the other agreement; if such arrangements are deemed as constituting the cross-border guarantee requiring registration by the foreign exchange regulatory authority, we could face order to rectify, warning and a fine no more than RMB300,000 pursuant to PRC laws and regulations relating to foreign exchanges. Please see “Risk Factors—Risks Related to Doing Business in China—PRC regulation of loans to and direct investment in PRC entities by offshore holding companies and governmental control of currency conversion may delay or prevent us from making loans to our PRC subsidiaries, consolidated affiliated entities and certain related parties, or making additional capital contributions to our PRC subsidiaries, which could adversely affect our ability to fund and expand our business” for more details. However, in practice, such arrangements do not meet the requirements for relevant registration and thus there is obstacle to completing the registration with relevant authority; instead, the PRC foreign exchange regulatory authority is more likely to require the relevant parties to revise the relevant loan agreement and remove the provisions it deems as constituting security interests or require the parties to repay the loan separately inside or outside the PRC. As of the date of this document, we have not received any enquiry, notice or penalty from the PRC foreign exchange regulatory authority regarding this matter. We and Du Xiaoman will not offset the loans inside and outside the PRC directly. If our arrangements with Du Xiaoman are raised by the PRC foreign exchange regulatory authority and determined against us, the fine is not a material penalty pursuant to relevant PRC laws and regulations relating to foreign exchanges and will not have a material adverse impact on our financial and business operations.

Other related parties

In 2018, 2019 and 2020, related party transactions with an investee over which we have significant influence, mainly related to hardware products purchased from and sold to the investee, which amounted to RMB1.9 billion and RMB249 million, respectively, in 2019, and RMB102 million and RMB77 million, respectively, in 2018. The Company acquired such investee in July 2020, and accordingly, all corresponding outstanding balances have been eliminated in the consolidated balance sheets as at December 31, 2020. The transaction amounts with the investee in 2020 were insignificant.

RELATED PARTY TRANSACTIONS

In 2018, 2019 and 2020, with the approval from our board of directors, we reimbursed Mr. Robin Yanhong Li the fees and expenses incurred in connection with his use of an aircraft beneficially owned by his family member for our business purposes. The hourly rate for use of the aircraft was determined based on an analysis of market rates for the charter of comparable aircrafts. The service charges for the use of the aircraft for 2018, 2019 and 2020 were insignificant.

REGULATIONS

This section sets forth a summary of the most significant rules and regulations that affect our business operations in the PRC.

Regulations on Foreign Investment

On January 1, 2020, the Foreign Investment Law and the Regulations for Implementation of the Foreign Investment Law (《中華人民共和國外商投資法實施條例》) (the “**Implementation Regulations**”) came into effect and became the principal laws and regulations governing foreign investment in the PRC, replacing the trio of prior laws regulating foreign investment in the PRC, namely, the Sino-foreign Equity Joint Venture Enterprise Law (《中華人民共和國中外合資經營企業法》), the Sino-foreign Cooperative Joint Venture Enterprise Law (《中華人民共和國中外合作經營企業法》) and the Wholly Foreign-invested Enterprise Law (《中華人民共和國外資企業法》), together with their implementation rules and ancillary regulations.

According to the Foreign Investment Law, “foreign investment” refers to the investment activities conducted directly or indirectly by foreign individuals, enterprises or other entities in the PRC, including the following circumstances: (i) the establishment of foreign-invested enterprises in the PRC by foreign investors solely or jointly with other investors, (ii) a foreign investors’ acquisition of shares, equity interests, property portions or other similar rights and interests of enterprises in the PRC, (iii) investment in new projects in the PRC by foreign investors solely or jointly with other investors, and (iv) investments made by foreign investors through means stipulated in laws or administrative regulations or other methods prescribed by the State Council.

Pursuant to the Foreign Investment Law, the PRC has adopted a reformed system with respect to foreign investment administration, under which the Chinese government applies national treatment to foreign investors in terms of investment entry and the foreign investor needs to comply with the requirements as provided in the negative list for foreign investment. The negative list will be issued by, amended or released upon approval by the State Council, from time to time. The negative list will consist of a list of industries in which foreign investments are prohibited and a list of industries in which foreign investments are restricted. Foreign investors will be prohibited from making investments in prohibited industries, while foreign investments must satisfy certain conditions stipulated in the negative list for investments in restricted industries. Foreign investments and domestic investments in industries outside the scope of the prohibited industries and restricted industries stipulated in the negative list will be treated equally. Any foreign-invested enterprise established prior to the effectiveness of the Foreign Investment Law may maintain its original corporate forms for a period of five years after January 1, 2020.

The Implementation Regulations restates certain principles of the Foreign Investment Law and further provides that, among others, (1) if a foreign-invested enterprise established prior to the effective date of the Foreign Investment Law fails to adjust its legal form or governance structure to comply with the provisions of the Companies Law of the PRC (《中華人民共和國公司法》) or the Partnership Enterprises Law of the PRC (《中華人民共和國合夥企業法》) as applicable and complete amendment registration before January 1, 2025, the enterprise registration authority will not process other registration matters of the foreign-invested enterprise and may publicize such non-compliance thereafter; (2) the provisions regarding equity interest transfer and distribution of profits and remaining assets as stipulated in the contracts among the joint venture parties of a foreign-invested enterprise established before the effective date of the Foreign Investment Law may, after adjustment of the legal form and governing structure of such foreign-invested enterprise, remain binding upon the parties.

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On December 31, 2019, the Ministry of Commerce of the PRC (the “**MOFCOM**”) and the State Administration of Market Regulation (the “**SAMR**”) jointly promulgated the Measures for Information Reporting on Foreign Investment (《外商投資信息報告辦法》), which became effective on January 1, 2020. Pursuant to the measures, where a foreign investor directly or indirectly carries out investment activities in China, the foreign investor or the foreign-invested enterprise must submit the investment information to the competent commerce department for further handling.

In December 2020, the NDRC and the MOFCOM promulgated the Measures for the Security Review of Foreign Investment (《外商投資安全審查辦法》), which came into effect on January 18, 2021. The NDRC and the MOFCOM will establish a working mechanism office in charge of the security review of foreign investment. Such measures define foreign investment as direct or indirect investment by foreign investors in the PRC, which includes (i) investment in new onshore projects or establishment of wholly foreign owned onshore companies or joint ventures with foreign investors; (ii) acquiring equity or asset of onshore companies by merger and acquisition; and (iii) onshore investment by and through any other means. Investment in certain key areas with bearing on national security, such as important cultural products and services, important information technology and internet services and products, key technologies and other important areas with bearing on national security which results in the acquisition of de facto control of investee companies, shall be filed with a specifically established office before such investment is carried out. What may constitute “onshore investment by and through any other means” or “de facto control” could be broadly interpreted under such measures. It is likely that control through contractual arrangement be regarded as de facto control based on provisions applied to security review of foreign investment in the free trade zone. Failure to make such filing may subject such foreign investor to rectification within prescribed period, and will be recorded as negative credit information of such foreign investor in the relevant national credit information system, which would then subject such investors to joint punishment as provided by relevant rules. If such investor fails to or refuses to undertake such rectification, it would be ordered to dispose of the equity or asset and to take any other necessary measures so as to return to the status quo and to erase the impact to national security.

Regulations on Value-Added Telecommunications Services and Internet Content Services

Regulations on Value-added telecommunications services and Internet content services

The Telecommunications Regulations of the PRC (《中華人民共和國電信條例》) (the “**Telecommunications Regulations**”) promulgated by the PRC State Council in September 2000, which were most recently amended in February 2016, categorize all telecommunication businesses in the PRC as either basic or value-added. Pursuant to the Telecommunications Regulations, commercial operators of value-added telecommunications services must first obtain a Value-Added Telecommunication Business Operating License from the Ministry of Industry and Information Technology of the PRC (the “**MIIT**”) or its provincial level counterparts. The Administrative Measures for Telecommunication Business Operating License (《電信業務經營許可管理辦法》), promulgated by the MIIT with latest amendments becoming effective in September 2017, set forth the types of licenses required for value-added telecommunications services and the qualifications and procedures for obtaining such licenses. For example, a value-added telecommunications service operator providing commercial value-added services in multiple provinces is required to obtain an inter-regional license, whereas a value-added telecommunications service operator providing the same services in one province is required to obtain a local license.

Internet content services, or ICP services, are classified as one of the value-added telecommunication businesses. The Administrative Measures on Internet Information Services (《互聯網信息服務管理辦

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法》), promulgated by the PRC State Council in September 2000 and amended in January 2011, require companies engaged in the provision of commercial internet content services to obtain a Value-added Telecommunication Business Operation Permit for ICP services, or an ICP license from the relevant government authorities before providing any commercial internet content services within the PRC. “Commercial internet content services” generally refer to provision of information service through public telecommunication network or internet for a fee. The Catalog of Classification of Telecommunications Services (《電信業務分類目錄》) (the “**Catalog of Telecommunication Businesses**”) promulgated by the MIIT in December 2015 and amended in June 2019 further divides ICP services into information publication platform and delivery services, information search and inquiry services, information communities platform services, instant message services, and information security and management services.

In June 2020, MIIT promulgated the Notice regarding Strengthening the Management of Call Center Business (《關於加強呼叫中心業務管理的通知》), which has strengthening the management on the admittance, codes, accessing, operation activities and certain other items.

Regulations on Content

National security considerations are an important factor in the regulation of internet content in the PRC. The National People’s Congress, the PRC’s national legislature, has enacted laws with respect to maintaining the security of internet operation and internet content. Under these laws and applicable regulations, violators may be subject to penalties, including criminal sanctions, for internet content that:

- opposes the fundamental principles stated in the PRC constitution;
- compromises national security, divulges state secrets, subverts state power or damages national unity;
- harms the dignity or interests of the state;
- incites ethnic hatred or racial discrimination or damages inter-ethnic unity;
- undermines the PRC’s religious policy or propagates heretical teachings or feudal superstitions;
- disseminates rumors, disturbs social order or disrupts social stability;
- disseminates obscenity or pornography, encourages gambling, violence, murder or fear or incites the commission of a crime;
- insults or slanders a third party or infringes upon the lawful rights and interests of a third party; or
- is otherwise prohibited by law or administrative regulations.

ICP operators are required to monitor their websites, including electronic bulletin boards. They may not post or disseminate any content that falls within the prohibited categories and must remove any such content from their websites. The PRC government may shut down the websites of ICP license holders that violate any of the above-mentioned content restrictions and revoke their ICP licenses. For instance, in 2017, the CAC, issued a series of regulatory documents providing that an ICP operator is obligated to monitor contents displayed and disseminated by users on its platform. These regulations apply to online services, including (i) online forum and community service, which allows users to publish information and interact with other users on an online forum, post bar or other form of online communities, (ii) online follow-up comment service, which allows users to post threads, reply to original content, leave messages and engage in live commenting with texts, symbols, expressions, pictures, audio/video on a website, mobile app or other forms of interactive platform; (iii) online group

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chat information service, which allows users to communicate and exchange information in a cyberspace created by the users on an online platform; (iv) online official account information service, which allows users to post texts, pictures, audio/video and other information in the form of an official account registered by the user on a website, mobile app or other network platform. Pursuant to these regulations, a service provider is required to, among others, (x) register and verify the identity information of each user, and (y) in the case of publication or dissemination of prohibited contents on the platform, take prompt rectification measures, including removing and terminating transmission of the illegal content, restricting the user right of the offender, banning the user account and shutting down the relevant forum or channel, and report to the regulatory authority.

In addition, in November 2018, the CAC issued a notice to require ICP operators to conduct security assessments on their Internet information services if their services include forums, blogs, microblogs, chat rooms, communication groups, public accounts, short videos, online live-streaming, information sharing, mini programs or such other functions that provide channels for the public to express opinions or have the capability of mobilizing the public to engage in specific activities. ICP operators must conduct self-assessment on, among others, the legality of new technology involved in the services and the effectiveness of security risk prevention measures, and file the assessment report to local competent Internet information office and public security authority. At the end of 2019, the CAC issued the Provisions on the Management of Network Information Content Ecology (《網絡信息內容生態治理規定》), or the CAC Order No.5, which became effective on March 1, 2020, to further strengthen the regulation and management of network information content. Pursuant to the CAC Order No.5, each network information content service platform is required, among others, (i) not to disseminate any information prohibited by laws and regulations, such as information jeopardizing national security; (ii) to strengthen the examination of advertisements published on such network information content service platform; (iii) to promulgate management rules and platform convention and improve user agreement, such that such network information content service platform could clarify users’ rights and obligations and perform management responsibilities required by laws, regulations, rules and convention; (iv) to establish convenient means for complaints and reports; and (v) to prepare annual work report regarding its management of network information content ecology. In addition, a network information content service platform must not, among others, (i) utilize new technologies such as deep-learning and virtual reality to engage in activities prohibited by laws and regulations; (ii) engage in online traffic fraud, malicious traffic rerouting and other activities related to fraudulent account, illegal transaction account or maneuver of users’ account; or (iii) infringe a third party’s legitimate rights or seek illegal interests by way of interfering with information display.

Restrictions on Foreign Ownership in Value-Added Telecommunications Services

Pursuant to the Provisions on Administration of Foreign-Invested Telecommunications Enterprises (《外商投資電信企業管理規定》), promulgated by the PRC State Council with the latest amendments becoming effective in February 2016, the ultimate foreign equity ownership in a value-added telecommunications service provider must not exceed 50%. However, the MIIT released an announcement in June 2015 to remove the restriction on foreign equity for “online data processing and transaction processing businesses (operational E-commerce)” as provided in the Catalog of Telecommunication Businesses promulgated by the MIIT. The Special Administrative Measures (Negative List) for Foreign Investment Access (《外商投資准入特別管理措施(負面清單)(2020年版)》) issued in 2020 allow a foreign investor to own more than 50% of the total equity interest in an e-commerce business, a domestic multi-party communication business, an information storage and re-transmission business and a call center business. In order to acquire any equity interest in a value-added telecommunication business in the PRC, a foreign investor must satisfy a number of stringent performance and operational experience requirements, including demonstrating a good track record

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and experience in operating a value-added telecommunication business overseas. Foreign investors that meet these requirements must obtain approvals from the MIIT and the MOFCOM (or the MOFCOM’s authorized local counterparts), which retain considerable discretion in granting approvals. According to publicly available information, the PRC government has issued telecommunication business operating licenses to only a limited number of foreign-invested companies.

A Notice on Intensifying the Administration of Foreign Investment in Value-Added Telecommunications Services (《信息產業部關於加強外商投資經營增值電信業務管理的通知》), issued by the MIIT in July 2006, prohibits domestic telecommunication service providers from leasing, transferring or selling Telecommunication Business Operating Licenses to any foreign investor in any form, or providing any resources, sites or facilities to any foreign investor for their illegal operation of a telecommunication business in the PRC. Pursuant to this notice, either the holder of a Value-Added Telecommunication Business Operating License or its shareholders must directly own the domain names and trademarks used by such license holder in its provision of value-added telecommunications services. The notice further requires each license holder to have the necessary facilities, including servers, for its approved business operations and to maintain the facilities in the regions covered by its license. If a license holder fails to comply with the requirements in the notice or cure any non-compliance, the MIIT or its local counterparts have the discretion to take measures against the license holder, including revoking its Value-added Telecommunication Business Operating License. Based on the Notice regarding the Strengthening of Ongoing and Post Administration of Foreign Investment Telecommunication Enterprises (《關於加強外商投資電信企業事中事後監管的通知》) issued by MIIT in October 2020, the MIIT will not issue Examination Letter for Foreign Investment in Telecommunication Business (《外商投資企業電信業務審定意見書》). Foreign invested enterprises would need to submit relevant foreign investment materials to MIIT for the establishment or change of telecommunication operating permits.

Regulations on Mobile Internet Applications

In June 2016, the CAC promulgated the Administrative Provisions on Mobile Internet Application Information Services (《移動互聯網應用程序信息服務管理規定》) (the “**Mobile Application Administrative Provisions**”), which became effective on August 1, 2016. Pursuant to the Mobile Application Administrative Provisions, a mobile internet app refers to an app software that runs on mobile smart devices providing information services after being pre-installed, downloaded or embedded through other means. Mobile internet app providers refer to the owners or operators of mobile internet apps. Internet app stores refer to platforms which provide services related to online browsing, searching and downloading of app software and releasing of development tools and products through the internet.

Pursuant to the Mobile Application Administrative Provisions, an internet app program provider must verify a user’s mobile phone number and other identity information under the principle of mandatory real name registration at the back-office end and voluntary real name display at the front-office end. An internet app provider must not enable functions that can collect a user’s geographical location information, access user’s contact list, activate the camera or recorder of the user’s mobile smart device or other functions irrelevant to its services, nor is it allowed to conduct bundle installations of irrelevant app programs, unless it has clearly indicated to the user and obtained the user’s consent on such functions and app programs. In respect of an internet app store service provider, the Mobile Application Administrative Provisions require that, among others, it must file a record with the local authority within 30 days after it rolls out the internet app store service online. It must also examine the authenticity, security and legality of internet app providers on its platform, establish a system to monitor app providers’ credit and file a record of such information with relevant governmental

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authorities. If an app provider violates the regulations, the internet app store service provider must take measures to stop the violations, including giving a warning, suspension of release, withdrawal of the app from the platform, keeping a record of the incident and reporting the incident to the relevant governmental authorities.

In December 2016, the MIIT promulgated the Interim Measures on the Administration of Pre-Installation and Distribution of Applications for Mobile Smart Terminals (《移動智能終端應用軟件預置和分發管理暫行規定》) (the “**Interim Measures**”), which came into effect on July 1, 2017. The Interim Measures aim to enhance the administration of mobile apps, and require, among others, that mobile phone manufacturers and internet information service providers must ensure that a mobile app, as well as its ancillary resource files, configuration files and user data can be uninstalled by a user on a convenient basis, unless it is a basic function software, which refers to a software that supports the normal functioning of the hardware and operating system of a mobile smart device.

Regulations on Internet Information Search Service

In June 2016, the CAC promulgated the Administrative Provisions on Internet Information Search Services (《互聯網信息搜索服務管理規定》) (the “**Search Services Administrative Provisions**”), which took effect on August 1, 2016. Pursuant to the Search Services Administrative Provisions, internet information search service refers to the service whereby users can search for information that is collected from the internet and processed by computer technology. The Search Services Administrative Provisions require that an internet information search service provider must not publish any information or contents prohibited by law in the form of links, abstracts, snapshots, associative words, related search or recommendations or otherwise. If an internet information search service provider identifies any search results that contain any information, website or app that is prohibited by law, it must stop displaying the search results, record the infraction and report it to the relevant governmental authority. In addition, an internet information search service provider is prohibited from seeking illegitimate interest by means of unauthorized disconnection of links, or provision of search results containing false information. If an internet information search service provider engages in paid search services, it must examine and verify the qualifications of its customers of the paid search services, specify the maximum percentage of search results as paid search results on a webpage, clearly distinguish paid search results from natural search results, and notably identify the paid search information item by item.

Regulations on News Display

Displaying news on a website and disseminating news through the internet are highly regulated in the PRC. The Provisional Measures for Administering Internet Websites Carrying on the News Displaying Business (《互聯網站從事登載新聞業務管理暫行規定》), jointly promulgated by the State Council News Office and the MIIT in November 2000, require an ICP operator (other than a government authorized news unit) to obtain an approval from the State Council News Office to post news on its website or disseminate news through the internet. Furthermore, the disseminated news must come from government-approved sources pursuant to contracts between the ICP operator and the sources, copies of which must be filed with the relevant government authorities.

In May 2017, the CAC issued the Provisions on the Administration of Internet News Information Services (《互聯網新聞信息服務管理規定》) (the “**Internet News Regulation**”), and its implementing rules, which became effective on June 1, 2017. Pursuant to the Internet News Regulation and its implementing rules, if an entity intends to provide internet news information service, it is required to obtain an approval from the State Council News Office and receive an Internet News Information

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Service License. Internet news information service refers to editing, publishing and reprinting and the dissemination platform service of internet news through internet websites, mobile apps, forums, blogs, micro-blogs, official accounts, instant message tools, live-streaming and other similar means. Pursuant to the Internet News Regulation, no internet news information service organizations may take the form of a foreign-invested enterprise, whether a joint venture or a wholly foreign-owned enterprise, and no cooperation between internet news information service organizations and foreign-invested enterprises is allowed prior to the security evaluation by the CAC.

Regulations on Internet Drug Information Services

According to the Provisions on the Administration of Internet Drug Information Services (《互聯網藥品信息服務管理辦法》), which was promulgated by the State Food and Drug Administration and most recently amended in November 2017, an enterprise publishing drug-related information must obtain a qualification certificate from the provincial-level food and drug administration before it applies for the ICP license or files with the MIIT or its local provincial-level counterpart. In addition, the Standing Committee of the National People’s Congress further amended the Drug Administration Law (《藥品管理法》) on August 26, 2019, which became effective on December 1, 2019. An ICP service operator that provides information regarding drugs or medical devices must obtain an Internet Drug Information Service Qualification Certificate (互聯網藥品信息服務許可證) from the applicable provincial level administrative authority.

Regulations on Internet Culture Activities

The Provisional Measures for the Internet Culture Administration (《互聯網文化管理暫行規定》), promulgated by the Ministry of Culture and with the latest amendment becoming effective in December 2017, require ICP operators engaging in “internet culture activities” to obtain a permit from the Ministry of Culture. The “internet culture activities” include, among other things, online dissemination of internet cultural products and the production, reproduction, importation, distribution and broadcasting of internet cultural products. In May 2019, the Ministry of Culture and Tourism issued the Circular regarding Adjusting the Scope of Approval of Internet Culture Business Permit and Further Regulating Approval Matters (《關於調整<網絡文化經營許可證>審批範圍進一步規範審批工作的通知》) to adjust the applicable scope of the Internet Culture Business Permit. Pursuant to the circular, the Ministry of Culture and Tourism will no longer be the authority supervising the online game industry and therefore the business scope of an Internet Culture Business Permit issued by it and its local counterparts will only cover internet cultural products including online music, online plays or programs, online performance, online works of art, online cartoon and exhibition and online matches, but exclude online games. Imported internet cultural products are subject to content review by the Ministry of Culture and Tourism before they are disseminated online, while domestic internet cultural products must be filed with the local branch of the Ministry of Culture within 30 days following the online dissemination. Service providers are also required to conduct self-review of the content of internet cultural products before they are put on the internet or submitted to the Ministry of Culture for approvals or filings.

The Several Suggestions on the Development and Administration of Internet Music (《文化部關於網絡音樂發展和管理的若干意見》), issued by the Ministry of Culture and becoming effective in November 2006, reiterate the requirement for an internet service provider to obtain the Internet Culture Business Permit to carry on any business of internet music products. In addition, foreign investors are prohibited from engaging in the internet culture business operation.

In October 2015, the Ministry of Culture promulgated a notice, which took effect on January 1, 2016, to further strengthen its regulation over online music, including requiring online platforms that allow

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users to upload self-created or performed music to set up real-time monitoring systems and requiring online music service providers to make quarterly filings of information related to their content self-review with the local counterpart of the Ministry of Culture from April 1, 2016.

The Regulations for the Administration of Audio and Video Products (《音像製品管理條例》), as released by the State Council in December 2001 and last amended in November 2020, require that the publication, production, duplication, importation, wholesale, retail and renting of audio and video products are subject to a license issued by competent authorities.

Regulations on Publication and Internet Publishing

In February 2016, the State Administration of Press, Publication, Radio, Film and Television (currently known as the National Press and Publication Administration, the “NPPA”), and the MIIT jointly issued the Administrative Provisions on Internet Publishing Service (《網絡出版服務管理規定》) (the “**Internet Publishing Regulation**”), which took effect on March 10, 2016, and replaced the Interim Provisions for the Administration of Internet Publishing (《互聯網出版管理暫行規定》) promulgated in 2002. The Internet Publishing Regulation requires that any entity engaged in the provision of online publications to the public via information networks obtain an Internet Publication License from the NPPA. Online publications refer to digital works with editing, production, processing and other publishing features, provided to the public via information networks, which mainly include: (i) informative and thoughtful text, pictures, maps, games, animation, audio and video digitizing books and other original digital works in fields such as literature, art and science, (ii) digital works consistent with the content of published books, newspapers, periodicals, audio-visual products and electronic publications, (iii) the network literature database or other digital works formed through aforementioned works by selecting, organizing, compiling and other means, and (iv) other types of digital works determined by the NPPA. The servers and storage facilities used by internet publishers must be located within the territory of the PRC. The Internet Publishing Regulation also provides that when an internet service provider provides manual intervention search ranking, advertising, promotion and other services to customers that provide internet publishing services, it is required to check and examine the Internet Publication Licenses obtained by the customers and the business scope of such licenses.

Regulations on Production and Operation of Audio/Video Programs

Under the Regulations on the Administration of Production of Radio and Television Programs (《廣播電視節目製作經營管理規定》) issued by the SAFRT in July 2004 and recently partly amended in October 2020, any entities that engage in the production of radio and television programs are required to apply for a Permit for Production and Operation of Radio and TV Programs (廣播電視節目製作經營許可證) from the competent administrative authority. Entities with this permit must conduct their business operations in compliance with the approved scope of production and operation.

On March 17, 2010, the SARFT issued the Internet Audio/Video Program Services Categories (Provisional) (《互聯網視聽節目服務業務分類目錄(試行)》), or the Provisional Categories, which were amended on March 10, 2017. The amended Provisional Categories classified Internet audio/video programs into four categories, which are further divided into seventeen sub-categories.

Regulations on Broadcasting Audio/Video Programs through the Internet

In December 2007, the State Administration of Radio, Film and Television, or the “SARFT” (currently known as NRTA) and the MIIT jointly promulgated the Rules for the Administration of Internet Audio and Video Program Services (《互聯網視聽節目服務管理規定》), commonly known as “Document

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56,” which took effect on January 31, 2008 and was further amended on August 28, 2015. Pursuant to Document 56, an online audio/video service provider must obtain an Online Audio/Video Program Transmission License, which has a term of three years, and operate in accordance with the scope of the business as stipulated in the license. Furthermore, Document 56 requires all online audio/video service providers to be either wholly state-owned or state-controlled. According to some official answers to press inquiries published on the SARFT’s website in February 2008, officials from the SARFT and the MIIT clarified that online audio/video service providers that already had been operating lawfully prior to the issuance of Document 56 may re-register and continue to operate without becoming state-owned or controlled, provided that the providers have not engaged in any unlawful activities. This exemption will not be granted to online audio/video service providers established after Document 56 was issued. In addition, foreign-invested enterprises are not allowed to engage in the above-mentioned businesses. On March 16, 2018, the NRTA issued the Notice on Further Regulating the Transmission Orders of Internet Audio and Video Program (《關於進一步規範網絡視聽節目傳播秩序的通知》), pursuant to which, among others, (i) online streaming platforms shall not illegally capture, edit, or reprogram audio-video programs, (ii) the movie clips and prevue broadcasted on the platform shall come from the licensed broadcasting and television programs; and (iii) the platform shall verify qualifications of sponsors for programs on the platform and shall refrain from accepting sponsorship or advertising from or cooperating in any other form with any unlicensed online audio/video service providers.

According to Document 56 and other relevant laws and regulations, audio-video programs provided by the entities supplying Internet audio-video program services shall not contain any illegal content or other content prohibited by the laws and regulations, such as any content against the basic principles in the PRC Constitution, any content that damages the sovereignty of the country or national security, and any content that disturbs social order or undermine social stability. An audio-video program that has already been broadcast shall be retained in full for at least 60 days. Movies, television programs and other media content used as Internet audio-video programs shall comply with relevant administrative regulations on programs broadcasts through radio, movie and television channels. Entities providing services related to Internet audio-video programs shall immediately delete the audio-video programs violating laws and regulations, keep relevant records, report relevant authorities and implement other regulatory requirements.

On October 31, 2018, the NRTA issued the Notice on Further Strengthening the Management of Radio and Television and Network Audiovisual Cultural Programs (《關於進一步加強廣播電視和網絡視聽文藝節目管理的通知》), or Notice 60. According to Notice 60, all radio and television broadcasting institutes, network audiovisual program service institutes and program production institutes shall stick to the right political direction and strengthen value guidance; pursue people-centered creative orientation to curb bad tendencies such as pursuing celebrities, pan-entertainment and so on; persist in providing high-quality content, constantly innovate programs, and strictly control the remuneration of guests; and strengthen the governance of TV series, network series (including network movies) to promote the benign development of the industry; shall strengthen the use and management of ratings (click-through rate) survey data and resolutely crack down on ratings (click-through rate) forgeries, etc.

On May 27, 2016, SAPPRFT issued the Notice on Relevant Issues concerning Implementing the Approval Works of Upgrading Mobile Internet Audio-Video Program Service (《關於做好移動互聯網視聽節目服務增項審核工作有關問題的通知》), the “**Mobile Audio-Video Program Notice**”). The Mobile Audio-Video Program Notice provides that the mobile Internet audio-video program services shall be deemed Internet audio-video program service. Entities which have obtained the approvals to provide the Internet audio-video program services may use mobile WAP websites or mobile applications to provide audio-video program services. Entities with regulatory approvals may operate mobile applications to provide the audio-video program services. The types of the programs shall be

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within the permitted scope as provided in the licenses and such mobile applications shall be filed with the NRTA and/or SFB.

The PRC government has also promulgated a series of special regulatory measures governing live-streaming services. In November 2016, the CAC promulgated the Administrative Provisions on Internet Live-streaming Service (《互聯網直播服務管理規定》), which took effect on December 1, 2016. Pursuant to the Administrative Provisions, internet live-streaming service refers to continuous publishing of real-time information to the public on internet by means of video, audio, graphics, text or other forms, and an internet live-streaming service provider refers to an operator of the platform providing internet live-streaming service. In accordance with the administrative provisions, an internet live-streaming service provider must verify and register the identity information of publishers of live-streaming programs and users on its platform, and file the identity information of the publishers with the local governmental authority for record. Any internet live-streaming service provider engaging in news service must obtain internet news information service qualification and operate within the permitted scope of such qualification. In September 2016, the SAPPRFT issued the Circular on Strengthening Administration of Live-streaming Service of Network Audio/Video Programs (《關於加強網絡視聽節目直播服務管理有關問題的通知》). Pursuant to the circular, any entity that intends to engage in live audio/video broadcasting of major political, military, economic, social, cultural or sport events or activities, or live audio/video broadcasting of general social or cultural group activities, general sporting events or other organizational events, must obtain an Online Audio/Video Program Transmission License with a permitted operation scope covering the above business activities. Any entity or individual without qualification is prohibited from broadcasting live audio/radio programs involving news, variety shows, sports, interviews, commentary or other forms of programs through any online live-streaming platform or online live broadcasting booth, nor are they permitted to start a live broadcasting channel for any audio or radio programs. In addition, no entity or individual other than licensed radio stations or television stations are allowed to use "radio station," "television station," "broadcasting station," "TV" or other descriptive terms exclusive to television and radio broadcasting organizations to engage in any business on the internet without approval. Furthermore, the CAC issued a notice in July 2017 which requires operators of internet news and information reproduction and broadcasting services, including commercial website apps that contain live-streaming features, and other internet live-streaming services, to file with the local CAC starting from July 15, 2017. The Circular on Tightening the Administration of Internet Live-Streaming Services (《關於加強網絡直播服務管理工作的通知》) jointly issued jointly by the MIIT, the CAC and several other government agencies in August 2018 reiterates the license requirements for online-streaming service providers and requires the operator to file with the local public security authority within 30 days after it commences the service online.

On March 29, 2019, the Administrative Provisions on Minor-oriented Programs (《未成年人節目管理規定》) was issued by the NRTA and has become effective since April 30, 2019. According to these provisions, network audio-visual programs with minors as their main participants or recipients shall not contain any contents which are harmful to the minors, such as violence, pornography, heresy, superstition, drug taking and other illegal contents. On November 18, 2019, the CAC, the Ministry of Culture and Tourism and the NRTA jointly issued the Administrative Provisions on Online Audio-visual Information Services (《網絡音視頻信息服務管理規定》), or Circular No.3, which took effective on January 1, 2020. According to the Circular No.3, Online Audio-visual Information Services refer to the services of producing, publishing and disseminating audio-visual information offered to the public via Internet platforms, such as websites and application programs. Circular No.3 requires that no individual or entity is allowed to (i) use the online audio-visual information services or related technologies to engage in any activities which may jeopardize national security, undermine social

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stability or infringe legitimate right of others; (ii) produce, publish or disseminate any audio-visual information prohibited by the laws and regulations, such as Internet rumors. A provider of audio-visual information services must establish, maintain and optimize a rumors refuting regime, under which once it identifies that any user of audio-visual information services produces, publishes or disseminates any rumor by virtue of the technology of producing forged pictures or audio-visual information based on deep-learning or virtual reality, such provider must take measures to refute such rumors in a timely manner and file such situations with the competent authorities governing Internet information, culture and tourism, and radio and television.

Regulations on Internet Map Services

According to the Administrative Rules of Surveying Qualification Certificate (《測繪資質管理規定》), as most recently amended by the National Administration of Surveying, Mapping and Geo-information (a.k.a. the State Bureau of Surveying and Mapping) in August 2014, the provision of internet map services by any non-surveying and mapping enterprise is subject to the approval of the National Administration of Surveying, Mapping and Geo-information and requires a Surveying and Mapping Qualification Certificate. Internet maps refer to maps called or transmitted through the internet. Pursuant to the Notice on Further Strengthening the Administration of Internet Map Services Qualification (《關於進一步加強互聯網地圖服務資質管理工作的通知》) issued by the National Administration of Surveying, Mapping and Geo-information in December 2011, any entity without a Surveying and Mapping Qualification Certificate for internet map services is prohibited from providing any internet map services. According to the Provisions on the Administration of Examination of Maps (《地圖審核管理規定》) most recently amended on July 24, 2019, subject to limited exceptions, an enterprise must first apply for an approval by the relevant regulatory authority, if it intends to engage in any of the following activities: (i) publication, display, production, posting, import or export of a map or a product attached with a map, (ii) re-publication, re-display, re-production, re-posting, re-import or re-export of a map the content of which has been changed after it is approved, or other commercial products attached with such a map, and (iii) publication or display of a map or a product attached with a map overseas. The operator of an approved internet map is required to file the updated contents of the map with the relevant regulatory authority semi-annually, and re-apply for a new approval of the map when the two-year term of the existing approval expires.

Regulations on Online Games

Pursuant to the Internet Publishing Regulation and the Circular on Mobile Game Publishing Service (《關於移動遊戲出版服務管理的通知》), the online games services provided on websites by online game operator partners may be deemed as a type of “online publication service”, and may be required to obtain an Internet Publication License from the NPPA.

In September 2009, the General Administration of Press and Publication (currently known as the NPPA) together with several other government agencies issued Notice Regarding the Consistent Implementation of the “Measures 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 Examination and Approval of Online Games and the Examination and Approval of Imported Online Games (《關於貫徹落實國務院<“三定”規定>和中央編辦有關解釋，進一步加強網絡遊戲前置審批和進口網絡遊戲審批管理的通知》), or the Circular 13, which explicitly prohibits foreign investors from participating in online game operating businesses through wholly-owned enterprises, equity joint ventures or cooperative joint ventures in the PRC. Circular 13 expressly prohibits foreign investors from gaining control over or participating in PRC operating companies’ online game operations through indirect means, such as establishing joint venture companies, entering

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into contractual arrangements with or providing technical support to the operating companies, or through a disguised form, such as incorporating user registration, user account management or payment through game cards into online game platforms that are ultimately controlled or owned by foreign investors. Certain foreign companies offer online games provided by their game operator partners on websites or through smartphone app distribution platforms which are owned and operated by their consolidated affiliated entities under contractual agreements. If such contractual arrangements were deemed to be “indirect means” or “disguised form” under Circular 13, such relevant contractual arrangements may be challenged by the NPPA or other governmental authorities.

In October 2019, the NPPA promulgated the Circular on Preventing Minors from Developing Online Game Addictions (《關於防止未成年人沉迷網絡遊戲的通知》), which mandates that online game operators take, among others, the following measures to prevent minors from being addicted to online games: (i) the operator shall ensure that its online game users use valid and true identity information to register their game accounts; (ii) the operator shall strictly control the time slot and duration allowed for minors to log in and play online games to the extent that it shall not provide any game service for the minors in any form from 10:00 PM each day to 8:00 AM the next day, and the length of time a minor spends in playing its online games must not exceed three hours accumulatively on each statutory holiday and one and a half hours on each business day; and (iii) the online game operator shall not offer any paid services to minors that are not suitable for their civil capacity. According to such circular, these requirements are pre-conditions for an operator to publish and operate any online game.

Regulations on Online Game Virtual Currency

The Interim Administration Measures of Online Games (《網絡遊戲管理暫行辦法》), which has been repealed on July 10, 2019 while no other regulation has been issued or promulgated as of the Latest Practicable Date to replace this regulation) require companies that (i) issue online game virtual currency (including prepaid cards and/or pre-payment or prepaid card points) or (ii) offer online game virtual currency transaction services to apply for the Internet Culture Business Permit from provincial branches of the Ministry of Culture. The regulations prohibit companies that issue online game virtual currency from providing services that would enable the trading of such virtual currency. Any company that fails to submit the requisite application will be subject to sanctions, including but not limited to termination of operation, confiscation of incomes and fines. The regulations also prohibit online game operators from allocating virtual items or virtual currency to players based on random selection through lucky draw, wager or lottery that involve cash or virtual currency directly paid by the players. In addition, companies that issue online game virtual currency must comply with certain specific requirements. For example, online games virtual currency can only be used for products and services related to the issuance company’s own online games. Pursuant to the Circular on Regulating Online Game Operation and Strengthening Interim and Ex Post Supervision (《關於規範網絡遊戲運營加強事中事後監管工作的通知》) issued by the Ministry of Culture in December 2016, which took effect on May 1, 2017 and repealed on August 19, 2019, an online game operator must not allow online game virtual currency to exchange for legal currency or items, except in the case of termination of online game operation where the online game operator may refund the balance of online game virtual currency to players in the form of legal currency or in other means acceptable to the players. Moreover, pursuant to the circular, regulations applicable to online game virtual currency also apply to such other virtual items where the virtual items are issued by the online game operator, can be exchangeable for other virtual items or value-added services related to the games, and can be purchased with legal currency or online game virtual currency or exchanged for online game virtual currency. As of the Latest Practicable Date, no government authority has issued or promulgated any provisions to replace the above-mentioned regulations.

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Regulations on Advertisements and Online Advertising

The PRC Advertising Law (《中華人民共和國廣告法》), as most recently amended in October 2018, outlines the regulatory framework for the advertising industry, and allows foreign investors to own up to all equity interests in PRC advertising companies.

Advertisers, advertising operators and advertising distributors are required by PRC advertising laws and regulations to ensure that the contents of the advertisements they prepare or distribute are true and in full compliance with applicable laws and regulations. For example, pursuant to PRC Advertising Law, advertisements must not contain, among other prohibited contents, terms such as “the state-level,” “the highest grade,” “the best” or other similar words. In addition, where a special government review is required for certain categories of advertisements before publishing, the advertisers, advertising operators and advertising distributors are obligated to confirm that such review has been performed and the relevant approval has been obtained. Pursuant to the PRC Advertising Law, the use of the internet to distribute advertisements shall not affect the normal use of the internet by users. Particularly, advertisements distributed on internet pages such as pop-up advertisements shall be indicated with a conspicuous mark for “close” to ensure the close of such advertisements by one click. Where internet information service providers know or should know that illegal advertisements are being distributed using their services, they shall prevent such advertisements from being distributed.

In addition to the above regulations, the Interim Administration Measures of Internet Advertising (《互聯網廣告管理暫行辦法》), the “**Internet Advertising Measures**”) which was promulgated by the then State Administration for Industry and Commerce (currently known as the SAMR) and became effective on September 1, 2016 also set forth certain compliance requirements for online advertising businesses. For example, search engine service providers must indicate paid search results as an advertisement and distinguish paid search results from natural search results on their websites. Advertising operators and distributors of internet advertisements must examine, verify and record identity information, such as name, address and contact information, of advertisers, and maintain an updated verification record on a regular basis. Moreover, advertising operators and advertising distributors must examine supporting documentation provided by advertisers and verify the contents of the advertisements against supporting documents before publishing. If the contents of advertisements are inconsistent with the supporting documentation, or the supporting documentation is incomplete, advertising operators and distributors must refrain from providing design, production, agency or publishing services. The Internet Advertising Measures also prohibit the following activities: (i) providing or using apps and hardware to block, filter, skip over, tamper with, or cover up lawful advertisements; (ii) using network access, network equipment and apps to disrupt the normal transmission of lawful advertisements or adding or uploading advertisements without authorization; and (iii) harming the interests of a third party by using fake statistics or traffic data.

The SAMR has promulgated the Guidance regarding Strengthening the Supervision over Marketing Activities by Internet Live-Streaming (《關於加強網絡直播營銷活動監管的指導意見》) in November 2020 to further regulated marketing activities by Internet live-streaming. The NRTA also issued a circular on the Strengthening Management of Live-Streaming of Internet Shows and Electronic Commerce (《關於加強網絡秀場直播和電商直播管理的通知》) in November 2020 to provide instruction to online marketing activities through live-streaming. Platforms providing live-streaming of Internet show or electronic commerce shall register with National Internet Video-audio Platform Information Management System no later than November 30, 2020. The overall ratio of front-line content reviewers to live-streaming rooms on such platforms shall be no less than 1:50. The training for content reviewers shall be strengthened and content reviewers who have passed the training shall be registered in the Reviewer Information Management System. A platform shall report the number of its

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live-streaming rooms, streamers and content reviewers to the provincial branch of the NRTA on a quarterly basis. Internet show live-streaming platforms shall tag content of live-streaming rooms and corresponding streamers by category. A streamer cannot change the category of the programs tagged in his or her live-streaming room without prior approval from the platform. Users that are minors or without real-name registration are prohibited from virtual tipping, and platforms shall cap the amount of virtual tipping per time, per day, and per month. When the virtual tipping by a user reaches half of the daily/monthly limit, a consumption notification from the platform and a confirmation from the user by text messages or other means are required before the processing the next transaction. When the amount of virtual tipping by a user reaches the daily/monthly limit, the platform shall suspend the virtual tipping function for such user for that day or month. To host any electronic commerce promotion events such as E-commerce Festival, E-commerce Day or Promotion Day in the forms of live-streaming rooms, live performances, live variety shows and other live programs, the platforms shall register the information of guests, streamers, content and settings with the local branch of NRTA 14 business days in advance. Internet electronic commerce live-streaming platforms shall conduct relevant qualification examination and real-name authentication on businesses and individuals providing live-streaming marketing services and keep complete examination and authentication records, and shall not enable imposters or businesses or individuals without qualification or real-name registration to conduct live-streaming marketing services.

Violation of these regulations may result in penalties, including fines, confiscation of advertising income, orders to cease dissemination of the advertisements and orders to publish an advertisement correcting the misleading information. In the case of serious violations, the SAMR or its local branches may force the violator to terminate its advertising operation or even revoke its business license. Furthermore, advertisers, advertising operators or advertising distributors may be subject to civil liability if they infringe on the legal rights and interests of third parties.

Regulations on Artificial Intelligence and Autonomous Driving Vehicles

The Chinese government has issued a series of guidelines to encourage and support the research and development of AI technology, such as the Three-Year Implementing Plan for Internet Plus Artificial Intelligence (《“互聯網+”人工智能三年行動實施方案》) issued in May 2016 and the Development Planning on the New Generation of Artificial Intelligence (《關於印發新一代人工智能發展規劃的通知》) issued in July 2017. In particular, the MIIT, the Ministry of Public Security and the Ministry of Transport, issued the Circular on the Norms on Administration of Road Testing of Autonomous Driving Vehicles (Trial Implementation) (《智能網聯汽車道路測試管理規範(試行)》) in April 2018, which became effective from May 1, 2018 and is the primary regulation governing protocol of road testing of autonomous driving vehicles in the PRC. Pursuant to this circular, any entity intending to conduct a road testing of autonomous driving vehicles must apply for and obtain a road-testing certificate and a temporary license plate for each tested car. To qualify for these required licenses, an applicant entity must satisfy, among others, the following requirements: (i) it must be an independent legal person registered under PRC law with the capacity to conduct manufacturing, technological research or testing of automobiles and automobile parts, which has established protocol to test and assess the performance of autonomous driving system and is capable of conducting real-time remote monitor of the tested cars; (ii) the vehicle under road testing must be equipped with a driving system that can switch between autonomous pilot model and human driving model in a safe, quick and simple manner and allows human driver to take control of the vehicle any time immediately when necessary; (iii) the tested vehicle must be equipped with the function of recording, storing and real-time monitoring the condition of the vehicle and is able to transmit real-time data of the vehicle, such as the driving model, location and speed; (iv) the applicant entity must sign an employment contract or a labor service contract with the driver of the tested vehicle, who must be a licensed driver with more

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than three years’ driving experience and a track record of safe driving and is familiar with the testing protocol for autonomous driving system and proficient in operating the system; (v) the applicant entity must insure each tested vehicle for at least RMB5 million against car accidents or provide a letter of guarantee covering the same. During testing, the testing entity should post a noticeable identification logo for autonomous driving test on each tested car and should not use autonomous driving model unless in the permitted testing areas specified in the road-testing certificate. If the testing entity intends to conduct road testing in the region beyond the administrative territory of the certificate issuing authority, it must apply for a separate road-testing certificate and a separate temporary license plate from the relevant authority supervising the road-testing of autonomous cars in that region. In addition, the testing entity is required to submit to the road-testing certificate issuing authority a periodical testing report every six months and a final testing report within one month after completion of the road testing. In the case of a car accident causing severe injury or death of personnel or vehicle damage, the testing entity must report the accident to the road-testing certificate issuing authority within 24 hours and submit a comprehensive analysis report in writing covering cause analysis, final liability allocation results, etc. within five working days after the traffic enforcement agency determines the liability for the accident. Some local governments, such as Beijing, Shanghai, Chongqing, Hunan and Tianjin, have issued local rules and regulations to regulate road testing of autonomous driving cars accordingly.

Regulation on Product Quality

Products made in mainland China shall be subject to the Product Quality Law of the PRC (《中華人民共和國產品質量法》) (the “**Product Quality Law**”), which was promulgated on February 22, 1993 and most recently amended on December 29, 2018. According to the Product Quality Law, a seller of a product shall be responsible for repairing, replacing or returning the product with any of the following defects, and shall compensate for the damages incurred by consumers who bought such defective product: (i) the product does not have the usability which such product should have and there are no prior indications about such situation; (ii) the actual quality of such product fails to comply with the standards specified on such product or the package of such product; and (iii) the actual quality of such product fails to meet the quality status specified by way of product specifications and samples. After the seller performs its obligation of repairing, replacing and returning the defective product and/or compensating for the customers’ damages, such seller is entitled to seek reimbursement from the manufacturer of such product, if it could be proved that the defect is caused by the manufacturer. According to the Product Quality Law, a manufacturer of a product shall be responsible to compensate for the damages to any person caused by the defect of such product, unless the manufacturer is able to prove that: (i) it did not circulate the product; (ii) the defect did not exist at the time when the product was circulated; or (iii) scientific or technologic knowledge at the time when such product was circulated was not such that it allowed the defect to be discovered.

Regulations on Tort Liability

In accordance with the Tort Liability Law of the PRC (《中華人民共和國侵權責任法》) (the “**Tort Liability Law**”), which became effective in July 2010, internet users and internet service providers bear tortious liabilities in the event that they infringe upon other persons’ rights and interests through the internet. Where an internet user conducts tortious acts through internet services, the infringed person has the right to request the internet service provider take necessary actions such as deleting contents, screening and de-linking. Failing to take necessary actions after being informed, the internet service provider will be subject to joint and several liabilities with the internet user with regard to the additional damages incurred. Where an internet service provider knows that an internet user is infringing upon other persons’ rights and interests through its internet service but fails to take necessary actions, it is jointly and severally liable with the internet user. In addition, in accordance

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with the Tort Liability Law, in the event of any damage arising from a defective product, the infringed person may seek compensation from either the manufacturer or the seller of such product. If the manufacturer has compensated the infringed person but the defect is caused by the fault of the seller, the manufacturer is entitled to seek reimbursement from the seller. If the seller has compensated the infringed person but the defect is caused by the manufacturer, the seller is entitled to seek reimbursement from the manufacturer. The National People’s Congress adopted the Civil Code of the PRC (《中華人民共和國民法典》), the “**Civil Code**”) on May 28, 2020, which came into effect on January 1, 2021 and revoked the Tort Liability Law. The Civil Code has further revised the Internet tort liability as originally provided in the Tort Liability Law. It has further elaborated on “safe harbor” rule with respect to an internet service provider from both the aspects of notice and counter notice, including (i) upon receiving notice from the right holder, promptly adopting necessary protective measures such as deletion, screening or disconnection of hyperlinks and reefing right holder’s notice to disputed internet user; and (ii) upon receiving counter-notice from the disputed internet user, referring such counter-notice to the claiming right holder and informing him/her to take other corresponding measures such as filing complaint with competent authorities or suit with courts. The Civil Code has also provides that where the internet service provider knew or should have known the infringing acts of the internet user, it shall be severally liable with such internet user. As for product liability, the Civil Code provides additional mitigation measures such as stop selling of defective products and stipulated that the seller and manufacturer shall also be liable for expanded damages caused by such defective products if no mitigation measures are provided or not sufficient. If a recall of defective product is required, the seller and the manufacturer shall be responsible to undertake fees paid by infringed users.

Regulations on Intellectual Property Rights

The PRC has adopted legislation governing intellectual property rights, including patents, copyrights, trademarks, and domain names.

Patent. The Patent Law of the PRC (《中華人民共和國專利法》) provides for patentable inventions, utility models and designs, which must meet three conditions: novelty, inventiveness and practical applicability. The State Intellectual Property Office under the State Council is responsible for examining and approving patent applications. A patent is valid for a term of twenty years in the case of an invention and a term of ten years in the case of utility models and designs.

Copyright. The Copyright Law of the PRC (《中華人民共和國著作權法》), the “**Copyright Law**”) and its implementation rules extend copyright protection to products disseminated over the internet and computer software. There is a voluntary registration system administered by the China Copyright Protection Center. Creators of protected works enjoy personal and property rights, including, among others, the right of disseminating the works through information networks.

Pursuant to the relevant PRC regulations, rules and interpretations, ICP operators will be jointly liable with the infringer if they (a) participate in, assist in or abet infringing activities committed by any other person through the internet, (b) are or should be aware of the infringing activities committed by their website users through the internet, or (c) fail to remove infringing content or take other action to eliminate infringing consequences after receiving a warning with evidence of such infringing activities from the copyright holder. The court will determine whether an internet service provider should have known of their internet users’ infringing activities based on how obvious the infringing activities are by taking into consideration a number of factors, including (i) the information management capabilities that the provider should have based on the possibility that the services provided by it may trigger infringing acts, (ii) the degree of obviousness of the infringing content, (iii) whether it has taken the initiative to select, edit, modify or recommend the contents involved, (iv) whether it has taken positive

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and reasonable measures against infringing acts, and (v) whether it has set up convenient programs to receive notices of infringement and made timely and reasonable responses to the notices. Where an internet service provider has directly obtained economic benefits from any contents made available by an internet user, it shall have a higher duty of care with respect to the internet user's act of infringement of others' copyrights. Advertisements placed for or other benefits particularly connected with specific contents may be deemed as direct economic benefits from such contents, but general advertising fees or service fees charged by an internet service provider for its internet services will not be included. In addition, where an ICP operator is clearly aware of the infringement of certain content against another's copyright through the internet, or fails to take measures to remove relevant contents upon receipt of the copyright holder's notice, and as a result, it damages the public interest, the ICP operator could be ordered to stop the tortious act and be subject to other administrative penalties such as confiscation of illegal income and fines. An ICP operator is also required to retain all infringement notices for a minimum of six months and to record the content, display time and IP addresses or the domain names related to the infringement for a minimum of 60 days.

Pursuant to the Copyright Law and its implementation rules, creators of protected works enjoy personal and property rights such as the right of disseminating the works through information networks. In addition, the Regulations for the Protection of Information Network Transmission Right (《信息網絡傳播權保護條例》) promulgated by the State Council on May 18, 2006, and amended on January 30, 2013, specify the rules on a safe harbor for use of copyrights and copyright management technology. An internet service provider may be exempted from liabilities for providing links to infringing or illegal content or providing other internet services which are used by its users to infringe others' copyright, if it does not know and does not have constructive knowledge that such content is infringing upon other parties' rights or is illegal. However, if the legitimate owner of the content notifies the internet service provider and requests removal of the links to the infringing content, the internet service provider would be deemed to have constructive knowledge upon receipt of such notification, but would be exempted from liabilities if it removes or disconnects the links to the infringing content at the request of the legitimate owner. At the request of the alleged infringer, the internet service provider should immediately restore links to content previously disconnected upon receipt of initial non-infringing evidence.

Software Products. The Regulation for the Protection of Computer Software (《計算機軟件保護條例》) promulgated by the State Council on December 20, 2001 and last amended on January 30, 2013. To further implementing this regulation, the Computer Software Copyright Registration Measures (《計算機軟件著作權登記辦法》) promulgated by the China Copyright Office on February 20, 2002, regulates software copyright registration, exclusive licensing contracts of software copyright and transfer agreements. Although such registration is not mandatory under PRC law, software copyright owners are encouraged to go through the registration process and registered software may receive better protection.

Trademark. The Trademark Law of the PRC (《中華人民共和國商標法》) and its implementation rules protect registered trademarks. The Trademark Office of National Intellectual Property Administration under the SAMR handles trademark registrations and grants a term of ten years to registered trademarks. Trademark license agreements must be filed with the Trademark Office of National Intellectual Property Administration for record.

Domain name. Domain names are protected under the Administrative Measures on the Internet Domain Names (《互聯網域名管理辦法》) promulgated by the MIIT in August 2017, which became effective in November 2017. The MIIT is the major regulatory body responsible for the administration of the PRC internet domain names, and under the supervision of the MIIT, the China Internet Network

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Information Center, or CNNIC, is responsible for the daily administration of “.cn” domain names and Chinese domain names. According to the Circular on Administration of the Use of Domain Names for Internet Information Services (《關於規範互聯網信息服務使用域名的通知》) issued by the MIIT in November 2017, only the internet information service provider itself or the shareholder(s), principal or senior management officer(s) of the internet information service provider are eligible to register the domain names used for the internet information services.

Regulations on Information Security

The National People’s Congress has enacted legislation that prohibits use of the internet that breaches the public security, disseminates socially destabilizing content or leaks state secrets. Breach of public security includes breach of national security and infringement on legal rights and interests of the state, society or citizens. Socially destabilizing content includes any content that incites defiance or violations of PRC laws or regulations or subversion of the PRC government or its political system, spreads socially disruptive rumors or involves cult activities, superstition, obscenities, pornography, gambling or violence. State secrets are defined broadly to include information concerning PRC national defense, state affairs and other matters as determined by the PRC authorities.

Pursuant to applicable regulations, ICP operators must complete mandatory security filing procedures and regularly update information security and monitoring systems for their websites with local public security authorities, and must also report any public dissemination of prohibited content.

In December 2015, the Standing Committee of the National People’s Congress promulgated the Anti-Terrorism Law of the PRC (《中華人民共和國反恐怖主義法》, the “**Anti-Terrorism Law**”), which took effect on January 1, 2016 and was amended on April 27, 2018. According to the Anti-Terrorism Law, telecommunication service operators or internet service providers shall (i) carry out pertinent anti-terrorism publicity and education to society; (ii) provide technical interfaces, decryption and other technical support and assistance for the competent departments to prevent and investigate terrorist activities; (iii) implement network security and information monitoring systems as well as safety and technical prevention measures to avoid the dissemination of terrorism information, delete the terrorism information, immediately halt its dissemination, keep relevant records and report to the competent departments once the terrorism information is discovered; and (iv) examine customer identities before providing services. Any violation of the Anti-Terrorism Law may result in severe penalties, including substantial fines.

In November 2016, the Standing Committee of the National People’s Congress promulgated the Cyber Security Law of the PRC (《中華人民共和國網絡安全法》, the “**Cyber Security Law**”), which took effect on June 1, 2017. In accordance with the Cyber Security Law, network operators must comply with applicable laws and regulations and fulfill their obligations to safeguard network security in conducting business and providing services. Network service providers must take technical and other necessary measures as required by laws, regulations and mandatory requirements to safeguard the operation of networks, respond to network security effectively, prevent illegal and criminal activities, and maintain the integrity, confidentiality and usability of network data.

In addition, the State Secrecy Bureau has issued provisions authorizing the blocking of access to any website it deems to be leaking state secrets or failing to comply with the relevant legislation regarding the protection of state secrets during online information distribution. Specifically, internet companies in the PRC with bulletin boards, chat rooms or similar services must apply for specific approval prior to operating such services.

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Furthermore, the Provisions on Technological Measures for Internet Security Protection (《互聯網安全保護技術措施規定》), promulgated by the Ministry of Public Security and became effective in March 2006, require all ICP operators to keep records of certain information about its 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 submit the above information as required by laws and regulations. The Decision on Strengthening Network Information Protection (《關於加強網絡信息保護的決定》, the “**Network Information Protection Decision**”), which was promulgated by the PRC National People’s Congress in December 2012, states that ICP operators must request identity information from users when ICP operators provide information publication services to the users. If ICP operators come across prohibited information, they must immediately cease the transmission of such information, delete the information, keep relevant records, and report to relevant government authorities.

On October 21, 2019, the Supreme People’s Court and the Supreme People’s Procuratorate of the PRC jointly issued the Interpretations on Certain Issues Regarding the Applicable of Law in the Handling of Criminal Case Involving Illegal Use of Information Networks and Assisting Committing Internet Crimes (《最高人民法院、最高人民檢察院關於辦理非法利用信息網絡、幫助信息網絡犯罪活動等刑事案件適用法律若干問題的解釋》), which came into effect on November 1, 2019, and further clarifies the meaning of Internet service provider and the severe situations of the relevant crimes.

Regulations on Internet Privacy

The PRC Constitution (《中華人民共和國憲法》) states that PRC law protects the freedom and privacy of communications of citizens and prohibits infringement of these rights. In recent years, PRC government authorities have enacted legislation on internet use to protect personal information from any unauthorized disclosure. The Network Information Protection Decision provides that electronic information that identifies a citizen or involves privacy of any citizen is protected by law and must not be unlawfully collected or provided to others. ICP operators collecting or using personal electronic information of citizens must specify the purposes, manners and scopes of information collection and uses, obtain consent of the relevant citizens, and keep the collected personal information confidential. ICP operators are prohibited from disclosing, tampering with, damaging, selling or illegally providing others with, collected personal information. ICP operators are required to take technical and other measures to prevent the collected personal information from any unauthorized disclosure, damage or loss. The Administrative Measures on Internet Information Services prohibit an ICP operator from insulting or slandering a third party or infringing upon the lawful rights and interests of a third party. According to the Provisions on Protection of Personal Information of Telecommunication and Internet Users (《電信和互聯網用戶個人信息保護規定》), which was promulgated by MIIT and became effective in September 2013, telecommunication business operators and ICP operators are responsible for the security of the personal information of users they collect or use in the course of their provision of services. Without obtaining the consent from the users, telecommunication business operators and ICP operators may not collect or use the users’ personal information. The personal information collected or used in the course of provision of services by the telecommunication business operators or ICP operators must be kept in strict confidence, and may not be divulged, tampered with or damaged, and may not be sold or illegally provided to others. The ICP operators are required to take certain measures to prevent any divulgence of, damage to, tampering with or loss of users’ personal information. In accordance with the Cyber Security Law, network operators are required to collect and use personal information in compliance with the principles of legitimacy, properness and necessity, and strictly within the scope of authorization by the subject of personal information unless otherwise prescribed by laws or regulations. In the event of any unauthorized disclosure, damage or loss of collected personal information, network operators must take immediate remedial measures, notify the affected users and report the incidents to the relevant authorities in a timely manner. If any user knows

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that a network operator illegally collects and uses his or her personal information in violation of laws, regulations or any agreement with the user, or the collected and stored personal information is inaccurate or wrong, the user has the right to request the network operator to delete or correct the relevant collected personal information.

The relevant telecommunications authorities are further authorized to order ICP operators to rectify unauthorized disclosure. ICP operators are subject to legal liability, including warnings, fines, confiscation of illegal gains, revocation of licenses or filings, closing of the relevant websites, administrative punishment, criminal liabilities, or civil liabilities, if they violate relevant provisions on internet privacy. Pursuant to the Ninth Amendment to the Criminal Law (《中華人民共和國刑法修正案(九)》) issued by the Standing Committee of the National People’s Congress in August 2015 and becoming effective in November 2015, the standards of crime of infringing citizens’ personal information were amended accordingly and the criminal culpability of unlawful collection, transaction, and provision of personal information has been reinforced. In addition, any ICP provider that fails to fulfill the obligations related to internet information security administration as required by applicable laws and refuses to rectify upon orders, will be subject to criminal liability for (i) any dissemination of illegal information in large scale; (ii) any severe effect due to the leakage of the client’s information; (iii) any serious loss of evidence of criminal activities; or (iv) other severe situations, and any individual or entity that (x) sells or provides personal information to others unlawfully, or (y) steals or illegally obtains any personal information, will be subject to criminal liability in severe situations. In addition, the Interpretations of the Supreme People’s Court and the Supreme People’s Procuratorate of the PRC on Several Issues Concerning the Application of Law in Handling Criminal Cases of Infringing Personal Information (《最高人民法院、最高人民檢察院關於辦理侵犯公民個人信息刑事案件適用法律若干問題的解釋》), effective in June 2017, have clarified certain standards for the conviction and sentencing in relation to personal information infringement. The PRC government has the power and authority to order ICP operators to turn over personal information if an internet user posts any prohibited content or engages in illegal activities on the internet. The Civil Code further provides in a stand-alone chapter of right of personality and reiterate that the personal information of a natural person shall be protected by the law. Any organization or individual shall legitimately obtain such personal information of others in due course on a need-to-know basis and ensure the safety and privacy of such information, and refrain from excessively handling or using such information.

With respect to the security of information collected and used by mobile apps, pursuant to the Announcement of Conducting Special Supervision against the Illegal Collection and Use of Personal Information by Apps (《關於開展APP違法違規收集使用個人信息專項治理的公告》), which was issued on January 23, 2019, app operators should collect and use personal information in compliance with the Cyber Security Law and should be responsible for the security of personal information obtained from users and take effective measures to strengthen the personal information protection. Furthermore, app operators should not force their users to make authorization by means of bundling, suspending installation or in other default forms and should not collect personal information in violation of laws, regulations or breach of user agreements. Such regulatory requirements were emphasized by the Notice on the Special Rectification of Apps Infringing upon User’s Personal Rights and Interests (《關於開展APP侵害用戶權益專項整治工作的通知》), which was issued by MIIT on October 31, 2019. On November 28, 2019, the CAC, the MIIT, the Ministry of Public Security and the SMAR jointly issued the Methods of Identifying Illegal Acts of Apps to Collect and Use Personal Information (《App違法違規收集使用個人信息行為認定方法》). This regulation further illustrates certain commonly-seen illegal practices of apps operators in terms of personal information protection, including “failure to publicize rules for collecting and using personal information”, “failure to expressly state the purpose, manner and scope of collecting and using personal information”, “collection and use of personal information

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without consent of users of such App”, “collecting personal information irrelevant to the services provided by such app in violation of the principle of necessity”, “provision of personal information to others without users’ consent”, “failure to provide the function of deleting or correcting personal information as required by laws” and “failure to publish information such as methods for complaints and reporting”. Among others, any of the following acts of an app operator will constitute “collection and use of personal information without consent of users”: (i) collecting an user’s personal information or activating the permission for collecting any user’s personal information without obtaining such user’s consent; (ii) collecting personal information or activating the permission for collecting the personal information of any user who explicitly refuses such collection, or repeatedly seeking for user’s consent such that the user’s normal use of such app is disturbed; (iii) any user’s personal information which has been actually collected by the app operator or the permission for collecting any user’s personal information activated by the app operator is beyond the scope of personal information which such user authorizes such app operator to collect; (iv) seeking for any user’s consent in a non-explicit manner; (v) modifying any user’s settings for activating the permission for collecting any personal information without such user’s consent; (vi) using users’ personal information and any algorithms to directionally push any information, without providing the option of non-directed pushing such information; (vii) misleading users to permit collecting their personal information or activating the permission for collecting such users’ personal information by improper methods such as fraud and deception; (viii) failing to provide users with the means and methods to withdraw their permission of collecting personal information; and (ix) collecting and using personal information in violation of the rules for collecting and using personal information promulgated by such app operator.

On August 22, 2019, the CAC promulgated the Children Information Protection Provisions (《兒童個人信息網絡保護規定》), which took effect on October 1, 2019, requiring that before collecting, using, transferring or disclosing the personal information of a child, the Internet service operator should inform the child’s guardians in a noticeable and clear manner and obtain their consents. Meanwhile, Internet service operators should take measures like encryption when storing children’s personal information.

In October 2020, the Standing Committee of the National People’s Congress issued the Draft Personal Information Protection Law (《個人信息保護法(草案)》) for public comments. The Draft Personal Information Protection Law integrates provisions from several rules with respect to personal information rights and privacy protection. According to the Draft Personal Information Protection Law, personal information refers to information related to identified or identifiable natural persons which is recorded by electronic or other means (excluding the anonymized information). The Draft Personal Information Protection Law provides the circumstances under which a personal information processor could process personal information, such as where the consent of the individual concerned is obtained and where it is necessary for the conclusion or performance of a contract to which such individual is a party to such contract. It also stipulates certain specific provisions with respect to the obligations of a personal information processor. As of the date of this document, the Draft Personal Information Protection Law has not come into effect.

Regulations on Anti-Monopoly Matters related to Internet Platform Companies.

The PRC Anti-monopoly Law (《中華人民共和國反壟斷法》), which took effect on August 1, 2008, prohibits monopolistic conduct such as entering into monopoly agreements, abusing market dominance and concentration of undertakings that may have the effect of eliminating or restricting competition. On February 7, 2021, the Anti-monopoly Commission of the State Council officially promulgated the Guidelines to Anti-Monopoly in the Field of Internet Platforms (《關於平台經濟領域的反壟斷指南》), or the Anti-Monopoly Guidelines for Internet Platforms. Pursuant to an official interpretation from the

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Anti-monopoly Commission of the State Council, the Anti-Monopoly Guidelines for Internet Platforms mainly covers five aspects, including general provisions, monopoly agreements, abusing market dominance, concentration of undertakings, and abusing of administrative powers eliminating or restricting competition. The Anti-Monopoly Guidelines for Internet Platforms prohibits certain monopolistic acts of internet platforms so as to protect market competition and safeguard interests of users and undertakings participating in internet platform economy, including without limitation, prohibiting platforms with dominant position from abusing their market dominance (such as discriminating customers in terms of pricing and other transactional conditions using big data and analytics, coercing counterparties into exclusivity arrangements, using technology means to block competitors’ interface, favourable positioning in search results of goods displays, using bundle services to sell services or products, compulsory collection of unnecessary user data). In addition, the Anti-Monopoly Guidelines for Internet Platforms also reinforces antitrust merger review for internet platform related transactions to safeguard market competition.

Regulations on Foreign Exchange

Foreign Currency Exchange

Pursuant to the Foreign Currency Administration Rules (《外匯管理條例》), as most recently amended in 2008, and various regulations issued by SAFE and other relevant PRC government authorities, RMB is freely convertible to the extent of current account items, such as trade related receipts and payments, interest and dividends. Capital account items, such as direct equity investments, loans and repatriation of investment, unless expressly exempted by laws and regulations, still require prior approval from SAFE or its provincial branch for conversion of RMB into a foreign currency, such as U.S. dollars, and remittance of the foreign currency outside of the PRC.

In August 2008, SAFE issued the Circular on the Relevant Operating Issues Concerning the Improvement of the Administration of the Payment and Settlement of Foreign Currency Capital of Foreign-Invested Enterprises (《關於完善外商投資企業外匯資本金支付結匯管理有關業務操作問題的通知》), or SAFE Circular 142, regulating the conversion by a foreign-invested enterprise of foreign currency-registered capital into RMB by restricting how the converted RMB may be used. In addition, SAFE promulgated Circular 45 on November 9, 2011 in order to clarify the application of SAFE Circular 142. Under SAFE Circular 142 and Circular 45, the RMB capital converted from foreign currency registered capital of a foreign-invested enterprise may only be used for purposes within the business scope approved by the applicable administrative authority and may not be used for equity investments within the PRC. In addition, SAFE strengthened its oversight of the flow and use of RMB capital converted from foreign currency registered capital of foreign-invested enterprises. The use of RMB capital may not be changed without SAFE’s approval, and RMB capital may not in any case be used to repay RMB loans if the proceeds of the loans have not been used.

To further reform the foreign exchange administration system in order to satisfy and facilitate the business and capital operations of foreign-invested enterprises, SAFE issued the Circular on the Relevant Issues Concerning the Launch of Reforming Trial of the Administration Model of the Settlement of Foreign Currency Capital of Foreign-Invested Enterprises in Certain Areas (《關於在部分地區開展外商投資企業外匯資本金結匯管理方式改革試點有關問題的通知》) in July 2014, which became effective on August 4, 2014. This circular suspends the application of SAFE Circular 142 in certain areas and allows a foreign-invested enterprise registered in these areas with a business scope including “investment” to use the RMB capital converted from foreign currency registered capital for equity investments within the PRC. SAFE released the Notice on the Reform of the Administration Method for the Settlement of Foreign Exchange Capital of Foreign-invested Enterprises (《關於改革

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外商投資企業外匯資金結匯管理方式的通知》) or SAFE Circular 19, in March 2015, which came into force and superseded SAFE Circular 142 on June 1, 2015. Circular 19 allows foreign-invested enterprises to settle their foreign exchange capital on a discretionary basis according to the actual needs of their business operation and provides the procedures for foreign-invested companies to use Renminbi converted from foreign currency-denominated capital for equity investment. Nevertheless, Circular 19 also reiterates the principle that Renminbi converted from foreign currency-denominated capital of a foreign-invested company may not be directly or indirectly used for purposes beyond its business scope.

In June 2016, SAFE issued the Circular on Reforming and Regulating Policies on the Control over Foreign Exchange Settlement of Capital Accounts (《關於改革和規範資本項目結匯管理政策的通知》), or Circular 16, which took effect on the same day. Compared to Circular 19, Circular 16 provides that discretionary foreign exchange settlement applies to foreign exchange capital, foreign debt offering proceeds and remitted foreign listing proceeds, and the corresponding Renminbi obtained from foreign exchange settlement are not restricted from extending loans to related parties or repaying the inter-company loans (including advances by third parties). However, there still exist substantial uncertainties with respect to the interpretation and implementation of Circular 16 in practice.

In November 2012, SAFE promulgated the Circular of Further Improving and Adjusting Foreign Exchange Administration Policies on Direct Investment (《關於進一步改進和調整直接投資外匯管理政策的通知》), as amended, which substantially amends and simplifies the foreign exchange procedure. Pursuant to this circular, the opening of various special purpose foreign exchange accounts, such as pre-establishment expenses accounts, foreign exchange capital accounts and guarantee accounts, the reinvestment of RMB proceeds by foreign investors in the PRC, and remittance of foreign exchange profits and dividends by a foreign-invested enterprise to its foreign shareholders no longer require the approval or verification of SAFE, and multiple capital accounts for the same entity may be opened in different provinces, which was not possible previously. In addition, SAFE promulgated the Circular on Printing and Distributing the Provisions on Foreign Exchange Administration over Domestic Direct Investment by Foreign Investors and the Supporting Documents (《關於印發〈外國投資者境內直接投資外匯管理規定〉及配套文件的通知》) in May 2013, as amended, which specifies that the administration by SAFE or its local branches over direct investment by foreign investors in the PRC shall be conducted by way of registration and banks shall process foreign exchange business relating to the direct investment in the PRC based on the registration information provided by SAFE and its branches.

After a Notice on Further Simplifying and Improving Foreign Exchange Administration Policy on Direct Investment (《關於進一步簡化和改進直接投資外匯管理政策的通知》), or SAFE Notice 13, became effective on June 1, 2015, instead of applying for approvals regarding foreign exchange registrations of foreign direct investment and overseas direct investment from SAFE, entities and individuals will be required to apply for such foreign exchange registrations from qualified banks. The qualified banks, under the supervision of SAFE, directly examine the applications and conduct the registration.

On October 23, 2019, SAFE issued the Circular on Further Promoting Cross-border Trade and Investment Facilitation (《關於進一步促進跨境貿易投資便利化的通知》), or SAFE Circular 28. Among others, SAFE Circular 28 relaxes the prior restrictions and allows the foreign-invested enterprises without equity investment as in their approved business scope to use their capital obtained from foreign exchange settlement to make domestic equity investment as long as the investments are real and in compliance with the foreign investment-related laws and regulations. In addition, SAFE Circular 28 stipulates that qualified enterprises in certain pilot areas may use their capital income from registered capital, foreign debt and overseas listing, for the purpose of domestic payments without providing

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authenticity certifications to the relevant banks in advance for those domestic payments. Payments for transactions that take place within the PRC must be made in RMB. Foreign currency revenues received by PRC companies may be repatriated into the PRC or retained outside of the PRC in accordance with requirements and terms specified by SAFE.

Dividend Distribution

Wholly foreign-owned enterprises and Sino-foreign equity joint ventures in the PRC may pay dividends only out of their accumulated profits, if any, as determined in accordance with PRC accounting standards and regulations. Additionally, these foreign-invested enterprises may not pay dividends unless they set aside at least 10% of their respective accumulated profits after tax each year, if any, to fund certain reserve funds, until such time as the accumulative amount of such fund reaches 50% of the enterprise’s registered capital. In addition, these companies also may allocate a portion of their after-tax profits based on PRC accounting standards to employee welfare and bonus funds at their discretion. These reserves are not distributable as cash dividends.

Regulations governing abovementioned dividend distribution arrangements have been replaced by the Foreign Investment Law and its implantation rules, which do not provide specific dividend distribution rules for foreign invested enterprises. However, the Foreign Investment Law and its implementation rules provide that after the conversion from a wholly foreign-owned enterprise or sino-foreign equity joint venture to a foreign invested enterprise under the Foreign Investment Law, distribution method of gains agreed in the joint venture agreements may continue to apply.

Foreign Exchange Registration of Offshore Investment by PRC Residents

Pursuant to SAFE’s Notice on Relevant Issues Concerning Foreign Exchange Administration for PRC Residents to Engage in Financing and Inbound Investment via Overseas Special Purpose Vehicles (《關於境內居民通過境外特殊目的公司融資及返程投資外匯管理有關問題的通知》), or SAFE Circular No. 75, issued in October 2005, and a series of implementation rules and guidance, including the circular relating to operating procedures that came into effect in July 2011 (《關於印發境內居民通過境外特殊目的公司融資及返程投資外匯管理操作規程的通知》), PRC residents, including PRC resident natural persons or PRC companies, must register with local branches of SAFE in connection with their direct or indirect offshore investment in an overseas special purpose vehicle, or SPV, for the purposes of overseas equity financing activities, and to update such registration in the event of any significant changes with respect to that offshore company. SAFE promulgated the Circular on Relevant Issues Concerning Foreign Exchange Control on Domestic Residents’ Offshore Investment and Financing and Roundtrip Investment through Special Purpose Vehicles (《關於境內居民通過特殊目的公司境外投資及返程投資外匯管理有關問題的通知》), or SAFE Circular No. 37, on July 4, 2014, which replaced SAFE Circular No. 75. SAFE Circular No. 37 requires PRC residents to register with local branches of SAFE in connection with their direct establishment or indirect control of an offshore entity, for the purpose of overseas investment and financing, with such PRC residents’ legally owned assets or equity interests in domestic enterprises or offshore assets or interests, referred to in SAFE Circular No. 37 as a “special purpose vehicle.” The term “control” under SAFE Circular No. 37 is broadly defined as the operation rights, beneficiary rights or decision-making rights acquired by the PRC residents in the offshore special purpose vehicles or PRC companies by such means as acquisition, trust, proxy, voting rights, repurchase, convertible bonds or other arrangements. SAFE Circular No. 37 further requires amendment to the registration in the event of any changes with respect to the basic information of the special purpose vehicle, such as changes in a PRC resident individual shareholder, name or operation period; or any significant changes with respect to the special purpose vehicle, such as an increase or decrease of capital contributed by PRC individuals, a share transfer or exchange, merger, division or

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other material event. If the shareholders of the offshore holding company who are PRC residents do not complete their registration with the local SAFE branches, the PRC subsidiaries may be prohibited from distributing their profits and proceeds from any reduction in capital, share transfer or liquidation to the offshore company, and the offshore company may be restricted in its ability to contribute additional capital to its PRC subsidiaries. Moreover, failure to comply with the SAFE registration and amendment requirements described above could result in liability under PRC law for evasion of applicable foreign exchange restrictions. After SAFE Notice 13 became effective on June 1, 2015, entities and individuals are required to apply for foreign exchange registration of foreign direct investment and overseas direct investment, including those required under SAFE Circular No. 37, with qualified banks, instead of SAFE. The qualified banks, under the supervision of SAFE, directly examine the applications and conduct the registration.

Under the Administration Measures on Individual Foreign Exchange Control (《個人外匯管理辦法》) issued by the People’s Bank of China, or the PBOC, in December 2006 and its implementation rules issued in January 2007 and revised in May 2016, all foreign exchange matters involved in employee share ownership plans and share option plans in which PRC citizens participate require approval from SAFE or its authorized branch. In February 2012, SAFE promulgated the Notices on Issues Concerning the Foreign Exchange Administration for Domestic Individuals Participating in Stock Incentive Plans of Overseas Publicly-Listed Companies (《關於境內個人參與境外上市公司股權激勵計劃外匯管理有關問題的通知》), or the Stock Option Rule, replacing the earlier rules promulgated in March 2007. Under the Stock Option Rule, PRC residents who are granted stock options by an overseas publicly listed company are required, through a PRC agent or PRC subsidiary of such overseas publicly listed company, to register with SAFE and complete certain other procedures. Failure of the option holders to complete their SAFE registrations may subject these PRC employees to fines and legal sanctions and may also limit the ability of the overseas publicly listed company to contribute additional capital into its PRC subsidiary and limit the PRC subsidiary’s ability to distribute dividends.

Regulations on Labor

The Labor Contract Law of the PRC (《中華人民共和國勞動合同法》, the “**Labor Contract Law**”), which became effective in January 2008 and last amended in December 2012, and its implementation rules, impose more restrictions on employers and have been deemed to increase labor costs for employers, compared to the Labor Law of the PRC (《中華人民共和國勞動法》, the “**Labor Law**”), which became effective in January 1995. For example, pursuant to the Labor Contract Law, an employer is obliged to sign a labor contract with an unlimited term with an employee if the employer continues to hire the employee after the expiration of two consecutive fixed-term labor contracts. The employer has to compensate the employee upon the expiration of a fixed-term labor contract, unless the employee refuses to renew such contract on terms the same as or more favorable to the employee than those contained in the expired contract. The employer also has to indemnify an employee if the employer terminates a labor contract without a cause permitted by law. In addition, under the Regulations on Paid Annual Leave for Employees (《職工帶薪年休假條例》), which became effective in January 2008, employees who have served more than one year for an employer are entitled to a paid vacation ranging from 5 to 15 days per year, depending on their length of service. Employees who waive such vacation time at the request of employers must be compensated for three times their regular salaries for each waived vacation day.

In addition, according to the PRC Social Insurance Law (《中華人民共和國社會保險法》) and the Regulations on the Administration of Housing Provident Funds (《住房公積金管理條例》), employers in China must provide employees with welfare schemes covering pension insurance, unemployment

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insurance, maternity insurance, work-related injury insurance, medical insurance and housing provident funds.

Regulations on Taxation

Enterprise Income Tax

Effective from January 1, 2008 and last amended on December 29, 2018, the PRC’s statutory enterprise income tax, or EIT, rate is 25%. An enterprise may benefit from a preferential tax rate of 15% under the PRC Enterprise Income Tax Law (《中華人民共和國企業所得稅法》), the “**EIT Law**”) if it qualifies as a “High and New Technology Enterprise” strongly supported by the state. Pursuant to the Administrative Measures on the Recognition of High and New Technology Enterprises (《高新技術企業認定管理辦法》), the “**Recognition Measures**”), as amended in January 2016, the provincial counterparts of the Ministry of Science and Technology, the Ministry of Finance and the State Administration of Taxation make joint determination on whether an enterprise is qualified as a “High and New Technology Enterprise” under the EIT Law. In making such determination, these government agencies consider, among other factors, ownership of core technology, whether the key technology supporting the core products or services falls within the scope of high and new technology strongly supported by the state as specified in the Recognition Measures, the ratios of research and development personnel to total personnel, the ratio of research and development expenditures to annual sales revenues, the ratio of revenues attributed to high and new technology products or services to total revenues, and other measures set forth in relevant guidance. A “High and New Technology Enterprise” certificate is effective for a period of three years.

An enterprise may benefit from a preferential tax rate of 10% under the EIT law if it qualifies as a “Key Software Enterprise”. Enterprises wishing to enjoy the “Key Software Enterprise” status will be subject to relevant governmental authorities’ assessment each year as to whether they are entitled to the preferential tax rate of 10%. Prior to May 2016, a “Key Software Enterprise” used to be designated jointly by the NDRC, the MIIT, the MOFCOM, the Ministry of Finance and the State Administration of Taxation. In May 2016, the four PRC governmental authorities jointly issued a notice, pursuant to which an enterprise may be entitled to the preferential income tax rate of 10% by filing with the local tax authority with supporting documentation proving its qualifications to be a “Key Software Enterprise” during its annual income tax filing process. In December 2020, the Ministry of Finance, the State Administration of Taxation, the NDRC, and the MIIT jointly issued a circular which has repealed the original preferential tax treatment applicable to the “Key Software Enterprise.” Such circular provides that the Key Software Enterprise’s EIT would be waived for five years since its first year of making profit and it may benefit from a preferential tax rate of 10% for the following years.

Withholding Tax

Under the EIT Law and its implementation rules, dividends, interests, rent or royalties payable by a foreign-invested enterprise to any of its non-resident enterprise investors, and proceeds from any such non-resident enterprise investor’s disposition of assets (after deducting the net value of such assets) are subject to the EIT at the rate of 10%, namely withholding tax, unless the non-resident enterprise investor’s jurisdiction of incorporation has a tax treaty or arrangement with the PRC that provides for a reduced withholding tax rate or an exemption from withholding tax. The Notice on Several Preferential Policies regarding Enterprise Income Tax Law (《關於企業所得稅若干優惠政策的通知》) jointly promulgated by the Ministry of Finance and State Administration of Taxation in February 2008, clarifies that undistributed profits earned by foreign-invested enterprises prior to January 1, 2008 will be exempted from any withholding tax.

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Hong Kong has a tax arrangement with PRC that provides for a lower withholding tax rate of 5% on dividends subject to certain conditions and requirements, such as the requirement that the Hong Kong resident enterprise own at least 25% of the PRC enterprise distributing the dividend at all times within the 12-month period immediately preceding the distribution of dividends and be a “beneficial owner” of the dividends. However, pursuant to Circular on Issues Concerning Implementing Dividend Clauses of Tax Treaties (《關於執行稅收協定股息條款有關問題的通知》), or SAT Circular 81, issued by the State Administration of Taxation in February 2009, if the relevant PRC tax authorities determine, in their discretion, that a company benefits from the reduced withholding tax rate on dividends due to a structure or arrangement designed for the primary purpose of obtaining favorable tax treatment, the PRC tax authorities may adjust the preferential tax treatment. Moreover, pursuant to Circular on Several Issues regarding the “Beneficial Owner” in Tax Treaties (《關於稅收協定中“受益所有人”有關問題的公告》), or SAT Circular 9, issued by the State Administration of Taxation in February 2018, which became effective from April 1, 2018 and superseded the SAT Circular 601 issued by the State Administration of Taxation in October 2009, a resident of a contracting state will not qualify for the benefits under the tax treaties or arrangements, if it is not the “beneficial owner” of the dividend, interest and royalty income. According to SAT Circular 9, a “beneficial owner” is required to have ownership and the right to dispose of the income or the rights and properties giving rise to the income, and generally engage in substantive business activities. An agent or conduit company will not be regarded as a “beneficial owner” and, therefore, will not qualify for treaty benefits. A conduit company normally refers to a company that is set up primarily for the purpose of evading or reducing taxes or transferring or accumulating profits. In addition, pursuant to Bulletin on Administrative Measures on Treaties Benefit for Non-resident Taxpayers (《非居民納稅人享受協定待遇管理辦法》), or SAT Circular 35, issued by the State Administration of Taxation in October 2019, non-resident enterprises are not required to obtain pre-approval from the relevant tax authority in order to enjoy the reduced withholding tax rate. Instead, non-resident enterprises may, if they determine by self-assessment that the prescribed criteria to enjoy the tax treaty benefits are met, directly apply for the reduced withholding tax rate, and file necessary forms and supporting documents when performing tax filings, which will be subject to post-filing examinations by the relevant tax authorities.

Tax Residence

Under the EIT Law and its implementation rules, an enterprise established outside of the PRC with “de facto management body” within the PRC is considered a resident enterprise and will be subject to the EIT at the rate of 25% on its worldwide income. The term “de facto management body” refers to “the establishment that exercises substantial and overall management and control over the production, business, personnel, accounts and properties of an enterprise.”

Pursuant to SAT Circular 82, issued by the State Administration of Taxation in April 2009, an overseas registered enterprise controlled by a PRC company or a PRC company group will be classified as a “resident enterprise” with its “de facto management body” located within the PRC if the following requirements are satisfied: (i) the senior management and core management departments in charge of its daily operations are mainly located in the PRC; (ii) its financial and human resources decisions are subject to determination or approval by persons or bodies located in the PRC; (iii) its major assets, accounting books, company seals, and minutes and files of its board and shareholders’ meetings are located or kept in the PRC; and (iv) no less than half of the enterprise’s directors or senior management with voting rights reside in the PRC. The State Administration of Taxation issued additional rules to provide more guidance on the implementation of SAT Circular 82 in July 2011, and issued an amendment to SAT Circular 82 delegating the authority to its provincial branches to determine whether a Chinese-controlled overseas-incorporated enterprise should be considered a PRC resident enterprise, in January 2014. Although the SAT Circular 82, the additional guidance and its amendment only apply

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to overseas registered enterprises controlled by PRC enterprises and not those controlled by PRC individuals or foreigners, the determining criteria set forth in the circular may reflect the State Administration of Taxation’s general position on how the “de facto management body” test should be applied in determining the tax resident status of offshore enterprises, regardless of whether they are controlled by PRC enterprises, individuals or foreigners.

PRC VAT in Lieu of Business Tax

In November 2011, the Ministry of Finance and the State Administration of Taxation jointly issued two circulars setting forth the details of the pilot VAT reform program, which change the charge of sales tax from business tax to VAT for certain pilot industries. The VAT reform program initially applied only to the pilot industries in Shanghai, and was expanded to eight additional regions, including, among others, Beijing and Guangdong province, in 2012. In August 2013, the program was further expanded nationwide. In May 2016, the pilot program was extended to cover additional industry sectors such as construction, real estate, finance and consumer services.

PRC Urban Maintenance and Construction Tax and Education Surcharge

Any entity, foreign-invested or purely domestic, or individual that is subject to consumption tax, VAT and business tax is also required to pay PRC urban maintenance and construction tax. The rates of urban maintenance and construction tax are 7%, 5% or 1% of the amount of consumption tax, VAT and business tax actually paid depending on where the taxpayer is located. All entities and individuals who pay consumption tax, VAT and business tax are also required to pay education surcharge at a rate of 3%, and local education surcharges at a rate of 2%, of the amount of VAT, business tax and consumption tax actually paid.

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AUTHORIZED AND ISSUED SHARE CAPITAL

The following is a description of the authorized and issued share capital of our Company immediately prior to and upon the completion of the [REDACTED], assuming that the [REDACTED] becomes unconditional and the [REDACTED] are issued pursuant to the [REDACTED] and without taking into account any allotment and issuance of Class A ordinary shares upon exercise of the [REDACTED], the Shares to be issued pursuant to the Share Incentive Plans, including pursuant to the exercise of options or the vesting of share awards that have been or may be granted from time to time and any issuance or repurchase of the Shares and/or ADSs that we may make.

1. Share capital as at the Latest Practicable Date

(i) *Authorized share capital*

| Number | Description of Shares | Approximate aggregate nominal value of shares |
|----------------|-------------------------|---|
| 66,000,000,000 | Class A ordinary shares | US\$41,250 |
| 2,832,000,000 | Class B ordinary shares | US\$ 1,770 |
| 800,000,000 | Preferred shares | US\$ 500 |
| Total | | US\$43,520 |

(ii) *Issued, fully paid or credited to be fully paid*

| Number | Description of Shares | Approximate aggregate nominal value of shares |
|---------------|-------------------------|---|
| 2,173,941,029 | Class A ordinary shares | US\$1,358.71 |
| 559,900,320 | Class B ordinary shares | US\$ 349.94 |
| 0 | Preferred shares | US\$ 0 |
| Total | | US\$1,708.65 |

(iii) *Issued and outstanding**

| Number | Description of Shares | Approximate aggregate nominal value of shares |
|---------------|-------------------------|---|
| 2,125,123,424 | Class A ordinary shares | US\$1,328.20 |
| 559,900,320 | Class B ordinary shares | US\$ 349.94 |
| 0 | Preferred shares | US\$ 0 |
| Total | | US\$1,678.14 |

Note:

* Excluding the 48,817,605 Class A ordinary shares issued to our depository bank for bulk issuance of ADSs reserved for future issuances upon the exercise or vesting of awards granted under our Share Incentive Plans.

2. Share capital immediately following the completion of the [REDACTED]

(i) *Authorized share capital*

| Number | Description of Shares | Approximate aggregate nominal value of shares |
|----------------|-------------------------|---|
| 66,000,000,000 | Class A ordinary shares | US\$41,250 |
| 2,832,000,000 | Class B ordinary shares | US\$ 1,770 |
| 800,000,000 | Preferred shares | US\$ 500 |
| Total | | US\$43,520 |

SHARE CAPITAL

(ii) *Issued fully paid or credited to be fully paid*

| Number | Description of Shares | Approximate aggregate nominal value of shares |
|--------------|-------------------------|---|
| [REDACTED] | Class A ordinary shares | US\$[REDACTED] |
| [REDACTED] | Class B ordinary shares | US\$[REDACTED] |
| [REDACTED] | Preferred shares | US\$[REDACTED] |
| Total | | US\$[REDACTED] |

(ii) *Issued and outstanding**

| Number | Description of Shares | Approximate aggregate nominal value of shares |
|--------------|-------------------------|---|
| [REDACTED] | Class A ordinary shares | US\$[REDACTED] |
| [REDACTED] | Class B ordinary shares | US\$[REDACTED] |
| [REDACTED] | Preferred shares | US\$[REDACTED] |
| Total | | US\$[REDACTED] |

Note:

* Excluding the 48,817,605 Class A ordinary shares issued to our depositary bank for bulk issuance of ADSs reserved for future issuances upon the exercise or vesting of awards granted under our Share Incentive Plans.

WEIGHTED VOTING RIGHTS STRUCTURE

Under our weighted voting rights structure, our share capital comprises Class A ordinary shares and Class B ordinary shares. Each Class A ordinary share entitles the holder to exercise one vote, and each Class B ordinary share entitles the holder to exercise 10 votes, respectively, on all matters subject to the vote at general meetings of the Company.

Pursuant to the Articles, the directors of our board may, from time to time subject to their fiduciary duties to act in the best interests of the Company and for a proper purpose, cause the Company to issue preferred shares and determine, among others, their conversion rights, which may include conversion to Class A and/or Class B ordinary shares. Such rights are subject to the approval and discretion of the board.

For further details, see the summary of the Articles of Association in Appendix III to this document.

The table below sets out the ownership and voting rights to be held by the WVR beneficiaries upon the completion of the [REDACTED]:

| | Number of Shares | Approximate percentage of issued and outstanding share capital ⁽¹⁾ | Approximate percentage of voting rights ⁽¹⁾⁽²⁾ |
|---|------------------|---|---|
| Class A ordinary shares held by the WVR beneficiaries . . . | [22,901,040] | [REDACTED]% | [REDACTED]% |
| Class B ordinary shares held by the WVR beneficiaries . . . | [559,900,320] | [REDACTED]% | [REDACTED]% |
| Total | [582,801,360] | [REDACTED]% | [REDACTED]% |

Notes:

(1) Excluding the [48,817,605] Class A ordinary shares issued to our depositary bank for bulk issuance of ADSs reserved for future issuances upon the exercise or vesting of awards granted under our Share Incentive Plans, and without taking into account any allotment and issuance of Shares upon exercise of the [REDACTED], the Shares to be issued pursuant to the Share Incentive Plans, including pursuant to the exercise of options or other awards that have been or may be granted from time to time and any issuance or repurchase of Shares and/or ADSs that we may make.

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- (2) On the basis that Class A ordinary shares entitle the Shareholder to one vote per share and Class B ordinary shares entitle the Shareholder to 10 votes per share.

Each Class B ordinary share is convertible into one Class A ordinary share at any time by the holder thereof. Upon the conversion of all the issued and outstanding Class B ordinary shares into Class A ordinary shares, the Company will issue 559,900,320 Class A ordinary shares, representing approximately [REDACTED] the total number of issued and outstanding Class A ordinary shares (without taking into account any allotment and issuance of Shares upon exercise of the [REDACTED], the Shares to be issued pursuant to the Share Incentive Plans, including pursuant to the exercise of options or the vesting of share awards that have been or may be granted from time to time and any issuance or repurchase of Shares and/or ADSs that we may make).

Each Class B ordinary share is convertible into one Class A ordinary share at any time by the holder thereof. If at any time Robin Yanhong Li and his Affiliates (as defined in the Articles of Association) collectively own less than 5% of the total number of the issued and outstanding Class B Ordinary Shares, each issued and outstanding Class B Ordinary Share shall be automatically and immediately converted into one Class A ordinary share, and no Class B Ordinary Shares shall be issued by the Company thereafter.

Class B ordinary shares shall also be automatically and immediately converted into an equal number of Class A ordinary shares:

- (1) upon any sale, pledge, transfer, assignment or disposition of such Class B ordinary shares by a holder thereto to any person or entity which is not an Affiliate (as defined in the Articles of Association) of such holder; or
- (2) where, within 6 months after by a transfer by a holder of Class B ordinary shares to an Affiliate of such holder, there is a change of the beneficial ownership of the Class B ordinary shares held by the Affiliate.

Apart from the aforementioned (1) and (2), a change in the beneficial ownership of Class B ordinary shares shall not cause a conversion of Class B ordinary shares to Class A ordinary shares.

WVR Beneficiaries

Immediately upon the completion of the [REDACTED], the WVR beneficiaries will be the following:

| | Number of Class A Ordinary Shares | Number of Class B Ordinary Shares | Approximate percentage of voting rights |
|--|--|--|---|
| Robin Yanhong Li | 18,291,280 | 439,200,000 | [REDACTED]% |
| Melissa Ma | 609,760 | 116,600,000 | [REDACTED]% |
| Shimoda Holdings, LLC ⁽¹⁾ | 4,000,000 | 4,000,000 | [REDACTED]% |
| Integrity Partners V, LLC ⁽²⁾ | 0 | 100,320 | [REDACTED]% |
| Total | 22,901,040 | 559,900,320 | [REDACTED]% |

Notes:

- (1) Shimoda Holdings, LLC (“Shimoda”) holds 500,000 ADSs and 4,000,000 Class B ordinary shares of the Company. Shimoda is affiliated with an early stage investor of the Company that invested in the Company before its US IPO in 2005.
- (2) Integrity Partners V, LLC (“Integrity”) holds 100,320 Class B ordinary shares of the Company was not a record shareholder of any Class A ordinary shares as at the Latest Practicable Date. Integrity is affiliated with an early stage investor of the Company that invested in the Company before its US IPO in 2005.

Mr. Robin Yanhong Li, the chairman and chief executive officer of the Company, owns shares in his personal capacity and through Handsome Reward Limited. Ms. Melissa Ma is the spouse of Mr. Li and

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holds shares in her personal capacity. To the best knowledge of the Company, Shimoda and Integrity and their respective ultimate beneficial owners are an independent third parties of and not core connected persons of the Company, and the ultimate beneficial owners of the Other WVR Beneficiaries do not have a role in the Company’s business and operations.

The Company’s WVR structure enables the WVR beneficiaries to hold shares with a higher voting power than the holders of Class A ordinary shares. Mr. Robin Yanhong Li, the chairman and chief executive officer of the Company, is the WVR beneficiary holding the highest percentage of voting rights; such shareholding will enable the Company to benefit from the continuing vision and leadership of Mr. Li, who will exercise his voting power with a view to the Company’s long-term prospects and strategy.

Prospective [REDACTED] are advised to be aware of the potential risks of [REDACTED] in companies with weighed voting rights structures, in particular that interests of the WVR beneficiaries may not necessarily always be aligned with those of our Shareholders as a whole, and that the WVR beneficiaries will be in a position to exercise their higher voting power to influence the affairs of our Company and the outcome of shareholders’ resolutions, irrespective of how other shareholders vote. Prospective [REDACTED] should make the decision to [REDACTED] in the Company only after due and careful consideration. For further information about the risks associated with the WVR structure adopted by the Company, please refer to “Risk Factors—Risks related to our Shares, our ADSs and the Listing”.

Save for the weighted voting rights attached to Class B ordinary shares, the rights attached to all classes of Shares are identical. For further information about the rights, preferences, privileges and restrictions of the Class A ordinary shares and Class B ordinary shares, please see “Summary of our Constitution and Cayman Companies Act—Articles of Association” in Appendix III to this document for further details.

Assumptions

The above table assumes that the [REDACTED] becomes unconditional and the Class A ordinary shares are issued pursuant to the [REDACTED]. The above does not take into account any Shares which may be issued or repurchased by us.

Ranking

The Shares are ordinary shares in the issued share capital of our Company and rank equally with all Shares currently in issue or to be issued and, in particular, will rank in full for all dividends or other distributions declared, made or paid on the Shares in respect of a record date which falls after the date of this document.

Share Repurchases

On June 26, 2018, our board of directors authorized a share repurchase program, under which we may repurchase up to US\$1.0 billion of our ADSs or ordinary shares over 12 months from June 27, 2018 through June 26, 2019. The share repurchase program was publicly announced on June 27, 2018.

On May 16, 2019, our board of directors authorized a new share repurchase program, under which we may repurchase up to US\$1.0 billion of our ADSs or ordinary shares, effective until July 1, 2020. The share repurchase program was publicly announced on May 16, 2019.

SHARE CAPITAL

The table below is a summary of the shares repurchased by us in 2019. All shares were repurchased in the open market pursuant to these share repurchase programs.

| <u>Period</u> | <u>(a) Total Number of ADSs Purchased</u> | <u>(b) Average Price Paid per ADS (US\$)</u> | <u>(c) Total Number of ADSs Purchased as Part of Publicly Announced Plans</u> | <u>(d) Approximate Dollar Value of ADSs that May Yet Be Purchased Under the Plans (US\$)</u> |
|---|---|--|---|--|
| May 1, 2019 to May 31, 2019 | 2,591,417 | 112.15 | 2,591,417 | 709,379,925 |
| August 1, 2019 to August 31, 2019 | 2,582,880 | 104.28 | 2,582,880 | 440,045,461 |
| October 1, 2019 to October 31, 2019 . . . | 1,277,274 | 99.61 | 1,277,274 | 312,814,075 |
| December 1, 2019 to December 31, 2019 | <u>193,767</u> | 114.92 | <u>193,767</u> | 290,546,496 |
| Total | <u>6,645,338</u> | 106.76 | <u>6,645,338</u> | 290,546,496 |

On May 13, 2020, our board of directors authorized a share repurchase program, under which we may repurchase up to US\$1.0 billion of our ADSs or shares, effective until July 1, 2021. On August 6, 2020, our board of directors approved a change to the 2020 share repurchase program, increasing the repurchase authorization from US\$1 billion to US\$3 billion and extending the effective time through December 31, 2022. In December 2020, our board of directors approved a further increase in the repurchase authorization from US\$3.0 billion to US\$4.5 billion. The source of funding for our share repurchase program is our offshore cash and primarily from our direct offshore debt financing.

The table below is a summary of the shares repurchased by us in 2020. All shares were repurchased in the open market pursuant to these share repurchase programs.

| <u>Period</u> | <u>Total Number of ADSs Purchased</u> | <u>Average Price Paid Per ADS</u> | <u>Total Number of ADSs Purchased as Part of the Publicly Announced Plan</u> | <u>Approximate Dollar Value of ADSs that May Yet Be Purchased Under the Plan</u> |
|--|---------------------------------------|-----------------------------------|--|--|
| February 1 – February 28, 2020 | 400 | US\$114.98 | 400 | US\$ 290,500,506 |
| March 1 – March 31, 2020 | 1,827,789 | US\$101.01 | 1,827,789 | US\$ 105,867,731 |
| May 13 – May 31, 2020 | 5,022,715 | US\$107.50 | 5,022,715 | US\$4,065,927,328 |
| August 1 – August 31, 2020 | 3,812,255 | US\$125.05 | 3,812,255 | US\$3,483,326,261 |
| September 1 – September 30, 2020 | 976,584 | US\$122.33 | 976,584 | US\$3,363,860,520 |
| October 1 – October 31, 2020 | 37,987 | US\$123.00 | 37,987 | US\$3,359,188,267 |
| November 1 – November 30, 2020 | 1,419,289 | US\$137.80 | 1,419,289 | US\$3,163,615,488 |
| December 1 – December 31, 2020 | <u>2,664,972</u> | US\$143.06 | <u>2,664,972</u> | US\$2,782,363,579 |
| Total | <u>15,761,991</u> | US\$120.69 | <u>15,761,991</u> | US\$2,782,363,579 |

USE OF [REDACTED]

We estimate that we will receive [REDACTED] from the [REDACTED] of approximately HK\$[REDACTED] billion after deducting estimated [REDACTED] fees and the estimated [REDACTED] payable by us and based upon an indicative [REDACTED] of HK\$[REDACTED] per [REDACTED] for both [REDACTED] and [REDACTED], and assuming the [REDACTED] is not exercised, or approximately HK\$[REDACTED] billion if the [REDACTED] is exercised in full.

The [REDACTED] in the [REDACTED] may be higher than, or the same as, the [REDACTED] in the [REDACTED]. See “Structure of the [REDACTED]—[REDACTED].”

We plan to use the [REDACTED] we will receive from the [REDACTED] for the following purposes:

- **approximately [REDACTED] (approximately HK\$[REDACTED], assuming that the [REDACTED] is not exercised) for continuing to invest in technology and enhance commercialization of our innovations centered around AI, including to:**
 - Attract and retain talents, in particular artificial intelligence and software engineers, data scientists, as well as other research and development staff, in order to improve our AI capabilities including but not limited to natural language processing, knowledge graph, speech recognition and synthesis, computer vision;
 - Strengthen the commercialization of AI cloud solutions and expand our portfolio of industry-specific AI cloud solutions by developing more AI capabilities, increasing cross-selling opportunities of various solutions to existing customers, acquiring new customers across industry verticals, and growing computing, storage, network, database and delivery capabilities;
 - Enhance the development and commercialization of intelligent driving and other growth initiatives, and continue to explore new and innovative application and monetization initiatives for our AI technology. For instance, we will continue to grow the accumulated test miles and improve simulation models with data from real world to increase the accuracy and effectiveness of our solutions to further enhance our L3 and L4 self-driving technology and to work with more automakers to power more passenger vehicles. We plan to invest in research and development of intelligent electric vehicles to achieve the mass production. We will also grow our fleet size of Apollo Robotaxi, obtain more driving licenses and expand geographic reach;
 - Invest in AI chips and scale IT infrastructure, including but not limited to investing more resources in chips design, procuring more servers and network equipment, and purchasing more cloud computing bandwidth, that collectively help optimize Baidu Brain and enhance our technology capabilities, as well as to improve the capacity of our operational flows and our external service capabilities; and
 - Selectively pursue suitable strategic partnerships, alliances, acquisitions and investments that have synergies with our business, such as those leveraging our AI capabilities, and our large user base to complement our organic growth. As of the Latest Practicable Date, we have not identified any other target of potential acquisition.

USE OF [REDACTED]

- **approximately [REDACTED] (approximately [REDACTED], assuming that the [REDACTED] is not exercised) for further growing Baidu Mobile Ecosystem and enhancing and diversifying monetization, including to:**
 - Continue improving functionalities and features of our mobile ecosystem to enhance our user engagement. For example, we will continue to improve Baidu App functionalities, and enhance the three AI building blocks—Baijiahao (BJH) Accounts, Smart Mini Program and Managed Page to improve overall mobile ecosystem;
 - Continue investing in and purchasing more dynamic and diversified content and service offerings to build a closed-loop content and service ecosystem, and optimize the AI building blocks for third-party content by attracting more content and service providers and users, as well as acquiring more licensed content. We will incentivize and attract more premium content creators to create high-quality content at our platform in a variety of formats such as short video and live streaming, as well as enrich the comprehensiveness of the content library of our knowledge and information products, such as Baidu Wiki, Baidu Knows;
 - Further expand user reach through branding and marketing activities, such as conducting targeted and precise marketing and promotional campaigns driven by insights into user preferences in the form of app store advertisements and collaborations with targeted brand. We will also continuously invest in product development to launch more products and services to meet our users’ evolving needs; and
 - Further strengthen our vertical and community offerings to provide superior experience to users, merchants and content providers. We will continue to improve the effectiveness of our online marketing services with our AI technology, and plan to further diversify monetization channels of our mobile ecosystem. In addition to growing our mobile ecosystem organically, we also plan to selectively pursue suitable strategic partnerships, alliances, acquisitions and investments.
- **approximately [REDACTED] (approximately [REDACTED], assuming that the [REDACTED] is not exercised) for general corporate purposes.** We will use the remaining [REDACTED] for working capital and general corporate purposes to support our business operation and growth.

To the extent that the [REDACTED] of the [REDACTED] are not immediately required for the above purposes or if we are unable to put into effect any part of our plan as intended, we may hold such unused [REDACTED] in cash or short term deposits at authorized financial institutions and/or licensed banks.

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

STRUCTURE OF THE [REDACTED]

[REDACTED]

STRUCTURE OF THE [REDACTED]

[REDACTED]

STRUCTURE OF THE [REDACTED]

[REDACTED]

STRUCTURE OF THE [REDACTED]

[REDACTED]

STRUCTURE OF THE [REDACTED]

[REDACTED]

STRUCTURE OF THE [REDACTED]

[REDACTED]

STRUCTURE OF THE [REDACTED]

[REDACTED]

STRUCTURE OF THE [REDACTED]

[REDACTED]

STRUCTURE OF THE [REDACTED]

[REDACTED]

HOW TO APPLY FOR [REDACTED]

[REDACTED]

HOW TO APPLY FOR [REDACTED]

[REDACTED]

HOW TO APPLY FOR [REDACTED]

[REDACTED]

HOW TO APPLY FOR [REDACTED]

[REDACTED]

THIS DOCUMENT IS IN DRAFT FORM, INCOMPLETE AND SUBJECT TO CHANGE AND THAT THE INFORMATION MUST BE READ IN CONJUNCTION WITH THE SECTION HEADED “WARNING” ON THE COVER OF THIS DOCUMENT

HOW TO APPLY FOR [REDACTED]

[REDACTED]

HOW TO APPLY FOR [REDACTED]

[REDACTED]

HOW TO APPLY FOR [REDACTED]

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[REDACTED]

HOW TO APPLY FOR [REDACTED]

[REDACTED]

HOW TO APPLY FOR [REDACTED]

[REDACTED]

HOW TO APPLY FOR [REDACTED]

[REDACTED]

The following is the text of a report set out on pages [IA-1 to IA-2], received from the Company’s reporting accountants, Ernst & Young, Certified Public Accountants, Hong Kong, for the purpose of incorporation in this [REDACTED]. It is prepared and addressed to the directors of the Company and to the Joint Sponsors pursuant to the requirements of HKSIR 200, Accountants’ Reports on Historical Financial Information in Investment Circulars issued by the Hong Kong Institute of Certified Public Accountants.

22/F, CITIC Tower
1 Tim Mei Avenue
Central, Hong Kong

[●]

The Directors
Baidu, Inc.

Merrill Lynch (Asia Pacific) Limited
CLSA Capital Markets Limited
Goldman Sachs (Asia) L.L.C.

Dear Sirs,

We report on the historical financial information of Baidu, Inc. and its subsidiaries (together, the “Company”) set out on pages IA-3 to IA-98, which comprises the consolidated balance sheets of the Company as at December 31, 2018, 2019 and 2020, and the consolidated statements of comprehensive income (loss), the consolidated statements of cash flows and the consolidated statements of shareholders’ equity of the Company for each of the years ended December 31, 2018, 2019 and 2020 (the “Track Record Period”), and a summary of significant accounting policies and other explanatory information (together, the “Historical Financial Information”). The Historical Financial Information set out on pages IA-3 to IA-98 forms an integral part of this report, which has been prepared for inclusion in the [REDACTED] of the Company dated [●] (the [REDACTED]) in connection with the listing of the shares of the Company on the Main Board of The Stock Exchange of Hong Kong Limited (the “Stock Exchange”).

Directors’ responsibility for the Historical Financial Information

The directors of the Company are responsible for the preparation of the Historical Financial Information that gives a true and fair view in accordance with the basis of presentation set out in note 2.(a) to the Historical Financial Information, and for such internal control as the directors determine is necessary to enable the preparation of the Historical Financial Information that is free from material misstatement, whether due to fraud or error.

Reporting accountants’ responsibility

Our responsibility is to express an opinion on the Historical Financial Information and to report our opinion to you. We conducted our work in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 200, *Accountants’ Reports on Historical Financial Information in Investment Circulars* issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”). This standard requires that we comply with ethical standards and plan and perform our work to obtain

reasonable assurance about whether the Historical Financial Information is free from material misstatement.

Our work involved performing procedures to obtain evidence about the amounts and disclosures in the Historical Financial Information. The procedures selected depend on the reporting accountants’ judgment, including the assessment of risks of material misstatement of the Historical Financial Information, whether due to fraud or error. In making those risk assessments, the reporting accountants consider internal control relevant to the entity’s preparation of the Historical Financial Information that gives a true and fair view in accordance with the basis of presentation set out in note 2.(a) to the Historical Financial Information, in order to design procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal control. Our work also included evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the Historical Financial Information.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion

In our opinion, the Historical Financial Information gives, for the purposes of the accountants’ report, a true and fair view of the consolidated financial position of the Company as at December 31, 2018, 2019 and 2020 and of the consolidated financial performance and cash flows of the Company for each of the Track Record Period in accordance with the basis of presentation set out in note 2.(a) to the Historical Financial Information.

Report on matters under the Rules Governing the Listing of Securities on the Stock Exchange and the Companies (Winding Up and Miscellaneous Provisions) Ordinance

Adjustments

In preparing the Historical Financial Information, no adjustments to the Historical Financial Statements as defined on page IA-3 have been made.

Dividends

We refer to note 27 to the Historical Financial Information which states that no dividends have been paid by the Company in respect of the Track Record Period.

No historical financial statements for the Company

As at the date of this report, no statutory financial statements have been prepared for the Company since its date of incorporation.

Certified Public Accountants
Hong Kong

I HISTORICAL FINANCIAL INFORMATION

Preparation of Historical Financial Information

Set out below is the Historical Financial Information which forms an integral part of this accountants’ report.

[The Historical Financial Information in this report was prepared based on previously issued financial statements of the Company for the Track Record Period. The previously issued financial statements were audited by Ernst & Young Hua Ming LLP in accordance with the standards of the Public Company Accounting Oversight Board (United States) (“PCAOB”) (the “Historical Financial Statements”).]

The Historical Financial Information is presented in Renminbi (“RMB”) and all values are rounded to the nearest million except when otherwise indicated.

APPENDIX IA

ACCOUNTANTS’ REPORT

BAIDU, INC.

CONSOLIDATED BALANCE SHEETS

(Amounts in millions of Renminbi (“RMB”), and in millions of U.S. Dollars (“US\$”), except for number of shares and per share data)

| | Notes | As of December 31, | | | |
|---|-------|--------------------|----------------|----------------|----------------------------|
| | | 2018 RMB | 2019 RMB | 2020 RMB | 2020 US\$ Note 2.(a) |
| ASSETS | | | | | |
| Current assets: | | | | | |
| Cash and cash equivalents | | 27,638 | 33,443 | 35,782 | 5,484 |
| Restricted cash | | 2,189 | 996 | 758 | 117 |
| Short-term investments, net | 4 | 111,626 | 112,924 | 126,402 | 19,372 |
| Accounts receivable, net | 7 | 6,015 | 7,416 | 8,668 | 1,328 |
| Amounts due from related parties | 23 | 785 | 1,594 | 726 | 111 |
| Other current assets, net | 8 | 6,841 | 9,189 | 11,006 | 1,687 |
| Total current assets | | 155,094 | 165,562 | 183,342 | 28,099 |
| Non-current assets: | | | | | |
| Fixed assets, net | 9 | 17,903 | 18,311 | 17,508 | 2,683 |
| Licensed copyrights, net | 5 | 6,641 | 6,287 | 6,435 | 986 |
| Produced content, net | 6 | 3,736 | 4,355 | 6,556 | 1,005 |
| Intangible assets, net | 10 | 2,540 | 1,600 | 2,022 | 310 |
| Goodwill | 10 | 18,536 | 18,250 | 22,248 | 3,410 |
| Long-term investments, net | 4 | 80,454 | 69,410 | 76,233 | 11,683 |
| Amounts due from related parties | 23 | 4,297 | 3,564 | 3,438 | 527 |
| Deferred tax assets, net | 16 | 2,324 | 2,193 | 1,674 | 257 |
| Operating lease right-of-use assets | 15 | — | 7,332 | 9,804 | 1,503 |
| Other non-current assets | 8 | 6,041 | 4,452 | 3,448 | 527 |
| Total non-current assets | | 142,472 | 135,754 | 149,366 | 22,891 |
| Total assets | | 297,566 | 301,316 | 332,708 | 50,990 |
| LIABILITIES AND EQUITY | | | | | |
| Current liabilities (including amounts of the consolidated VIEs without recourse to the primary beneficiaries of RMB 18,812, RMB24,692 and RMB 25,051 (US\$3,839) as of December 31, 2018, 2019 and 2020, respectively): | | | | | |
| Short-term loans | 12 | 3,046 | 2,618 | 3,016 | 462 |
| Accounts payable and accrued liabilities | 11 | 35,381 | 32,701 | 36,716 | 5,627 |
| Customer deposits and deferred revenue | | 9,221 | 11,062 | 12,626 | 1,935 |
| Deferred income | | 523 | 529 | 158 | 24 |
| Long-term loans, current portion | 12 | 84 | 737 | 7,427 | 1,138 |
| Convertible senior notes, current portion | 14 | — | — | 4,752 | 728 |
| Notes payable, current portion | 13 | 6,871 | 5,219 | — | — |
| Amounts due to related parties | 23 | 1,727 | 2,231 | 1,324 | 203 |
| Operating lease liabilities | 15 | — | 2,283 | 2,366 | 364 |
| Total current liabilities | | 56,853 | 57,380 | 68,385 | 10,481 |

APPENDIX IA

ACCOUNTANTS’ REPORT

BAIDU, INC.

CONSOLIDATED BALANCE SHEETS—continued

(Amounts in millions of Renminbi (“RMB”), and in millions of U.S. Dollars (“US\$”), except for number of shares and per share data)

| | Notes | As of December 31, | | | |
|---|-------|--------------------|----------------|----------------|----------------------------|
| | | 2018 RMB | 2019 RMB | 2020 RMB | 2020 US\$ Note 2.(a) |
| Non-current liabilities (including amounts of the consolidated VIEs without recourse to the primary beneficiaries of RMB2,417, RMB6,295 and RMB 5,519 (US\$846) as of December 31, 2018, 2019 and 2020, respectively): | 1 | | | | |
| Deferred income | | 54 | 17 | 97 | 15 |
| Deferred revenue | | 1,309 | 1,009 | 686 | 105 |
| Amounts due to related parties | 23 | 4,360 | 3,846 | 3,543 | 543 |
| Long-term loans | 12 | 7,456 | 7,804 | — | — |
| Notes payable | 13 | 42,735 | 38,090 | 48,408 | 7,419 |
| Convertible senior notes | 14 | 4,712 | 12,297 | 11,927 | 1,828 |
| Deferred tax liabilities | 16 | 4,099 | 3,273 | 3,067 | 470 |
| Operating lease liabilities | 15 | — | 4,486 | 4,693 | 719 |
| Other non-current liabilities | | 236 | 299 | 59 | 9 |
| Total non-current liabilities | | 64,961 | 71,121 | 72,480 | 11,108 |
| Total liabilities | | 121,814 | 128,501 | 140,865 | 21,589 |
| Commitments and contingencies | 18 | | | | |
| Redeemable noncontrolling interests | 19 | 716 | 1,109 | 3,102 | 475 |
| Equity | | | | | |
| Class A Ordinary Shares, par value US\$0.000000625 per share, 66,000,000,000 shares authorized, and 2,218,695,360 shares, 2,190,529,680 shares and 2,107,228,720 shares issued and outstanding as at December 31, 2018, December 31, 2019 and December 31, 2020, respectively (<i>Note</i>) | 20 | — | — | — | — |
| Class B Ordinary Shares, par value US\$0.000000625 per share, 2,832,000,000 shares authorized, and 576,100,320 shares, 576,100,320 shares and 571,900,320 shares issued and outstanding as at December 31, 2018, December 31, 2019 and December 31, 2020, respectively (<i>Note</i>) | 20 | — | — | — | — |
| Additional paid-in capital | | 33,441 | 38,714 | 47,213 | 7,236 |
| Retained earnings | 20 | 129,246 | 126,268 | 135,284 | 20,733 |
| Accumulated other comprehensive (loss) income | 20 | 210 | (1,383) | 199 | 30 |
| Total Baidu, Inc. shareholders’ equity | | 162,897 | 163,599 | 182,696 | 27,999 |
| Noncontrolling interests | | 12,139 | 8,107 | 6,045 | 927 |
| Total equity | | 175,036 | 171,706 | 188,741 | 28,926 |
| Total liabilities, redeemable noncontrolling interests and equity | | 297,566 | 301,316 | 332,708 | 50,990 |

Note: Par value per share and the number of shares as of December 31, 2018, 2019 and 2020 have been retrospectively adjusted for the Share Subdivision that became effective on March 1, 2021 as detailed in Note 2.(a) and Note 21.

APPENDIX IA

ACCOUNTANTS’ REPORT

BAIDU, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(Amounts in millions of Renminbi (“RMB”), and in millions of U.S. Dollars (“US\$”), except for number of shares and per share (or ADS) data)

| | Notes | For the Years Ended December 31, | | | |
|--|-------|----------------------------------|----------------|----------------|--------------------|
| | | 2018 | 2019 | 2020 | 2020 |
| | | RMB | RMB | RMB | US\$ Note 2.(a) |
| Revenues: | | | | | |
| Online marketing services | | 81,912 | 78,093 | 72,840 | 11,163 |
| Others | | 20,365 | 29,320 | 34,234 | 5,247 |
| Total revenues | 24 | 102,277 | 107,413 | 107,074 | 16,410 |
| Operating costs and expenses: | | | | | |
| Cost of revenues | | 51,744 | 62,850 | 55,158 | 8,454 |
| Selling, general and administrative | | 19,231 | 19,910 | 18,063 | 2,769 |
| Research and development | | 15,772 | 18,346 | 19,513 | 2,989 |
| Total operating costs and expenses | | 86,747 | 101,106 | 92,734 | 14,212 |
| Operating profit | | 15,530 | 6,307 | 14,340 | 2,198 |
| Other income (loss): | | | | | |
| Interest income | | 4,451 | 6,060 | 5,358 | 822 |
| Interest expense | | (1,883) | (2,960) | (3,103) | (476) |
| Foreign exchange loss, net | | (122) | (33) | (660) | (101) |
| Loss from equity method investments | 4 | (79) | (1,254) | (2,248) | (345) |
| Others, net | 4 | 9,428 | (8,460) | 9,403 | 1,441 |
| Total other income (loss), net | | 11,795 | (6,647) | 8,750 | 1,341 |
| Income (loss) before income taxes | | 27,325 | (340) | 23,090 | 3,539 |
| Income taxes | 16 | 4,743 | 1,948 | 4,064 | 623 |
| Net income (loss) | | 22,582 | (2,288) | 19,026 | 2,916 |
| Less: net loss attributable to noncontrolling interests | | (4,991) | (4,345) | (3,446) | (528) |
| Net income attributable to Baidu, Inc. | | 27,573 | 2,057 | 22,472 | 3,444 |
| Earnings per share for Class A and Class B ordinary shares (Note): | 21 | | | | |
| Basic | | 9.83 | 0.71 | 8.19 | 1.26 |
| Diluted | | 9.75 | 0.70 | 8.12 | 1.24 |
| Earnings per ADS (1 ADS equals 8 Class A ordinary shares) (Note): | 21 | | | | |
| Basic | | 78.64 | 5.68 | 65.54 | 10.04 |
| Diluted | | 78.03 | 5.60 | 64.98 | 9.96 |
| Weighted average number of Class A and Class B ordinary shares outstanding (in millions) (Note): | | | | | |
| Basic | | 2,792 | 2,787 | 2,732 | 2,732 |
| Diluted | | 2,814 | 2,791 | 2,756 | 2,756 |
| Other comprehensive income (loss): | 20 | | | | |
| Foreign currency translation adjustments | | 194 | (782) | 1,936 | 296 |
| Unrealized gains (losses) on available-for-sale investments, net of reclassification | | 92 | (708) | (161) | (25) |
| Other comprehensive income (loss), net of tax | | 286 | (1,490) | 1,775 | 271 |
| Comprehensive income (loss) | | 22,868 | (3,778) | 20,801 | 3,187 |
| Less: comprehensive loss attributable to noncontrolling interests and redeemable noncontrolling interests | | (3,985) | (4,242) | (3,253) | (499) |
| Comprehensive income attributable to Baidu, Inc. | | 26,853 | 464 | 24,054 | 3,686 |

Note: Basic and diluted earnings per share and the number of shares for the years ended December 31, 2018, 2019 and 2020 have been retrospectively adjusted for the Share Subdivision that became effective on March 1, 2021 as detailed in Note 2.(a) and Note 21.

APPENDIX IA

ACCOUNTANTS’ REPORT

BAIDU, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in millions of Renminbi (“RMB”), and in millions of U.S. Dollars (“US\$”))

| | For the Years Ended December 31, | | | |
|---|----------------------------------|-----------------|-----------------|--------------------|
| | 2018 | 2019 | 2020 | 2020 |
| | RMB | RMB | RMB | US\$ Note 2.(a) |
| Cash flows from operating activities: | | | | |
| Net income (loss) | 22,582 | (2,288) | 19,026 | 2,916 |
| Adjustments to reconcile net income (loss) to net cash generated from operating activities: | | | | |
| Depreciation of fixed assets and computer parts | 3,730 | 5,615 | 5,772 | 885 |
| Amortization of intangible assets | 385 | 661 | 544 | 83 |
| Deferred income tax, net | (761) | (696) | 115 | 17 |
| Share-based compensation | 4,676 | 5,626 | 6,728 | 1,031 |
| Allowance for credit losses | 451 | 429 | 679 | 104 |
| Investment and interest income | (7,648) | (2,305) | (11,966) | (1,833) |
| Amortization and impairment of licensed copyrights | 12,253 | 12,885 | 11,864 | 1,818 |
| Amortization and impairment of produced content | 2,266 | 2,977 | 4,534 | 695 |
| Impairment of other assets | 1,208 | 10,714 | 2,928 | 449 |
| Share of losses from equity method investments | 79 | 1,254 | 2,248 | 345 |
| (Gain)/loss on disposal of subsidiaries | (5,525) | 578 | — | — |
| Barter transaction revenue | (1,083) | (683) | (1,376) | (211) |
| Accretion on convertible senior notes and asset-backed debt securities | 25 | 380 | 501 | 77 |
| Other non-cash expenses | 99 | 76 | 739 | 113 |
| Others | (51) | (78) | 71 | 10 |
| Changes in operating assets and liabilities, net of effects of | | | | |
| Accounts receivable | (1,611) | (1,779) | (1,660) | (254) |
| Amounts due from related parties | 527 | (135) | 125 | 19 |
| Licensed copyrights | — | — | (10,528) | (1,613) |
| Produced content | (4,545) | (3,596) | (6,728) | (1,031) |
| Other assets | 3,212 | (863) | (351) | (54) |
| Customer deposits and deferred revenue | 912 | 1,515 | 1,177 | 180 |
| Accounts payable and accrued liabilities | 4,094 | (1,653) | 208 | 32 |
| Deferred income | (64) | (37) | (293) | (45) |
| Amounts due to related parties | 756 | (139) | (157) | (24) |
| Net cash generated from operating activities | 35,967 | 28,458 | 24,200 | 3,709 |
| Cash flows from investing activities: | | | | |
| Acquisition of fixed assets | (8,772) | (6,428) | (5,084) | (779) |
| Acquisition of businesses, net of cash acquired | (1,978) | (969) | (2,396) | (367) |
| Acquisition of licensed copyrights | (13,116) | (12,152) | — | — |
| Acquisition of intangible assets | (385) | (541) | (247) | (38) |
| Purchases of held-to-maturity investments | (27,640) | (120,189) | (159,197) | (24,399) |
| Maturities of held-to-maturity investments | 49,040 | 46,563 | 134,299 | 20,582 |
| Purchases of available-for-sale investments | (284,149) | (218,171) | (133,008) | (20,384) |
| Sales and maturities of available-for-sale investments | 239,861 | 291,163 | 135,606 | 20,783 |
| Purchases of other long-term investments | (9,891) | (6,322) | (4,467) | (685) |
| Proceeds from disposal of long-term investments | 2,524 | 7,517 | 6,523 | 1,000 |
| Disposal of subsidiaries’ shares | 5,581 | (476) | (486) | (74) |
| Loans provided to related parties | (8,632) | — | — | — |
| Repayment of loans provided to related parties | 12,270 | 24 | 917 | 140 |
| Micro loan origination and disbursement (Note) | (35,824) | — | — | — |
| Principal payments received on micro loans (Note) | 38,063 | — | — | — |
| Purchases of other invested securities (Note) | (16,362) | — | — | — |
| Sales and maturities of other invested securities (Note) | 24,949 | — | — | — |
| Other investing activities | 1 | 7 | (12) | (2) |
| Net cash used in investing activities | (34,460) | (19,974) | (27,552) | (4,223) |

Note: The financial services business (“Du Xiaoman”) was disposed in the year of 2018. Please see Note 4 for further information.

APPENDIX IA

ACCOUNTANTS’ REPORT

BAIDU, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS—continued

(Amounts in millions of Renminbi (“RMB”), and in millions of U.S. Dollars (“US\$”))

| | For the Years Ended December 31, | | | |
|--|----------------------------------|----------------|---------------|--------------------|
| | 2018 | 2019 | 2020 | 2020 |
| | RMB | RMB | RMB | US\$ Note 2.(a) |
| Cash flows from financing activities: | | | | |
| Proceeds from short-term loans | 3,787 | 2,738 | 3,559 | 545 |
| Repayments of short-term loans | (1,055) | (3,166) | (3,223) | (494) |
| Proceeds from long-term loans | 1,168 | 946 | — | — |
| Repayments of long-term loans | (98) | (168) | (709) | (109) |
| Loans borrowed from related parties | 3,732 | — | — | — |
| Repayment of loans borrowed from related parties | — | — | (356) | (55) |
| Proceeds from issuance of long-term notes, net of issuance costs | 18,050 | (10) | 13,346 | 2,046 |
| Repayment of long-term notes | (6,846) | (6,912) | (5,378) | (824) |
| Proceeds from issuance of convertible notes, net of issuance costs | 5,035 | 7,910 | 5,151 | 789 |
| Purchase of capped calls | (465) | (567) | — | — |
| Proceeds from issuance of subsidiaries’ shares | 15,689 | 401 | 4,662 | 715 |
| Repurchase of ordinary shares | (3,312) | (4,958) | (13,054) | (2,001) |
| Proceeds from exercise of share options | 676 | 18 | 228 | 35 |
| Proceeds from issuance of redeemable noncontrolling interests | — | — | 1,669 | 257 |
| Proceeds from third-party investors for sale of financial products (Note) | 15,143 | — | — | — |
| Repayment to third-party investors for sale of financial products (Note) | (33,376) | — | — | — |
| Proceeds from secured borrowings from third-party financial institutions (Note) | 10,380 | — | — | — |
| Repayment of secured borrowings from third-party financial institutions (Note) | (13,426) | — | — | — |
| Other financing activities | — | (105) | (230) | (35) |
| Net cash provided by (used in) financing activities | 15,082 | (3,873) | 5,665 | 869 |
| Effect of exchange rate changes on cash, cash equivalents and restricted cash | 1,902 | 1 | (212) | (32) |
| Net increase in cash, cash equivalents and restricted cash | 18,491 | 4,612 | 2,101 | 323 |
| Cash, cash equivalents and restricted cash at beginning of the year | 11,336 | 29,827 | 34,439 | 5,278 |
| Cash, cash equivalents and restricted cash at end of the year | 29,827 | 34,439 | 36,540 | 5,601 |
| Supplemental disclosures: | | | | |
| Interest paid | 1,579 | 2,448 | 2,204 | 338 |
| Income taxes paid | 5,509 | 4,100 | 3,608 | 553 |
| Non-cash investing and financing activities: | | | | |
| Acquisition of fixed assets included in accounts payable and accrued liabilities | 1,516 | 1,020 | 984 | 151 |
| Non-cash acquisitions of investments | 764 | 28 | 54 | 8 |

Note: The financial services business (“Du Xiaoman”) was disposed in the year of 2018. Please see Note 4 for further information.

APPENDIX IA

ACCOUNTANTS’ REPORT

BAIDU, INC.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS’ EQUITY

(Amounts in millions of Renminbi (“RMB”) except for number of shares)

| | Attributable to Baidu, Inc. | | | | | | |
|---|-----------------------------|--------|----------------------------|-------------------|---|--------------------------|----------------------------|
| | Ordinary shares | | Additional paid-in capital | Retained earnings | Accumulated other comprehensive income (loss) | Noncontrolling interests | Total shareholders’ equity |
| | Number of shares (Note) | Amount | | | | | |
| | | RMB | RMB | RMB | RMB | RMB | RMB |
| Balances at December 31, 2017 | 2,785,298,560 | — | 12,088 | 102,328 | 930 | 4,004 | 119,350 |
| Cumulative effect of accounting change | — | — | — | 2,787 | (1,854) | — | 933 |
| Net income | — | — | — | 27,573 | — | (4,991) | 22,582 |
| Other comprehensive income | — | — | — | — | 1,134 | 1,006 | 2,140 |
| Business combinations | — | — | 75 | — | — | 1,312 | 1,387 |
| Issuance of shares by the Company’s subsidiaries to noncontrolling interest | — | — | 14,984 | — | — | (733) | 14,251 |
| Exercise of share-based awards | 26,070,320 | — | 689 | — | — | — | 689 |
| Share-based compensation | — | — | 4,340 | — | — | 217 | 4,557 |
| Accretion of redeemable noncontrolling interests | — | — | — | (130) | — | (16) | (146) |
| Repurchase and retirement of ordinary shares | (16,573,200) | — | — | (3,312) | — | — | (3,312) |
| Disposal of subsidiaries’ shares | — | — | 1,323 | — | — | 235 | 1,558 |
| Conversion of iQIYI preferred shares recognized as redeemable noncontrolling interests to ordinary shares | — | — | — | — | — | 11,150 | 11,150 |
| Equity component of convertible senior notes issued by iQIYI, net of issuance costs | — | — | 206 | — | — | 156 | 362 |
| Purchase of capped calls | — | — | (264) | — | — | (201) | (465) |
| Balances at December 31, 2018 | 2,794,795,680 | — | 33,441 | 129,246 | 210 | 12,139 | 175,036 |
| Net income | — | — | — | 2,057 | — | (4,345) | (2,288) |
| Other comprehensive income | — | — | — | — | (1,593) | 103 | (1,490) |
| Business combinations | — | — | — | — | — | 266 | 266 |
| Acquisition of non-controlling interests in a subsidiary | — | — | (22) | — | — | (43) | (65) |
| Issuance of shares by the Company’s subsidiaries to noncontrolling interest | — | — | (19) | — | — | 325 | 306 |
| Exercise of share-based awards | 24,997,040 | — | 18 | — | — | — | 18 |
| Share-based compensation | — | — | 5,045 | — | — | 504 | 5,549 |
| Dividends paid and payable by the Company’s subsidiaries | — | — | — | — | — | (128) | (128) |
| Accretion of redeemable noncontrolling interests | — | — | — | (77) | — | (34) | (111) |
| Repurchase and retirement of ordinary shares | (53,162,720) | — | — | (4,958) | — | — | (4,958) |
| Disposal of subsidiaries’ shares | — | — | 13 | — | — | (863) | (850) |
| Equity component of convertible senior notes issued by iQIYI, net of issuance costs | — | — | 559 | — | — | 429 | 988 |
| Purchase of capped calls | — | — | (321) | — | — | (246) | (567) |
| Balances at December 31, 2019 | 2,766,630,000 | — | 38,714 | 126,268 | (1,383) | 8,107 | 171,706 |

APPENDIX IA

ACCOUNTANTS’ REPORT

BAIDU, INC.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS’ EQUITY—continued

(Amounts in millions of Renminbi (“RMB”) except for number of shares)

| | Attributable to Baidu, Inc. | | | | | | |
|---|-----------------------------|--------|----------------------------|-------------------|---|--------------------------|----------------------------|
| | Ordinary shares | | Additional paid-in capital | Retained earnings | Accumulated other comprehensive (loss) income | Noncontrolling interests | Total shareholders’ equity |
| | Number of shares (Note) | Amount | | | | | |
| | | RMB | RMB | RMB | RMB | RMB | RMB |
| Balances at December 31, 2019 | 2,766,630,000 | — | 38,714 | 126,268 | (1,383) | 8,107 | 171,706 |
| Cumulative effect of accounting change | — | — | — | (314) | — | (43) | (357) |
| Net income | — | — | — | 22,472 | — | (3,446) | 19,026 |
| Other comprehensive income | — | — | — | — | 1,582 | 193 | 1,775 |
| Business combinations | — | — | — | — | — | 798 | 798 |
| Issuance of shares by the Company’s subsidiaries to noncontrolling interest | — | — | 2,260 | — | — | 2,397 | 4,657 |
| Exercise of share-based awards | 38,595,040 | — | 302 | — | — | — | 302 |
| Share-based compensation | — | — | 5,749 | — | — | 645 | 6,394 |
| Dividends payable by the Company’s subsidiaries | — | — | — | — | — | (70) | (70) |
| Return of equity to noncontrolling interest shareholders | — | — | — | — | — | (2,704) | (2,704) |
| Accretion of redeemable noncontrolling interests | — | — | — | (88) | — | (39) | (127) |
| Repurchase and retirement of ordinary shares | (126,096,000) | — | — | (13,054) | — | — | (13,054) |
| Equity component of convertible senior notes issued by iQIYI, net of issuance costs | — | — | 208 | — | — | 187 | 395 |
| Others | — | — | (20) | — | — | 20 | — |
| Balances at December 31, 2020 | 2,679,129,040 | — | 47,213 | 135,284 | 199 | 6,045 | 188,741 |
| Balances at December 31, 2020, in | | | | | | | |
| US\$ | | | 7,236 | 20,733 | 30 | 927 | 28,926 |

Note: The number of shares has been retrospectively adjusted for the Share Subdivision that became effective on March 1, 2021 as detailed in Note 2.(a) and Note 21.

II NOTES TO HISTORICAL FINANCIAL INFORMATION

1. ORGANIZATION

Baidu, Inc. (“Baidu” or the “Company”) was incorporated under the laws of the Cayman Islands on January 18, 2000. The Company, its subsidiaries, variable interest entities (“VIEs”) and subsidiaries of the VIEs are hereinafter collectively referred to as the “Group”.

As of December 31, 2020, the Company has subsidiaries incorporated in countries and jurisdictions including the People’s Republic of China (“PRC”), Hong Kong, Japan, Cayman Islands and British Virgin Islands (“BVI”). As of December 31, 2020, the Company also effectively controls a number of VIEs through the Primary Beneficiaries, as defined below. The VIEs include:

- Beijing Baidu Netcom Science Technology Co., Ltd. (“Baidu Netcom”), controlled by the Company;
- Beijing Perusal Technology Co., Ltd. (“Beijing Perusal”), controlled by the Company;
- Beijing iQIYI Science & Technology Co., Ltd. (“Beijing iQIYI”), and other VIEs controlled by iQIYI, Inc. (“iQIYI VIEs”); and
- Other VIEs controlled by the Company or the Company’s subsidiaries.

The Group’s operations are consisting of Baidu Core and iQIYI. Baidu Core offers online marketing service, and other services including Baidu cloud services and other growth initiatives including Apollo intelligent driving, Xiaodu smart devices, etc.. iQIYI is an innovative market-leading online entertainment service and offers membership services, online advertising services, content distribution and other services. The Group’s principal geographic market is in the PRC. The Company does not conduct any substantive operations of its own, but conducts its primary business operations through its subsidiaries and VIEs in the PRC.

PRC laws and regulations prohibit or restrict foreign ownership of internet content, value-added telecommunication-based online advertising, audio and video services, and mobile application distribution businesses, etc. To comply with these foreign ownership restrictions, the Group operates its websites and primarily provides services subject to such restriction in the PRC through the VIEs, the PRC legal entities that were established or whose equity shares were held by the individuals authorized by the Group. The paid-in capital of the VIEs was mainly funded by the Company or its subsidiaries through loans extended to the authorized individuals who were the shareholders of the VIEs. The Company or its subsidiaries has entered into proxy agreements or powers of attorney and exclusive equity purchase option agreement with the VIEs and nominee shareholders of the VIEs through the Company or its subsidiaries (“Primary Beneficiaries”), which give the Primary Beneficiaries the power to direct the activities that most significantly affect the economic performance of the VIEs and to acquire the equity interests in the VIEs when permitted by the PRC laws, respectively. Certain exclusive agreements have been entered into with the VIEs through the Primary Beneficiaries or their wholly-owned subsidiaries in the PRC, which obligate the Primary Beneficiaries to absorb losses or receive economic benefits of the VIEs’ that could potentially be significant to the VIEs or entitle the Primary Beneficiaries to receive economic benefits from the VIEs that could potentially be significant to the VIEs. In addition, the Group has entered into certain agreements with the shareholders of the VIEs through the Primary Beneficiaries or their wholly-owned subsidiaries, including loan agreements for the paid-in capital of the VIEs and equity pledge agreements for the equity interests in the VIEs held by the shareholders of the VIEs.

Despite the lack of legal majority ownership, there exists a parent-subsidary relationship between the Primary Beneficiaries and the VIEs through the aforementioned agreements with the shareholders of the VIEs. The shareholders of the VIEs effectively assigned all of their voting rights underlying their equity interest in the VIEs to the Primary Beneficiaries. In addition, through the other exclusive agreements, which consist of operating agreements, technology consulting and services agreements

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

1. ORGANIZATION—continued

and license agreements, the Primary Beneficiaries, by themselves or their wholly-owned subsidiaries in the PRC, demonstrate their ability and intention to continue to exercise the ability to absorb losses or receive economic benefits that could potentially be significant to the VIEs. The VIEs are subject to operating risks, which determine the variability of the Company’s interest in those entities. Based on these contractual arrangements, the Company consolidates the VIEs as required by Accounting Standards Codification (“ASC”) Topic 810, *Consolidation*.

Unrecognized revenue-producing assets held by the VIEs include certain internet content provisions and other licenses, domain names and trademarks. The internet content provisions and other licenses, which are held by the VIEs that provide the relevant services, are required under relevant PRC laws, rules and regulations for the operation of Internet businesses in the PRC, and therefore are integral to the Company’s operations.

The principal terms of the agreements entered into amongst the VIEs, their respective shareholders and the Primary Beneficiaries before the amendments made in March 2018 are further described below.

Loan Agreements

Pursuant to loan agreements amongst the shareholders of Baidu Netcom and Baidu Online Network Technology (Beijing) Co., Ltd. (“Baidu Online”), one of the Company’s subsidiaries, Baidu Online provided interest-free loans in an aggregate amount of RMB13.4 billion to the shareholders of Baidu Netcom solely for the latter to fund the capitalization of Baidu Netcom. The loans can be repaid only with the proceeds from the sale of the shareholders’ equity interest in Baidu Netcom to Baidu Online or its designated person. The term of the loan agreements will expire on July 9, 2029 and August 19, 2029, and can be extended with the written consent of both parties before its expiration.

Pursuant to loan agreements amongst the shareholders of Baidu Perusal and Baidu Online, the amount of loans extended to the respective shareholders of Beijing Perusal is RMB3.2 billion. The term of the loan agreements will expire on March 30, 2028 and October 29, 2029, and can be extended with the written consent of both parties before its expiration. Each of the loan agreements amongst Baidu Online or other subsidiaries and the respective shareholders of Beijing Perusal or other VIEs, including iQIYI VIEs, contains substantially the same terms as those described above, except that the amount of the loans and the contract expiration date varies. Beijing QIYI Century Science & Technology Co., Ltd (“Beijing QIYI Century”), a wholly-owned foreign enterprise of iQIYI, has extended the term of the amended and restated loan agreement.

Exclusive Equity Purchase and Transfer Option Agreement

Pursuant to the exclusive equity purchase and transfer option agreement amongst the shareholders of Baidu Netcom, Baidu Netcom and Baidu Online, the shareholders of Baidu Netcom irrevocably granted Baidu Online or its designated person(s) an exclusive option to purchase, to the extent permitted under PRC law, all or part of the equity interests in Baidu Netcom for the cost of the initial contributions to the registered capital or the minimum amount of consideration permitted by applicable PRC law. The shareholders should remit to Baidu Online any amount that is paid by Baidu Online or its designated person(s) in connection with the purchased equity interest. Baidu Online or its designated person(s) have sole discretion to decide when to exercise the option, whether in part or in full. Any and all dividends and other capital distributions made by Baidu Netcom to its shareholders should be repaid to Baidu Online in full amount. Baidu Online would provide unlimited financial support to Baidu Netcom if, in the normal operation of business, Baidu Netcom would become in need of any form of reasonable financial support. If Baidu Netcom were to incur any loss and as a result

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

1. ORGANIZATION—continued

Exclusive Equity Purchase and Transfer Option Agreement—continued

cannot repay any loans from Baidu Online, Baidu Online should unconditionally forgive any such loans to Baidu Netcom given that Baidu Netcom provides sufficient proof for its loss and incapacity to repay. The agreement will terminate when the shareholders of Baidu Netcom have transferred all their equity interests in Baidu Netcom to Baidu Online or its designated person(s) or upon expiration of the term of business of Baidu Online or Baidu Netcom.

Each of the exclusive equity purchase and transfer option agreements amongst the Company, Baidu Online, Beijing Perusal and its shareholders and iQIYI, Beijing QIYI Century, Beijing iQIYI and its shareholders contains substantially the same terms as those described above, except that the initial term of the amended and restated exclusive purchase option agreement amongst iQIYI, Beijing QIYI Century, Beijing iQIYI and its shareholder is ten years, which has been extended, and can be further renewed at iQIYI’s discretion.

Commitment Letters

Pursuant to the commitment letter dated January 30, 2013, under the condition that Beijing iQIYI remains as a consolidated affiliated entity of iQIYI under United States generally accepted accounting principles (“U.S. GAAP”) and the relevant contractual arrangements remain in effect, iQIYI commits to provide unlimited financial support to Beijing iQIYI, if Beijing iQIYI requires any form of reasonable financial support for its normal business operations. If Beijing iQIYI incurs any losses and as a result cannot repay its loans from iQIYI and Beijing QIYI Century, one of iQIYI’s subsidiaries, iQIYI and Beijing QIYI Century would unconditionally forgive their loans to Beijing iQIYI, if Beijing iQIYI provides sufficient proof for its loss and incapacity to repay.

The commitment letters executed by other iQIYI VIEs contain terms similar to the terms described above.

Proxy Agreement/Power of Attorney

Pursuant to the proxy agreement between Baidu Online and the shareholders of Baidu Netcom, the shareholders of Baidu Netcom agreed to entrust all the rights to exercise their voting power and any other rights as shareholders of Baidu Netcom to the person(s) designated by Baidu Online. The shareholders of Baidu Netcom have each executed an irrevocable power of attorney to appoint the person(s) designated by Baidu Online as their attorney-in-fact to vote on their behalf on all matters requiring shareholder approval. The proxy agreement would be in effect for an unlimited term unless terminated in writing by Baidu Online. The power of attorney would be in effect for as long as the shareholders of Baidu Netcom hold any equity interests in Baidu Netcom.

Each of the proxy agreements or shareholder voting rights trust agreements amongst Baidu Online or other subsidiaries and the shareholders of Beijing Perusal and other VIEs contains substantially the same terms as those described above. Each of the proxy agreements will be in effect for an unlimited term unless terminated in writing by Baidu Online or other subsidiaries. Each of the powers of attorney will be in effect for as long as the shareholder of Beijing Perusal or other VIEs, including iQIYI VIEs, holds any equity interests in Beijing Perusal or other VIEs, including iQIYI VIEs, as the case may be.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

1. ORGANIZATION—continued

Operating Agreement

Pursuant to the operating agreement amongst Baidu Online, Baidu Netcom and the shareholders of Baidu Netcom, Baidu Online provides guidance and instructions on Baidu Netcom’s daily operations and financial affairs. Baidu Online has the power to appoint senior executives of Baidu Netcom. The shareholders of Baidu Netcom must appoint the candidates recommended by Baidu Online as their representatives on Baidu Netcom’s board of directors. In addition, Baidu Online agrees to guarantee Baidu Netcom’s performance under any agreements or arrangements relating to Baidu Netcom’s business arrangements with any third party. In return, Baidu Netcom agrees that without the prior consent of Baidu Online, Baidu Netcom will not engage in any transactions that could materially affect the assets, liabilities, rights or operations of Baidu Netcom, including, without limitation, incurrence or assumption of any indebtedness, sale or purchase of any assets or rights, incurrence of any encumbrance on any of its assets or intellectual property rights in favor of a third party or transfer of any agreements relating to its business operation to any third party. The agreement will be in effect for an unlimited term, until the term of business of Baidu Online or Baidu Netcom expires and extension is denied by the relevant approval authorities.

The operating agreement amongst Baidu Online, Beijing Perusal and its shareholders contains substantially the same terms as those described above.

Pursuant to the amended and restated business operation agreement amongst Beijing QIYI Century, Beijing iQIYI and its shareholder, Beijing QIYI Century provides guidance and instructions on Beijing iQIYI’s daily operations and financial affairs. In addition, Beijing QIYI Century agrees to guarantee Beijing iQIYI’s performance under any agreements or arrangements relating to Beijing iQIYI’s business arrangements with any third party. The agreement can only be unilaterally revoked by Beijing QIYI Century. The initial term of the agreement is ten years, which has been extended, and can be further renewed at Beijing QIYI Century’s discretion.

Exclusive Technology Consulting and Services Agreement

Pursuant to the exclusive technology consulting and services agreement between Baidu Online and Baidu Netcom, Baidu Online has the exclusive right to provide technology consulting and services related to, among other things, the maintenance of servers, software development, design of advertisements, and e-commerce technical services to Baidu Netcom. Baidu Online owns the intellectual property rights resulting from the performance of this agreement. Baidu Netcom agrees to pay service fees to Baidu Online and Baidu Online has the right to adjust the service fees at its sole discretion without the consent of Baidu Netcom. The agreement will be in effect for an unlimited term, until the term of business of one party expires and extension is denied by the relevant approval authorities.

Each of the exclusive technology consulting and services agreements between Baidu Online or other subsidiaries and Beijing Perusal or other VIEs, including iQIYI VIEs, contains substantially the same terms as those described above, except the basis of determining the service fees may differ and that the initial term of the exclusive technology consulting and services agreement between Beijing QIYI Century and Beijing iQIYI dated November 23, 2011 is ten years, and has been extended.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

1. ORGANIZATION—continued

License Agreements

Baidu Online and Baidu Netcom entered into a software license agreement and a web layout copyright license agreement (collectively, the “License Agreements”). Pursuant to the License Agreements between Baidu Online and Baidu Netcom, Baidu Online has granted to Baidu Netcom the right to use (including but not limited to) a software license and a web layout copyright license. Baidu Netcom may only use the licenses in its own business operations. Baidu Online has the right to adjust the service fees at its sole discretion. The software license agreement and web layout copyright license agreement were renewed since their original expiration and would be in effect for an unlimited term, until the term of business of one party expires and extension is denied by the relevant approval authorities.

Baidu Online entered into web layout copyright license agreements with Beijing Perusal. Each of the license agreements between the Baidu Online and Beijing Perusal or other VIEs contains substantially the same terms as those described above. Each of the web layout copyright license agreements was renewed in 2013 and would be in effect for an unlimited term, until the term of business of one party expires and extension is denied by the relevant approval authorities.

Pursuant to the trademark license agreement and the software usage license agreement amongst Beijing QIYI Century and Beijing iQIYI effective November 23, 2011, Beijing QIYI Century granted a non-exclusive and non-transferable license, without sublicensing rights, to Beijing iQIYI to use its trademarks and software. Beijing iQIYI may only use the licenses in its own business operations. Beijing QIYI Century has the right to adjust the service fees at its sole discretion. The initial term of the two agreements is five years and the software usage license agreement may be extended upon the written consent of Beijing QIYI Century. The trademark license agreement is automatically extended for successive one-year periods after its expiration unless Beijing QIYI Century early terminates the agreement in accordance with the provisions of the agreement. The software usage license agreement was extended for another five years after its initial term, and was extended for another ten years in December 2020.

Business Cooperation Agreement

Pursuant to the business cooperation agreement amongst Beijing QIYI Century and Beijing iQIYI effective November 23, 2011, Beijing iQIYI agrees to provide Beijing QIYI Century with services, including internet information services, online advertising and other services reasonably necessary within the scope of Beijing QIYI Century’s business. Beijing iQIYI agrees to use, technology services provided by Beijing QIYI Century on its website, including but not limited to, P2P download and video on-demand systems. Beijing QIYI Century agrees to pay specified service fees to Beijing iQIYI as consideration for the internet information services and other services provided by Beijing iQIYI. Beijing iQIYI has the right to waive the service fees at its discretion. The initial term of this agreement is ten years, which has been extended, and can be further renewed at Beijing QIYI Century’s discretion.

Equity Pledge Agreement

Pursuant to the equity pledge agreement between Baidu Online and the shareholders of Baidu Netcom, the shareholders of Baidu Netcom pledged all of their equity interests in Baidu Netcom to Baidu

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

1. ORGANIZATION—continued

Equity Pledge Agreement—continued

Online to guarantee their obligations under the loan agreement and Baidu Netcom’s performance of its obligations under the exclusive technology consulting and services agreement. If Baidu Netcom or its shareholders breach their respective contractual obligations, Baidu Online, as the pledgee, will be entitled to certain rights, including the right to sell the pledged equity interests. The shareholders of Baidu Netcom agreed not to dispose of the pledged equity interests or take any actions that would prejudice Baidu Online’s interest. The equity pledge agreement will expire two years after expiration of the term or the fulfillment by Baidu Netcom and its shareholders of their respective obligations under the exclusive technology consulting and services agreement and the loan agreement.

Each of the equity pledge agreements amongst Baidu Online or other subsidiaries and the shareholders of Beijing Perusal or other VIEs, including iQIYI VIEs, contains substantially the same terms, including its term to expiration, as those described above.

Through the design of the aforementioned agreements, the shareholders of the VIEs effectively assigned their full voting rights to Baidu Online, which gives Baidu Online the power to direct the activities that most significantly impact the VIEs’ economic performance. Baidu Online obtains the ability to approve decisions made by the VIEs and the ability to acquire the equity interests in the VIEs when permitted by PRC law. Baidu Online is obligated to absorb losses or receive economic benefits of the VIEs that could potentially be significant to the VIEs through providing unlimited financial support to the VIEs or is entitled to receive economic benefits from the VIEs that could potentially be significant to the VIEs through the exclusive technology consulting and service fees. As a result of these contractual agreements, Baidu Online is determined to be the primary beneficiary of the VIEs. Despite the lack of technical majority ownership, there exists a parent-subsidiary relationship between the Company and the VIEs through these contractual agreements, and the Company consolidates the VIEs through Baidu Online.

Through the Contractual Arrangements, the shareholders of the VIEs effectively assigned all of their voting rights underlying their equity interest in iQIYI VIEs to iQIYI. In addition, through the other exclusive agreements, which consist of the operation agreements, business cooperating agreement, exclusive technology consulting and services agreements and trademark and software usage license agreements, iQIYI, through its wholly-owned subsidiaries in the PRC, have the right to receive economic benefits from iQIYI VIEs that potentially could be significant to iQIYI VIEs. Lastly, through the commitment letters, iQIYI has the obligation to absorb losses of iQIYI VIEs that could potentially be significant to iQIYI VIEs. Therefore, iQIYI is considered the primary beneficiary of iQIYI VIEs and consolidates iQIYI VIEs and their subsidiaries.

In March 2018, the contractual agreements for certain VIEs, including Baidu Netcom and Beijing Perusal, were amended to include the following terms:

(a) Exclusive equity purchase and transfer option agreement

The Company has (i) an exclusive option to purchase, when and to the extent permitted under PRC laws, all or part of the equity interests in the VIE or all or part of the assets held by the VIE, (ii) an exclusive right to cause the nominee shareholders to transfer their equity interest in the VIE to the Company or any designated person and (iii) an obligation to provide unlimited financial

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

1. ORGANIZATION—continued

Equity Pledge Agreement—continued

support to the VIEs when the VIEs become in need of any form of reasonable financial support in the normal operation of business. If the VIEs were to incur any loss and as a result cannot repay any loans from the Company, the Company will unconditionally forgive any such loans to the VIEs upon provision by the VIEs of sufficient proof for its loss and incapacity to repay.

(b) Proxy Agreements/Power of Attorney

The appointment of any individuals to exercise the powers and rights assigned pursuant to the Proxy Agreement requires the approval of the Company. All the activities in relation to such powers and rights assigned are directed and approved by the Company. The shareholders of the VIEs agreed to entrust all the rights to exercise their voting power and any other rights as shareholders of the VIEs to the person(s) designated by the Company. The shareholders of the VIEs have each executed an irrevocable power of attorney to appoint the person(s) designated by the Company as their attorney-in-fact to vote on their behalf on all matters requiring shareholder approval.

As a result, the power and the rights pursuant to the Proxy Agreements have since been effectively reassigned from Baidu Online to the Company which has the power to direct the activities of the VIEs that most significantly impact the VIEs’ economic performance. The Company or its subsidiaries is also obligated to absorb the expected losses or receive economic benefits of the VIE through the agreements mentioned above. Therefore, the Company has replaced Baidu Online as the primary beneficiary of Baidu Netcom and Beijing Perusal since March 2018. As the VIEs were subject to indirect control by the Company through its subsidiaries immediately before and direct control immediately after the contractual agreements were amended, the change of the primary beneficiary of the VIEs was accounted for as a common control transaction based on the carrying amount of the net assets transferred.

In the opinion of the Company’s legal counsel, (i) the ownership structure relating to the VIEs of the Company is in compliance with existing PRC laws and regulations; (ii) the contractual arrangements entered into by the Company, the corresponding subsidiaries in the PRC, the VIEs and their respective shareholders are valid, binding and enforceable, and will not result in any violation of PRC laws or regulations currently in effect; and (iii) the execution, delivery and performance of the contractual arrangements does not result in any violation of the provisions of the articles of association or business licenses of the corresponding subsidiaries in the PRC or the VIEs.

However, uncertainties in the PRC legal system could cause the Company’s current ownership structure to be found in violation of any existing and/or future PRC laws or regulations and could limit the Company’s ability, through the Primary Beneficiaries, to enforce its rights under these contractual arrangements. Furthermore, shareholders of the VIEs may have interests that are different with those of the Company, which could potentially increase the risk that they would seek to breach the existing terms of the aforementioned agreements.

In addition, if the current structure or any of the contractual arrangements were found to be in violation of any existing or future PRC laws, the Company may be subject to penalties, which may include but not be limited to, the cancellation or revocation of the Company’s business and operating licenses, being required to restructure the Company’s operations or discontinue the Company’s operating activities. The imposition of any of these or other penalties may result in a material and adverse effect on the Company’s ability to conduct its operations. In such case, the Company may not be able to operate or control the VIEs, which may result in deconsolidation of the VIEs.

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

1. ORGANIZATION—continued

Equity Pledge Agreement—continued

The following tables set forth the financial statement balances and amounts of the VIEs and their subsidiaries were included in the consolidated financial statements after the elimination of intercompany balances and transactions among VIEs and their subsidiaries within the Group.

| | As of December 31, | | |
|--|--------------------|--------|--------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| Assets | | | |
| Cash and cash equivalents | 1,895 | 2,313 | 2,348 |
| Short-term investments, net | 2,912 | 1,892 | 6,930 |
| Accounts receivable, net | 3,750 | 5,023 | 6,614 |
| Others | 4,275 | 5,750 | 8,097 |
| Total current assets | 12,832 | 14,978 | 23,989 |
| Fixed assets, net | 4,183 | 3,839 | 4,978 |
| Intangible assets, net | 4,032 | 1,404 | 1,499 |
| Licensed copyrights, net | 2,018 | 1,641 | 993 |
| Produced content, net | 3,735 | 4,355 | 6,130 |
| Long-term investments, net | 18,923 | 21,825 | 20,707 |
| Operating lease right-of-use assets | — | 6,525 | 6,460 |
| Others | 6,886 | 7,970 | 7,717 |
| Total non-current assets | 39,777 | 47,559 | 48,484 |
| Total | 52,609 | 62,537 | 72,473 |
| Liabilities | | | |
| Accounts payable and accrued liabilities | 13,889 | 15,774 | 15,420 |
| Customer deposits and deferred revenue | 3,704 | 4,841 | 6,047 |
| Operating lease liabilities | — | 2,110 | 2,068 |
| Others | 1,219 | 1,967 | 1,516 |
| Total current third-party liabilities | 18,812 | 24,692 | 25,051 |
| Operating lease liabilities | — | 4,227 | 4,376 |
| Others | 2,417 | 2,068 | 1,143 |
| Total non-current third-party liabilities | 2,417 | 6,295 | 5,519 |
| Amounts due to the Company and its non-VIE subsidiaries, net | 22,398 | 17,121 | 19,592 |
| Total | 43,627 | 48,108 | 50,162 |

| | For the years ended December 31, | | |
|---|----------------------------------|---------|---------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| Total revenues | 33,992 | 51,988 | 52,666 |
| Net (loss) income | (6,834) | (2,950) | 2,091 |
| Net cash provided by operating activities | 2,396 | 1,649 | 4,616 |
| Net cash used in investing activities | (16,674) | (4,829) | (8,382) |
| Net cash provided by financing activities | 11,916 | 3,604 | 3,859 |

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

1. ORGANIZATION—continued

Equity Pledge Agreement—continued

As of December 31, 2020 there was no pledge or collateralization of the VIEs’ assets that can only be used to settle obligations of the VIEs, other than aforementioned in the equity pledge agreements and collateralization of a VIE’s office building, restricted cash as described in Note 12. The amount of the net assets of the VIEs was RMB22.3 billion as of December 31, 2020. The creditors of the VIEs’ third-party liabilities did not have recourse to the general credit of the Company in normal course of business. The Company did not provide or intend to provide financial or other supports not previously contractually required to the VIEs during the years presented.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of Presentation and Principles of Consolidation

The consolidated financial statements are prepared in accordance with U.S. GAAP.

Effective on March 1, 2021, the Company has changed its authorized share capital by one-to-eighty subdivision of Shares (the “Share Subdivision”). Each share classified as Class A ordinary shares, Class B ordinary shares and preferred shares of a par value of US\$0.00005 each in the share capital of the Company (including authorized issued and unissued Class A ordinary shares, Class B ordinary shares and preferred shares) be sub-divided into 80 shares of a par value of US\$0.000000625 each. Following the Share Subdivision, the authorized share capital of the Company will be US\$43,520 divided into 66,000,000,000 Class A ordinary shares of a par value of US\$0.000000625 each, 2,832,000,000 Class B ordinary shares of a par value of US\$0.000000625 each and 800,000,000 preferred shares of a par value of US\$0.000000625 each. The number of issued and unissued Class A ordinary shares, Class B ordinary shares and preferred shares as disclosed elsewhere in the consolidated financial statements are presented on a basis after taking into account the effects of the Share Subdivision and have been retrospectively adjusted, where applicable. Simultaneously with the Share Subdivision, the change in ratio of the Company’s ADS to Class A ordinary share (the “ADS Ratio Change”) also became effective. Following the ADS Ratio Change, each ADS now represents eight Class A ordinary shares. Previously, ten ADSs represented one Class A ordinary share. Given that the ADS Ratio Change was exactly proportionate to the Share Subdivision, no new ADSs were issued to any ADS holder and the total number of the Company’s outstanding ADSs remains unchanged immediately after the Share Subdivision and the ADS Ratio Change became effective.

The consolidated financial statements include the financial statements of the Company, its subsidiaries, VIEs and subsidiaries of the VIEs. All inter-company transactions and balances between the Company, its subsidiaries, VIEs and subsidiaries of the VIEs are eliminated upon consolidation. The Company included the results of operations of acquired businesses from the respective dates of acquisition.

(b) Recently adopted accounting pronouncements

Adoption of ASU 2016-13

In June 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments* (“ASU 2016-13”) which requires the measurement and recognition of expected credit losses for financial assets held at amortized cost and is codified in ASC Topic 326, *Financial Instruments – Credit Losses* (“ASC 326”). ASU 2016-13 replaces the existing

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(b) Recently adopted accounting pronouncements—continued

Adoption of ASU 2016-13—continued

incurred loss impairment model with an expected loss methodology, which will result in more timely recognition of credit losses. Further, ASU 2016-13 modified the impairment model of available-for-sale debt securities and required the company to determine whether all or a portion of the unrealized loss on an available-for-sale debt security is a credit loss. The Company adopted ASU 2016-13 on January 1, 2020, using a modified retrospective transition method and did not restate the comparable periods, which resulted in a cumulative-effect adjustment to decrease the opening balance of retained earnings on January 1, 2020 by RMB314 million, including the allowance for credit losses for account receivable, contract assets and debt securities.

Adoption of ASU 2017-04

In January 2017, the FASB issued ASU No. 2017-04, *Simplifying the Test for Goodwill Impairment*, which simplifies the accounting for goodwill impairment by eliminating Step two from the goodwill impairment test. If the carrying amount of a reporting unit exceeds its fair value, an impairment loss shall be recognized in an amount equal to that excess, versus determining an implied fair value in Step two to measure the impairment loss. The Company adopted this guidance on a prospective basis on January 1, 2020 with no material impact on its consolidated financial statements as a result of adopting the new standard.

Adoption of ASU 2019-02

In March 2019, the FASB issued ASU No. 2019-02, *Improvements to Accounting for Costs of Films and License Agreements for Program Materials* (“ASU 2019-02”), which includes the following major changes from previous legacy GAAP that are applicable to the Company:

- The content distinction for capitalization of production costs of an episodic television series and production costs of films is removed;
- Entities are required to test films and license agreements for program material for impairment at a film group level when the film or license agreements are predominantly monetized with other films and license agreements;
- Entities shall assess estimates of the use of a film in a film group and account for such changes prospectively;
- Cash outflows for the costs incurred to obtain rights for both produced and licensed content are required to be reported as operating cash outflows in the statement of cash flows.

The Company adopted ASU 2019-02 on January 1, 2020, using a prospective transition method. For the year ended December 31, 2020, cash outflows for the costs incurred to acquire licensed copyrights are reported as operating cash outflows in the Company’s consolidated statement of cash flows whereas they were reported as investing cash outflows prior to the adoption of ASU 2019-02. There was no material impact to the consolidated balance sheet or consolidated statement of comprehensive income (loss). See the Company’s updated accounting policies for Produced Content and Licensed Copyrights for further details.

Cash paid for content, which includes both licensed copyrights and produced content, is RMB17.0 billion for the year ended December 31, 2020.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(c) Use of Estimates

The preparation of the financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Management evaluates estimates, including those related to the standalone selling prices of performance obligations and amounts of variable considerations of revenue contracts, the allowances for credit losses of accounts receivable, contract assets and debt securities, fair values of certain debt and equity investments, future viewership consumption patterns and useful lives of licensed copyrights and produced content, future revenues generated by the broadcasting and sublicensing rights of content assets (licensed and produced), fair values of licensed copyrights and produced contents monetized as a film group or individually, fair value of nonmonetary content exchanges, impairment of long-lived assets, long-term investments and goodwill, the purchase price allocation and fair value of pre-existing equity interests, noncontrolling interests and redeemable noncontrolling interests with respect to business combinations, deferred tax valuation allowance and the fair value of share-based awards and estimated forfeitures for share-based awards among others. Management bases the estimates on historical experience and on various other assumptions that are believed to be reasonable, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Actual results could differ from these estimates.

(d) Foreign Currency

The Company’s functional currency is the US\$. The Company’s subsidiaries, VIEs and subsidiaries of the VIEs determine their functional currencies based on the criteria of ASC Topic 830, *Foreign Currency Matters*. The Company uses the RMB as its reporting currency. The Company uses the exchange rate as of the balance sheet date to translate its assets and liabilities and the average daily exchange rate for each month to translate its income and expense items to reporting currency. Any translation gains (losses) are recorded in other comprehensive income (loss). Transactions denominated in foreign currencies are measured and recorded into the functional currency at the exchange rates prevailing on the transaction dates. Assets and liabilities denominated in foreign currencies other than functional currency are remeasured into the functional currency at the exchange rates prevailing at the balance sheet date. Exchange gains and losses are included in earnings as a component of “Other income (loss), net.”

(e) Segment Reporting

As of December 31, 2018, 2019 and 2020, the Company had two reportable segments, Baidu Core and iQIYI. Baidu Core mainly provides search-based, feed-based and other online marketing services, as well as products and services from its new AI initiatives. iQIYI is an online entertainment service provider that offers original, professionally produced and partner-generated content on its platform. In early April 2018, iQIYI completed its initial public offering (“IPO”) on the Nasdaq Global Market.

The Company’s chief executive officer, who has been identified as the chief operating decision marker (“CODM”), reviews the operating results of Baidu Core and iQIYI, to allocate resources and assess the Company’s performance. Accordingly, the financial statements include segment information which reflects the current composition of the reportable segments in accordance with ASC Topic 280, *Segment Reporting*.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(f) Business Combinations

The Company accounts for its business combinations using the purchase method of accounting in accordance with ASC Topic 805, *Business Combinations*. The purchase method of accounting requires that the consideration transferred to be allocated to the assets, including separately identifiable assets and liabilities the Company acquired, based on their estimated fair values. The consideration transferred in an acquisition is measured as the aggregate of the fair values at the date of exchange of the assets given, liabilities incurred, and equity instruments issued as well as the contingent considerations as of the acquisition date. The costs directly attributable to the acquisition are expensed as incurred. Identifiable assets, liabilities and contingent liabilities acquired or assumed are measured separately at their fair value as of the acquisition date, irrespective of the extent of any noncontrolling interests. The excess of (i) the total of cost of acquisition, fair value of the noncontrolling interests and acquisition date fair value of any previously held equity interests in the acquiree over (ii) the fair value of the identifiable net assets of the acquiree, is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in earnings.

In a business combination achieved in stages, the Company remeasures its previously held equity interest in the acquiree immediately before obtaining control at its acquisition-date fair value and the re-measurement gain or loss, if any, is recognized in “Others, net” in the consolidated statements of comprehensive income (loss).

The determination and allocation of fair values to the identifiable assets acquired, liabilities assumed and noncontrolling interests is based on various assumptions and valuation methodologies requiring considerable judgment from management. The most significant variables in these valuations are discount rates, the number of years on which to base the cash flow projections, as well as the assumptions and estimates used to determine the cash inflows and outflows. The Company determines discount rates to be used based on the risk inherent in the related activity’s current business model and industry comparisons.

(g) Cash, Cash Equivalents and Restricted Cash

Cash and cash equivalents primarily consist of cash, money market funds, investments in interest bearing demand deposit accounts, time deposits and highly liquid investments with original maturities of three months or less from the date of purchase and are stated at cost which approximates their fair value.

Restricted cash mainly represents escrow amount deposited for a business acquisition and cash pledged for short-term facilities.

(h) Accounts Receivable and Contract Assets, net

Accounts receivable are recognized and carried at the original invoiced amount less an allowance for credit losses. The Company maintains an allowance for credit losses in accordance with ASC 326 and records the allowance for credit losses as an offset to accounts receivable and contract assets, and the estimated credit losses charged to the allowance is classified as “Selling, general and administrative” in the consolidated statements of comprehensive income (loss).

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(h) Accounts Receivable and Contract Assets, net—continued

The Company assesses collectability by reviewing accounts receivable and contract assets on a collective basis where similar characteristics exist, primarily based on similar business line, service or product offerings and on an individual basis when the Company identifies specific customers with known disputes or collectability issues. In determining the amount of the allowance for credit losses, the Company considers historical collectability based on past due status, the age of the accounts receivable balances and contract assets balances, credit quality of the Company’s customers based on ongoing credit evaluations, current economic conditions, reasonable and supportable forecasts of future economic conditions, and other factors that may affect the Company’s ability to collect from customers.

(i) Receivables from Online Payment Agencies, net

Receivables from online payment agencies are funds due from the third-party online payment service providers for clearing transactions. Funds were paid or deposited by customers or users through these online payment agencies for services provided by the Company. The Company considers and monitors the credit worthiness of the third-party payment service providers and recognizes credit losses based on ongoing credit evaluations. Receivable balances are written off when they are deemed uncollectible. The balances are included in “Other current assets, net” on the consolidated balance sheets. As of December 31, 2018, 2019 and 2020, no allowance for credit losses was provided for the receivables from online payment agencies.

(j) Investments

Short-term investments

All highly liquid investments with original maturities less than twelve months are classified as short-term investments. Investments that are expected to be realized in cash during the next twelve months are also included in short-term investments.

The Company accounts for short-term debt investments in accordance with ASC Topic 320, *Investments—Debt Securities* (“ASC 320”). The Company classifies the short-term investments in debt as held-to-maturity, trading or available-for-sale whose classification determines the respective accounting methods stipulated by ASC 320. Dividend and interest income, including amortization of the premium and discount arising at acquisition, for all categories of investments in securities are included in earnings. Any realized gains or losses on the sale of the short-term investments are determined on a specific identification method, and such gains and losses are reflected in earnings during the period in which gains or losses are realized.

Securities that the Company has the positive intent and ability to hold to maturity are classified as held-to-maturity securities and stated at amortized cost less allowance for credit losses.

Securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities, in accordance with ASC 320. Unrealized holding gains and losses for trading securities are included in earnings.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(j) Investments—continued

Short-term investments—continued

Debt investments not classified as trading or as held-to-maturity are classified as available-for-sale debt securities, which are reported at fair value, with unrealized gains and losses recorded in “Accumulated other comprehensive (loss) income” on the consolidated balance sheets.

The allowance for credit losses of the held-to-maturity debt securities reflects the Company’s estimated expected losses over the contractual lives of the held-to-maturity debt securities and is charged to “Others, net” in the consolidated statements of comprehensive income (loss). Estimated allowances for credit losses are determined by considering reasonable and supportable forecasts of future economic conditions in addition to information about past events and current conditions. As of December 31, 2018, 2019 and 2020, the allowance for credit losses provided for the held-to-maturity debt securities held by the Company was insignificant.

Long-term investments

The Company’s long-term investments consist of equity investments with readily determinable fair value, equity method investments, equity investments without readily determinable fair value, other investments accounted for at fair value, held-to-maturity debt investments and available-for-sale debt investments.

The Company adopted ASU No. 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities* (“ASU 2016-01”), codified in ASC Topic 321, *Investments—Equity Securities* (“ASC 321”) from January 1, 2018 and the cumulative effect of RMB1.9 billion representing the unrealized gains of available-for-sale equity securities before the adoption was recorded as an adjustment to the opening retained earnings. Pursuant to ASC 321, equity investments, except for those accounted for under the equity method, those that result in consolidation of the investee and certain other investments, are measured at fair value, and any changes in fair value are recognized in earnings. For equity securities without readily determinable fair value and do not qualify for the existing practical expedient in ASC Topic 820, *Fair Value Measurements and Disclosures* (“ASC 820”) to estimate fair value using the net asset value per share (or its equivalent) of the investment, the Company elected to use the measurement alternative to measure those investments at cost, less any impairment, plus or minus changes resulting from observable price changes in orderly transactions for identical or similar investments of the same issuer, if any. Significant judgments are required to determine (i) whether observable price changes are orderly transactions and identical or similar to an investment held by the Company; and (ii) the selection of appropriate valuation methodologies and underlying assumptions, including expected volatility and the probability of exit events as it relates to liquidation and redemption features used to measure the price adjustments for the difference in rights and obligations between instruments. Equity securities with readily determinable fair values are measured at fair value, and any changes in fair value are recognized in “Others, net” in the consolidated statements of comprehensive income (loss).

For equity investments measured at fair value with changes in fair value recorded in earnings, the Company does not assess whether those securities are impaired. For equity investments that the Company elects to use the measurement alternative, the Company makes a qualitative assessment considering impairment indicators to evaluate whether investments are impaired at each reporting date.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(j) Investments—continued

Long-term investments—continued

Impairment indicators considered include, but are not limited to, a significant deterioration in the earnings performance or business prospects of the investee, including factors that raise significant concerns about the investee’s ability to continue as a going concern, a significant adverse change in the regulatory, economic, or technologic environment of the investee and a significant adverse change in the general market condition of either the geographical area or the industry in which the investee operates. If a qualitative assessment indicates that the investment is impaired, the entity has to estimate the investment’s fair value in accordance with the principles of ASC 820. If the fair value is less than the investment’s carrying value, the Company recognizes an impairment loss in net income equal to the difference between the carrying value and fair value.

Investments in entities in which the Company can exercise significant influence but does not own a majority equity interest or control are accounted for using the equity method of accounting in accordance with ASC Topic 323, *Investments-Equity Method and Joint Ventures* (“ASC 323”). Under the equity method, the Company initially records its investment at cost and the difference between the cost of the equity investee and the amount of the underlying equity in the net assets of the equity investee is accounted for as if the investee were a consolidated subsidiary. The Company subsequently adjusts the carrying amount of its investment to recognize the Company’s proportionate share of each equity investee’s net income or loss into earnings. The Company will discontinue applying the equity method if an investment (plus additional financial support provided to the investee, if any) has been reduced to zero. When the Company has other investments in its equity-method investee and is not required to advance additional funds to that investee, the Company would continue to report its share of equity method losses in its consolidated statements of comprehensive income (loss) after its equity-method investment in ordinary shares has been reduced to zero, to the extent of and as an adjustment to the adjusted basis of the Company’s other investments in the investee. Such losses are first applied to those investments of a lower liquidation preference before being further applied to the investments of a higher liquidation preference. The Company adopted a one-quarter lag in reporting for its share of equity income/(loss) in all of its equity method investees.

The Company evaluates its equity method investments for impairment at each reporting date, or more frequently if events or changes in circumstances indicate that the carrying amount of the investment might not be recoverable. Factors considered by the Company when determining whether an investment has been other-than-temporarily-impaired, include, but are not limited to, the length of the time and the extent to which the market value has been less than cost, the financial performance and near-term prospect of the investee, and the Company’s intent and ability to retain the investment until the recovery of its cost. An impairment loss on the equity method investments is recognized in earnings when the decline in value is determined to be other-than-temporary and is allocated to the individual net assets underlying equity method investments in the following order: 1) reduce any equity method goodwill to zero; 2) reduce the individual basis differences related to the investee’s long-lived assets pro rata based on their amounts relative to the overall basis difference at the impairment date; and 3) reduce the individual basis difference of the investee’s remaining assets in a systematic and rational manner.

In accordance with ASC Subtopic 946-320, *Financial Services—Investment Companies, Investments—Debt and Equity Securities* (“ASC 946-320”), the Company accounts for long-term equity investments

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(j) Investments—continued

Long-term investments—continued

in unlisted companies held by consolidated investment companies at fair value. These investments were initially recorded at their transaction price net of transaction costs, if any. Fair value of these investments are re-measured at each reporting date in accordance with ASC 820.

Available-for-sale debt investments are convertible debt instruments issued by private companies and investment in preferred shares that is redeemable at the Company's option, which are measured at fair value. Interest income is recognized in earnings. All other changes in the carrying amount of these debt investments are recognized in other comprehensive income (loss).

(k) Fair Value Measurements of Financial Instruments

Financial instruments are in the form of cash and cash equivalents, restricted cash, short-term investments, accounts receivable, amounts due from and due to related parties, other receivables, long-term investments, short-term loans, accounts payable and accrued liabilities, customer advances and deposits, derivative instruments, notes payable, convertible senior notes and long-term loans. Except for the current portion of long-term loans and notes payables, the carrying values of the aforementioned financial instruments included in current assets and liabilities approximate their respective fair values because of their general short maturities. The carrying amounts of long-term loans approximate fair values as the related interest rates currently offered by financial institutions for similar debt instruments of comparable maturities. The fair value of long-term investments, notes payable and convertible senior notes that are not reported at fair value are disclosed in Note 25.

(l) Fixed Assets

Fixed assets are stated at cost less accumulated depreciation. Depreciation is recorded on a straight-line basis over the shorter of the estimated useful lives of the assets or the term of the related lease, as follows:

| | |
|--|--|
| Office building | - 43 to 45 years |
| Office building related facility, machinery and equipment | - 15 years |
| Computer equipment | - 3 to 5 years |
| Office equipment | - 3 to 5 years |
| Vehicles | - 5 years |
| Leasehold improvements | - over the shorter of lease terms or estimated useful lives of the assets |

Fixed assets have no estimated residual value except for the office building and its related facility, machinery and equipment, which have an estimated residual value of 4% of the cost.

Repair and maintenance costs are charged to expense as incurred, whereas the cost of renewals and betterments that extend the useful life of fixed assets are capitalized as additions to the related assets. Retirements, sales and disposals of assets are recorded by removing the cost and accumulated depreciation from the asset and accumulated depreciation accounts with any resulting gain or loss reflected in earnings. All direct and indirect costs that are related to the construction of fixed assets and

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(l) Fixed Assets—continued

incurred before the assets are ready for their intended use are capitalized as construction in progress. Construction in progress is transferred to specific fixed assets items and depreciation of these assets commences when they are ready for their intended use.

Interest costs are capitalized if they are incurred during the acquisition, construction or production of a qualifying asset and such costs could have been avoided if expenditures for the assets have not been made. Capitalization of interest costs commences when the activities to prepare the asset are in progress and expenditures and borrowing costs are being incurred. Interest costs are capitalized until the assets are ready for their intended use. Interest costs capitalized for the years ended December 31, 2018, 2019 and 2020 were insignificant.

(m) Licensed Copyrights, net

Licensed copyrights consist of professionally-produced content such as films, television series, variety shows and other video content acquired from external parties. The license fees are capitalized and, unless prepaid, a corresponding liability is recorded when the cost of the content is known, the content is accepted by the Company in accordance with the conditions of the license agreement and the content is available for its first showing on the Company’s websites. Licensed copyrights are presented on the consolidated balance sheets as current and non-current based on estimated time of usage.

The Company’s licensed copyrights include the right to broadcast and in some instances, the right to sublicense. The broadcasting right, refers to the right to broadcast the content on its own websites and the sublicensing right, refers to the right to sublicense the underlying content to external parties. When licensed copyrights include both broadcasting and sublicensing rights, the content costs are allocated to these two rights upon initial recognition, based on the relative proportion of the estimated total revenues that will be generated by each right over its estimated useful lives.

For the right to broadcast the contents on its own websites that generates online advertising and membership services revenues, based on factors including historical and estimated future viewership patterns, the content costs are amortized using an accelerated method by content categories over the shorter of each content’s contractual period or estimated useful lives within ten years, beginning with the month of first availability. Content categories accounting for most of the Group’s content include newly released drama series, newly released movies, animations, library drama series and library movies. Estimates of future viewership consumption patterns and estimated useful lives are reviewed periodically, at least on an annual basis and revised, if necessary. Revisions to the amortization patterns are accounted for as a change in accounting estimate prospectively in accordance with ASC Topic 250, *Accounting Changes and Error Corrections* (“ASC 250”).

For the right to sublicense the content to external parties that generates direct content distribution revenues, the content costs are amortized based on its estimated usage pattern and recorded as cost of revenues.

(n) Produced Content, net

The Company produces original content in-house and collaborates with external parties. Produced content primarily consists of films, episodic series, variety shows and animations. The costs incurred in

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(n) Produced Content, net—continued

the physical production of original content includes direct production costs, production overhead and acquisition costs. Production costs for original content that are predominantly monetized in a film group are capitalized and reported separately as non-current assets with caption of “Produced content, net” on the consolidated balance sheets. Production costs for original content predominantly monetized on its own are capitalized to the extent that they are recoverable from total revenues expected to be earned (“ultimate revenue”); otherwise, they are expensed as cost of revenues. Ultimate revenue estimates include revenue expected to be earned from all sources, including exhibition, licensing, or exploitation of produced content if the Company has demonstrated a history of earning such revenue. The Company estimates ultimate revenue to be earned during the estimated useful lives of produced content based on anticipated release patterns and historical results of similar produced content, which are identified based on various factors, including cast and crew, target audience and popularity. Produced content also includes cash expenditures made to acquire a proportionate share of certain rights to films including profit sharing, distribution and/or other rights. Exploitation costs are expensed as incurred.

Based on factors including historical and estimated future viewership consumption patterns, the Group amortizes film costs for produced content that is predominantly monetized in a film group. For produced content that is monetized on its own, the Group considers historical and estimated usage patterns to determine the pattern of amortization for film costs. Based on the estimated patterns, the Group amortizes produced content using an accelerated method over its estimated useful lives within ten years, beginning with the month of first availability and such costs are included in “Cost of revenues” in the consolidated statement of comprehensive income (loss).

(o) Change in accounting estimates of licensed copyrights and produced content

In 2020, the Company revised its estimation of the estimated future viewership consumption patterns and extended the estimated useful lives of its licensed copyrights and produced content to better reflect the usage of these content assets. As a result of these revisions, amortization expense decreased by RMB680 million, and net loss decreased by RMB680 million for the year ended December 31, 2020, respectively. The impact to basic and diluted EPS for the year ended December 31, 2020 was insignificant.

(p) Impairment of licensed copyrights and produced content

The Company’s business model is mainly subscription and advertising based, as such the majority of the Company’s content assets (licensed copyrights and produced content) are predominantly monetized with other content assets, whereas a smaller portion of the Company’s content assets are predominantly monetized at a specific title level such as variety shows and investments in a proportionate share of certain rights to films including profit sharing, distribution and/or other rights. Because the identifiable cash flows related to content launched on the Company’s Mainland China platform are largely independent of the cash flows of other content launched on the Company’s overseas platform, the Company has identified two separate film groups. The Company reviews its film groups and individual content for impairment when there are events or changes in circumstances that indicate the fair value of a film group or individual content may be less than its unamortized costs. Examples of such events or changes in circumstances include, a significant adverse change in technological, regulatory, legal,

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(p) Impairment of licensed copyrights and produced content—continued

economic, or social factors, that could affect the fair value of the film group or the public’s perception of a film or the availability of a film for future showings, a significant decrease in the number of subscribers or forecasted subscribers, or the loss of a major distributor, a change in the predominant monetization strategy of a film that is currently monetized on its own, actual costs substantially in excess of budgeted costs, substantial delays in completion or release schedules, or actual performance subsequent to release failing to meet expectations set before release such as a significant decrease in the amount of ultimate revenue expected to be recognized.

When such events or changes in circumstances are identified, the Company assesses whether the fair value of an individual content (or film group) is less than its unamortized film costs, determines the fair value of an individual content (or film group) and recognizes an impairment charge for the amount by which the unamortized capitalized costs exceed the individual content’s (or film group’s) fair value. The Company mainly uses a discounted cash flow approach to determine the fair value of an individual content or film group, for which the most significant inputs include forecasted future revenues, costs and operating expenses attributable to an individual content or the film group and the discount rate. An impairment loss attributable a film group is allocated to individual licensed copyrights and produced content within the film group on a pro rata basis using the relative carrying values of those assets as the Company cannot estimate the fair value of individual contents in the film group without undue cost and effort.

(q) Impact of COVID-19

During the year ended December 31, 2020, the Company’s operations has been affected by the COVID-19 pandemic. The Company’s online marketing revenues declined compared to the prior period mainly due to weakness in online advertising demand as its customers in certain industries are negatively impacted by COVID-19. The Company has also provided additional credit losses for accounts receivable and contract assets, recognized impairment charges on its long-term investments, intangible asset and content assets, and recorded its share of losses from equity method investees in the year ended December 31, 2020, due to the impact of COVID-19 and other factors. In addition, increased market volatility has contributed to larger fluctuations in the valuation of the Company’s equity investments.

There are still uncertainties of COVID-19’s future impact, and the extent of the impact will depend on a number of factors, including the duration and severity of COVID-19, possibility of a second wave in China, the development and progress of distribution of COVID-19 vaccine and other medical treatment, the potential change in user behavior, especially on internet usage due to the prolonged impact of COVID-19, the actions taken by government authorities, particularly to contain the outbreak, stimulate the economy to improve business condition especially for SMEs, almost all of which are beyond the Company’s control. As a result, certain of the Company’s estimates and assumptions, including the allowance for credit losses, the valuation of certain debt and equity investments, long-term investments, content assets and long-lived assets subject to impairment assessments, require significant judgments and carry a higher degree of variabilities and volatilities that could result in material changes to the Company’s current estimates in future periods.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(r) Goodwill and Intangible Assets

Goodwill

Goodwill represents the excess of the purchase price over the fair value of the identifiable net assets acquired in a business combination. The Company assesses goodwill for impairment in accordance with ASC Subtopic 350-20, *Intangibles—Goodwill and Other: Goodwill* (“ASC 350-20”), which requires that goodwill to be tested for impairment at the reporting unit level at least annually and more frequently upon the occurrence of certain events, as defined by ASC 350-20. As of December 31, 2018, 2019 and 2020, the Company has two reporting units, consisting of Baidu Core and iQIYI.

The Company has the option to assess qualitative factors first to determine whether it is necessary to perform the quantitative test in accordance with ASC 350-20. In the qualitative assessment, the Company considers primary factors such as industry and market considerations, overall financial performance of the reporting unit, and other specific information related to the operations. If the Company believes, as a result of the qualitative assessment, that it is more-likely-than-not that the fair value of the reporting unit is less than its carrying amount, the quantitative impairment test described above is required. Otherwise, no further testing is required. The quantitative impairment test compares the fair value of the reporting unit with its carrying amount, including goodwill. If the carrying amount of a reporting unit exceeds its fair value, an impairment loss shall be recognized in an amount equal to that excess.

The Company performed qualitative assessments for the reporting unit of Baidu Core in the years ended 2018, 2019 and 2020. Based on the requirements of ASC 350-20, the Company evaluated all relevant factors including, but not limited to, macroeconomic conditions, industry and market conditions, financial performance, and the share price of the Company. The Company weighed all factors in their entirety and concluded that it was not more-likely-than-not the fair value was less than the carrying amount of Baidu Core, and further impairment testing on goodwill was unnecessary as of December 31, 2018, 2019 and 2020.

The Company elected to choose to bypass the qualitative assessment and proceed directly to perform quantitative test for the reporting unit of iQIYI. Subsequent to iQIYI’s IPO, the Company primarily considered the quoted market price of iQIYI’s share to determine the fair value of the reporting unit. As of December 31, 2018, 2019 and 2020, the fair value of iQIYI exceeded its carrying amount, therefore, goodwill related to the iQIYI reporting unit was not impaired and the Company was not required to perform further testing.

On disposal of a portion of reporting unit that constitutes a business, the attributable amount of goodwill is included in the determination of the amount of profit or loss on disposal. When the Group disposes of a business within the reporting unit, the amount of goodwill disposed is measured on the basis of the relative fair value of the business disposed and the portion of the reporting unit retained. This relative fair value approach is not used when the business to be disposed was not integrated into the reporting unit after its acquisition, in which case the current carrying amount of the acquired goodwill should be included in the carrying amount of the business to be disposed.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(r) Goodwill and Intangible Assets—continued

Intangible assets

Intangible assets with finite lives are carried at cost less accumulated amortization. All intangible assets with finite lives are amortized using the straight-line method over their estimated useful lives.

Intangible assets have weighted average useful lives from the date of purchase as follows:

| | |
|---------------------------------------|------------|
| Trademarks | - 10 years |
| Technology | - 7 years |
| Intellectual property right | - 7 years |
| Online literature | - 8 years |
| Others | - 8 years |

Intangible assets with indefinite useful life are not amortized and are tested for impairment annually or more frequently, if events or changes in circumstances indicate that they might be impaired in accordance with ASC Subtopic 350-30, *Intangibles-Goodwill and Other: General Intangibles Other than Goodwill* (“ASC 350-30”).

Upon the initial application of ASU No. 2016-02, *Leases* (Topic 842) (“ASU 2016-02”) on January 1, 2019, codified in ASC 842, *Leases* (“ASC 842”), land use rights were presented as operating lease right-of-use assets (“ROU assets”). Such amount was included in the opening balance of operating lease ROU assets as of January 1, 2019 with no adjustments made to the comparative periods.

(s) Impairment of Long-Lived Assets Other Than Goodwill

The Company evaluates long-lived assets, such as fixed assets and purchased or internally developed intangible assets with finite lives other than licensed copyrights and produced contents, for impairment whenever events or changes in circumstances indicate the carrying value of an asset may not be recoverable in accordance with ASC Topic 360, *Property, Plant and Equipment*. When such events occur, the Company assesses the recoverability of the asset group based on the undiscounted future cash flows the asset group is expected to generate and recognizes an impairment loss when estimated undiscounted future cash flows expected to result from the use of the asset group plus net proceeds expected from disposition of the asset group, if any, is less than the carrying value of the asset group. If the Company identifies an impairment, the Company reduces the carrying amount of the asset group to its estimated fair value based on a discounted cash flow approach or, when available and appropriate, to comparable market values and the impairment loss, if any, is recognized in “Others, net” in the consolidated statements of comprehensive income (loss). The Company uses estimates and judgments in its impairment tests and if different estimates or judgments had been utilized, the timing or the amount of any impairment charges could be different. Asset groups to be disposed of would be reported at the lower of the carrying amount or fair value less costs to sell, and no longer depreciated. The assets and liabilities of a disposal group classified as held for sale would be presented separately in the appropriate asset and liability sections of the consolidated balance sheets.

(t) Leases

The Company adopted ASC 842 from January 1, 2019 by using the modified retrospective method and did not restate the figures presented for the 2018 comparative year. The Company has elected the

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(t) Leases—continued

package of practical expedients, which allows the Company not to reassess (1) whether any expired or existing contracts as of the adoption date are or contain a lease, (2) lease classification for any expired or existing leases as of the adoption date and (3) initial direct costs for any expired or existing leases as of the adoption date. The Company also elected the practical expedient not to separate lease and non-lease components of contracts, except for bandwidth service included in internet data center (“IDC”) facilities lease contracts. Lastly, the Company elected the short-term lease exemption for all contracts with lease terms of 12 months or less.

The Company determines if an arrangement is a lease or contains a lease at lease inception. For operating leases, the Company recognizes an ROU asset and a lease liability based on the present value of the lease payments over the lease term on the consolidated balance sheets at commencement date. For finance leases, assets are included in “Other non-current assets” on the consolidated balance sheets. As most of the Company’s leases do not provide an implicit rate, the Company estimates its incremental borrowing rate based on the information available at the commencement date in determining the present value of lease payments. The incremental borrowing rate is estimated to approximate the interest rate on a collateralized basis with similar terms and payments, and in economic environments where the leased asset is located. The Company’s leases often include options to extend and lease terms include such extended terms when the Company is reasonably certain to exercise those options. Lease terms also include periods covered by options to terminate the leases when the Company is reasonably certain not to exercise those options. Lease expense is recorded on a straight-line basis over the lease term.

(u) Revenue Recognition

The Company adopted ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* (“ASU 2014-09”), codified in ASC Topic 606, *Revenue from Contracts with Customers* (“ASC 606”), from January 1, 2018 using the modified retrospective method. The cumulative effect of adopting ASC 606 resulted in an increase of RMB933 million to the opening balance of retained earnings at January 1, 2018, which is primarily related to the Company’s online marketing revenues.

Revenue is recognized when control of promised goods or services is transferred to the Company’s customers in an amount of consideration to which an entity expects to be entitled to in exchange for those goods or services. Revenue is recorded net of valued added taxes (“VAT”).

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(u) Revenue Recognition—continued

The Company’s revenue recognition policies effective on the adoption date of ASC 606 are as follows:

Performance-based online marketing services

Cost-per-click (“CPC”)

The Company’s auction-based P4P platform enables customers to bid for priority placement of paid sponsored links and reach users who search for information related to their products or services. P4P online marketing customers can choose from search-based and feed-based online marketing services, and select criteria for their inventory purchase, such as daily spending limit and user profile targeted, including, but not limited to, users from specific regions in China and users online during specific time period. Revenue is recognized when all of the revenue recognition criteria are met, which is generally when a user clicks on one of the customer-sponsored links or feed-based marketing.

Other performance-based online marketing services

To the extent the Company provides online marketing services based on performance criteria other than cost-per-click, such as the number of downloads (and user registration) of mobile apps and the pre-determined ratios of completed transaction volumes, revenue is recognized when the specified performance criteria are met along with the satisfaction of other applicable revenue recognition criteria.

Online display advertising services

The Company provides online display advertising services to its customers by integrating text description, image and/or video, and displaying the advertisement in the search result, in Baidu Feed or on other properties. The Company recognizes revenue on a pro-rata basis over the contractual term for cost per time advertising arrangements, commencing on the start date of the display advertisement, or based on the number of times that the advertisement has been displayed for cost per thousand impressions advertising arrangements.

For advertisements to be displayed in different spots, placed under different forms and displayed at different times, the Company would evaluate all of the performance obligations in the arrangement to determine whether each performance obligation is distinct. Consideration is allocated to each performance obligation based on its standalone selling price at contract inception. The Company generally determines standalone selling prices based on the prices charged to customers on a standalone basis or estimates it using an expected cost plus margin approach. If a promised good or service does not meet the criteria to be considered distinct, it is combined with other promised goods or services until a distinct bundle of goods or services exists.

Baidu Union online marketing services

Baidu Union is a program through which the Company expands distribution of its customers’ sponsored links or advertisements by leveraging the traffic of Baidu Union partners’ online properties.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(u) Revenue Recognition—continued

Baidu Union online marketing services—continued

The Company acquires traffic from Baidu Union partners and is responsible for service fulfillment, pricing and bearing inventory risks. The services which the Company provided to customers through Baidu Union partners’ online properties include CPC, other performance-based online marketing services and online display advertising services. These services are provided in the same way to our customers as those through Baidu’s own platforms or properties. As principal, the Company recognizes revenue from Baidu Union on a gross basis. Payments made to Baidu Union partners are recorded as traffic acquisition costs, which are included in “Cost of revenues” in the consolidated statements of comprehensive income (loss).

Online marketing services customers are required to pay a deposit before using the Company’s services. Once their account balance falls below a designated amount, they will receive an automated notice from the Company to replenish their accounts. Customer deposit is deducted and revenue is recognized when a user clicks on the customer’s link in the search result, when other performance criteria other than CPC have been satisfied, or when online display advertising services have been provided. The Company offers payment terms to certain customers based on their credit history with the Company and other credit factors. The Company may also offer payment terms to certain agencies, as is common in the industry.

Collection

Certain customers of online marketing services are required to pay a deposit before using the Company’s services and are sent automated reminders to replenish their accounts when the balance falls below a designated amount. The deposits received are recorded as “Customer deposits and deferred revenue” on the consolidated balance sheets. The amounts due to the Company are deducted from the deposited amounts when users click on the paid sponsored links in the search results or other performance criteria have been satisfied. In addition, the Company offers payment terms to some customers based on their historical marketing placements and credibility. The Company also offers longer payment terms to certain online payment agencies, consistent with industry practice.

Payment terms and conditions vary by customer and are based on the billing schedule established in the Company’s contracts or purchase orders with customers, but the Company generally provides credit terms to customers within one year; therefore, the Company has determined that its contracts do not include a significant financing component.

Sales incentives

The Company provides sales incentives to third-party agents that entitle them to receive price reductions on the online marketing services by meeting certain cumulative consumption requirements. The Company accounts for these incentives granted to customers as variable consideration and net them against revenue. The amount of variable consideration is measured based on the most likely amount of incentives to be provided to customers.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(u) Revenue Recognition—continued

Membership services

The Company offers membership services to subscribing members with various privileges, which primarily include access to exclusive and ad-free streaming of premium content 1080P/4K high-definition video, Dolby Audio, and accelerated downloads and others, or personal cloud services, in exchange for non-refundable upfront membership fees. When the receipt of membership fees is for services to be delivered over a period of time, the receipt is initially recorded as “Customer deposits and deferred revenue” and revenue is recognized ratably over the membership period as services are rendered. Membership services revenue also includes fees earned from subscribing members for on-demand content purchases and early access to premium content. The Company is the principal in its relationships where partners, including consumer electronics manufacturers (TVs and cell phones), mobile operators, internet service providers and online payment agencies, provide access to the membership services or payment processing services as the Company retains control over its service delivery to its subscribing members. Typically, payments made to the partners, are recorded as “Cost of revenues”. For the sale of the right to other membership services through strategic cooperation with other parties, the Company recognizes revenue on a net basis when the Company does not control the specified services before they are transferred to the customer.

Content distribution

The Company generates revenues from sub-licensing content licensed from vendors for cash or through nonmonetary exchanges mainly with other online video broadcasting companies. The exclusive licensing agreements the Company enters into with the vendors have a specified license period and provides the Company rights to sub-license these contents to other parties. The Company enters into a non-exclusive sub-license agreement with a sub-licensee for a period that falls within the original exclusive license period. For cash sub-licensing transactions, the Company is entitled to receive the sub-license fee under the sub-licensing arrangements and does not have any future obligation once it has provided the underlying content to the sub-licensee (which is provided at or before the beginning of the sub-license period). The sub-licensing of content represents a license of functional intellectual property which grants a right to use the Company’s licensed copyrights, and is recognized at the point in time when the licensed copyright is made available for the customer’s use and benefit.

The Company also enters into nonmonetary transactions to exchange online broadcasting rights of licensed copyrights with other online video broadcasting companies from time to time. The exchanged licensed copyrights provide rights for each party to broadcast the licensed copyrights received on its own website only. Each transferring party retains the right to continue broadcasting the exclusive content on its own website and/or sublicense the rights to the content it surrendered in the exchange. The Company accounts for these nonmonetary exchanges based on the fair value of the asset received. Barter sublicensing revenues are recognized in accordance with the same revenue recognition criteria above. The Company estimates the fair value of the licensed copyrights received using a market approach based on various factors, including the purchase price of similar non-exclusive and/or exclusive contents, broadcasting schedule, cast and crew, theme, popularity, and box office. The transaction price of nonmonetary exchange revenues is calculated on the individual content asset basis. For a significant nonmonetary exchange, the Company further reviews the fair value by analyzing

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(u) Revenue Recognition—continued

Content distribution—continued

against the cost of the licensed copyrights bartered out and/or engages a third-party valuation firm to assess the reasonableness of its fair value. The attributable cost of sublicensing transactions, whether for cash or through nonmonetary exchanges, is recognized as cost of revenues through the amortization of the sublicensing right component of the exclusive licensed copyright.

The Company recognized barter sublicensing revenues of RMB1.1 billion, RMB683 million and RMB1.4 billion and related costs of RMB1.0 billion, RMB570 million and RMB1.1 billion for the years ended December 31, 2018, 2019 and 2020, respectively.

Cloud Services

The Company provides public cloud services, which include computing database, storage and other services to enterprise and personal customers and allow customers to use hosted software over the contract period without taking possession of the software, generally on either a subscription or consumption basis. The Company also provides proprietary cloud services and solutions which mainly include hardware, software licensing and software installation service. Revenue related to cloud services provided on a subscription basis is recognized ratably over the contract period. Revenue related to cloud services provided on a consumption basis, such as the amount of storage used in a period, is recognized based on the customer utilization of such resources.

Cloud service revenue is recognized over time if one of the following three criteria is met: (i) the customer simultaneously receives and consumes the benefits as the Company performs; (ii) the Company’s performance creates or enhances an asset that the customer controls as the asset is created or enhanced; (iii) the asset delivered has no alternative use and the Company has an enforceable right to payment for performance completed to date. Otherwise, revenue is recognized at a point in time upon customer acceptance of the cloud services.

Sales of hardware

The Company sells hardware products via third party agents or directly to end customers. Revenue from the sales of hardware is recognized when control of the goods is transferred to customers, which generally occurs when the products are delivered and accepted by the customers. Revenue is recorded net of sales incentives and return allowance.

Financial services

The Company offered financial services which included provision of installment payment services to consumers and wealth management services to third-party investors. Interest income earned from provision of financial services was reported as “Other revenues” and reported on a net basis after deduction of related interest costs incurred. The Company recognized gross interest income of RMB3.3 billion and interest costs of RMB1.6 billion for the year ended December 31, 2018. The financial services business was disposed of in August 2018 (Note 4).

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(u) Revenue Recognition—continued

Other revenue recognition related policies

For arrangements that include multiple performance obligations, primarily for advertisements to be displayed in different spots, placed under different forms and displayed at different times and proprietary cloud services, which mainly include hardware, software licensing and software installation service, the Company would evaluate all of the performance obligations in the arrangement to determine whether each performance obligation is distinct. Consideration is allocated to each performance obligation based on its standalone selling price at contract inception. The Company generally determines standalone selling prices based on the prices charged to customers on a standalone basis or estimates it using an expected cost plus margin approach. If a promised good or service does not meet the criteria to be considered distinct, it is combined with other promised goods or services until a distinct bundle of goods or services exists.

Timing of revenue recognition may differ from the timing of invoicing to customers. For certain services, customers are required to pay before the services are delivered to the customer. When either party to a revenue contract has performed, the Company recognizes a contract asset or a contract liability on the consolidated balance sheets, depending on the relationship between the entity’s performance and the customer’s payment.

Contract liabilities were mainly related to fees for membership services to be provided over the membership period, which were presented as “Customer deposits and deferred revenue” on the consolidated balance sheets. Balances of contract liabilities were RMB6.1 billion and RMB6.7 billion as of December 31, 2019 and December 31, 2020, respectively. Revenue recognized for the year ended December 31, 2020 that was included in contract liabilities as of January 1, 2020 was RMB4.0 billion.

Contract assets mainly represent unbilled amounts mainly related to the Company’s rights to consideration for advertising services and cloud services delivered and are included in “Other current assets, net” on the consolidated balance sheets. As of December 31, 2018, 2019 and 2020, contract assets were RMB1.4 billion, RMB1.9 billion and RMB1.8 billion, net of an allowance for credit losses of RMB21 million, RMB7 million and RMB27 million, respectively.

The Company does not disclose the value of unsatisfied performance obligations for (i) contracts with an original expected length of one year or less and (ii) contracts for which the Company recognizes revenue at the amount to which it has the right to invoice for services performed.

The Company’s disaggregated revenues disclosures are presented in Note 24.

(v) Cost of Revenues

Cost of revenues consists primarily of traffic acquisition costs, bandwidth costs, depreciation, content costs, payroll, cost of hardware sold and related costs of operations.

Traffic acquisition costs represent the amounts paid or payable to Baidu Union partners who direct search queries to the Company’s websites or distribute the Company’s customers’ paid links through their properties. These payments are primarily based on revenue sharing arrangements under which the Company pays its Baidu Union partners and other business partners a percentage of the fees it earns from its online marketing customers.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(w) Advertising and Promotional Expenses

Advertising and promotional expenses, including advertisements through various forms of media and kinds of marketing and promotional activities, are included in “Selling, general and administrative expense” in the consolidated statements of comprehensive income (loss) and are expensed when incurred. Advertising and promotional expenses for the years ended December 31, 2018, 2019 and 2020 were RMB10.1 billion, RMB10.5 billion and RMB8.4 billion, respectively.

(x) Research and development expenses

Research and development expenses consist primarily of personnel-related costs. The Company expenses research and development costs as they are incurred, except for (i) costs to develop internal-use software or add significant upgrades and enhancements resulting in additional functionality to internal-use software that meet the capitalization criteria in accordance with ASC Subtopic 350-40, *Intangibles-Goodwill and Other, Internal-Use Software*; and (ii) costs incurred to develop software to be sold/licensed or embedded in its products sold to customers, which are capitalized once technology feasibility is established, which is when a completed detail program design of the product is available in accordance with ASC 950-20, *Costs of Software to be Sold, Leased or Marketed*. Capitalized software development costs have not been material for the periods presented.

(y) Government Subsidies

Government subsidies primarily consist of financial subsidies received from provincial and local governments for operating a business in their jurisdictions and compliance with specific policies promoted by the local governments. For certain government subsidies, there are no defined rules and regulations to govern the criteria necessary for companies to receive such benefits, and the amount of financial subsidy is determined at the discretion of the relevant government authorities. The government subsidies of non-operating nature with no further conditions to be met are recorded as non-operating income in “Others, net” in the consolidated statements of comprehensive income (loss) when received. The government subsidies with certain operating conditions are recorded as “Deferred income” when received and is recognized as income in “Others, net” or as a reduction of specific operating costs and expenses when the conditions are met for which the grants are intended to compensate.

(z) Income Taxes

The Company recognizes income taxes under the liability method. Deferred income taxes are recognized for differences between the financial reporting and tax bases of assets and liabilities at enacted tax rates in effect for the years in which the differences are expected to reverse. The Company records a valuation allowance against the amount of deferred tax assets that it determines is not more-likely-than-not to be realized. The effect on deferred taxes of a change in tax rates is recognized in earnings in the period that includes the enactment date.

Deferred income taxes are recognized on the undistributed earnings of subsidiaries, which are presumed to be transferred to the parent company and are subject to withholding taxes, unless there is sufficient evidence to show that the subsidiary has invested or will invest the undistributed earnings indefinitely or that the earnings will be remitted in a tax-free liquidation.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(z) Income Taxes—continued

The Company applies the provisions of ASC Topic 740, *Income Taxes* (“ASC 740”), in accounting for uncertainty in income taxes. ASC 740 clarifies the accounting for uncertainty in income taxes by prescribing the recognition threshold a tax position is required to meet before being recognized in the financial statements. The Company has elected to classify interest and penalties related to an uncertain tax position (if and when required) as part of income tax expense in the consolidated statements of comprehensive income (loss).

(aa) Share-based Compensation

The Company accounts for share-based compensation in accordance with ASC Topic 718, *Compensation-Stock Compensation* (“ASC 718”). The Company has elected to recognize share-based compensation using the straight-line method for all share-based awards issued with no performance conditions. For awards with performance conditions, compensation cost is recognized on an accelerated basis if it is probable that the performance condition will be achieved.

Forfeitures are estimated based on historical experience and are periodically reviewed. Cancellation of an award accompanied by the concurrent grant of a replacement award is accounted for as a modification of the terms of the cancelled award (“modified awards”). The compensation costs associated with the modified awards are recognized if either the original vesting condition or the new vesting condition is achieved. Total recognized compensation cost for the awards is at least equal to the fair value of the awards at the grant date unless at the date of the modification the performance or service conditions of the original awards are not expected to be satisfied. The incremental compensation cost is measured as the excess of the fair value of the replacement award over the fair value of the cancelled award at the cancellation date. Therefore, in relation to the modified awards, the Company recognizes share-based compensation over the vesting periods of the replacement award, which comprises, (i) the amortization of the incremental portion of share-based compensation over the remaining vesting term and (ii) any unrecognized compensation cost of the original award, using either the original term or the new term, whichever results in higher expenses for each reporting period.

The Company adopted ASU No. 2018-07, *Compensation—Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting to simplify the accounting for share-based payments to nonemployees* (“ASU 2018-07”) on January 1, 2019 using the modified retrospective method. Subsequent to the adoption, the Company measures equity-classified nonemployee awards using their fair value on grant date. The impact of adopting ASU 2018-07 was insignificant.

(bb) Earnings Per Share (“EPS”)

The Company computes earnings per Class A and Class B ordinary shares in accordance with ASC Topic 260, *Earnings Per Share* (“ASC 260”), using the two-class method. Under the provisions of ASC 260, basic earnings per share is computed using the weighted average number of ordinary shares outstanding during the period except that it does not include unvested ordinary shares subject to repurchase or cancellation. The Company’s outstanding Class A and Class B ordinary shares were retroactively adjusted for the Share Subdivision as disclosed in Note 2.(a) and Note 21. The Company adjusts for the accretion of the redeemable noncontrolling interests in the calculation of income available to ordinary shareholders of the Company used in the earnings per share calculation.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(bb) Earnings Per Share (“EPS”)—continued

Diluted earnings per share is computed using the weighted average number of ordinary shares and, if dilutive, potential ordinary shares outstanding during the period. Potentially dilutive securities such as stock options, restricted shares and convertible senior notes have been excluded from the computation of diluted net income per share if their inclusion is anti-dilutive. Potential ordinary shares consist of the incremental ordinary shares issuable upon the exercise of stock options, restricted shares subject to forfeiture, and contracts that may be settled in the Company’s stock or cash. The dilutive effect of outstanding stock options and restricted shares is reflected in diluted earnings per share by application of the treasury stock method. The computation of the diluted earnings per Class A ordinary share assumes the conversion of Class B ordinary shares to Class A ordinary shares, while diluted earnings per Class B ordinary share does not assume the conversion of such shares. The Company adjusts for the securities issued by subsidiaries and equity method investees in the calculation of income available to ordinary shareholders of the Company used in the diluted earnings per share calculation.

The liquidation and dividend rights of the holders of the Company’s Class A and Class B ordinary shares are identical, except with respect to voting rights. As a result, and in accordance with ASC 260, the undistributed earnings for each year are allocated based on the contractual participation rights of the Class A and Class B ordinary shares as if the earnings for the year had been distributed. As the liquidation and dividend rights are identical, the undistributed earnings are allocated on a proportionate basis. Further, as the conversion of Class B ordinary shares is assumed in the computation of the diluted earnings per Class A ordinary share, the undistributed earnings are equal to net income for that computation.

For the purposes of calculating the Company’s basic and diluted earnings per Class A and Class B ordinary shares, the ordinary shares relating to the options that were exercised are assumed to have been outstanding from the date of exercise of such options.

(cc) Contingencies

The Company records accruals for certain of its outstanding legal proceedings or claims when it is probable that a liability will be incurred and the amount of loss can be reasonably estimated. The Company evaluates, on a quarterly basis, developments in legal proceedings or claims that could affect the amount of any accrual, as well as any developments that would make a loss contingency both probable and reasonably estimable. The Company discloses the amount of the accrual if it is material.

When a loss contingency is not both probable and estimable, the Company does not record an accrued liability but discloses the nature and the amount of the claim, if material. However, if the loss (or an additional loss in excess of the accrual) is at least reasonably possible, then the Company discloses an estimate of the loss or range of loss, unless it is immaterial or an estimate cannot be made. The assessment of whether a loss is probable or reasonably possible, and whether the loss or a range of loss is estimable, often involves complex judgments about future events. Management is often unable to estimate the loss or a range of loss, particularly where (i) the damages sought are indeterminate, (ii) the proceedings are in the early stages, or (iii) there is a lack of clear or consistent interpretation of laws specific to the industry-specific complaints among different jurisdictions. In such cases, there is considerable uncertainty regarding the timing or ultimate resolution of such matters, including eventual loss, fine, penalty or business impact, if any.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(dd) Concentration of Risks

Concentration of credit risk

Financial instruments that potentially subject the Company to significant concentration of credit risk primarily consist of cash and cash equivalents, restricted cash, debt investments, accounts receivable, contract assets, receivables from online payment agencies and amounts due from related parties. As of December 31, 2020, the Company has RMB172.7 billion in cash and cash equivalents, restricted cash, and debt investments, 90% and 10% of which are held by financial institutions in the PRC and international financial institutions outside of the PRC, respectively. The Company’s total cash and cash equivalents, restricted cash, and debt investments held at four financial institutions in the PRC exceeded 10%, representing 30%, 21%, 16% and 11% of the Company’s total cash and cash equivalents, restricted cash, and debt investments as of December 31, 2020, respectively.

PRC state-owned banks, such as Bank of China, are subject to a series of risk control regulatory standards, and PRC bank regulatory authorities are empowered to take over the operation and management when any of those banks faces a material credit crisis. The Company does not foresee substantial credit risk with respect to cash and cash equivalents, restricted cash and short-term investments held at the PRC state-owned banks. Meanwhile, China does not have an official deposit insurance program, nor does it have an agency similar to what was the Federal Deposit Insurance Corporation (FDIC) in the U.S. In the event of bankruptcy of one of the financial institutions in which the Company has deposits or investments, it may be unlikely to claim its deposits or investments back in full. The Company selected reputable international financial institutions with high rating rates to place its foreign currencies. The Company regularly monitors the rating of the international financial institutions to avoid any potential defaults. There has been no recent history of default in relation to these financial institutions.

Accounts receivable, contract assets, receivables from online payment agencies and amounts due from related parties are typically unsecured and derived from revenue earned from customers and agents in China, which are exposed to credit risk. The risk is mitigated by credit evaluations the Company performs on its customers and its ongoing monitoring process of outstanding balances. The Company maintains reserves for estimated credit losses and these losses have generally been within its expectations. As of December 31, 2018, 2019 and 2020, the Company had no single customer with a receivable balance exceeding 10% of the total accounts receivable balance.

No customer or any Baidu Union partner generated greater than 10% of total revenues in any of the three years presented.

Amounts due from related parties are typically unsecured. In evaluating the collectability of the amounts due from related parties, the Company considers many factors, including the related parties’ repayment history and their credit-worthiness. The Company maintains reserves for estimated credit losses and these losses have generally been within its expectations.

Business and economic risks

The Company participates in the dynamic and competitive high technology industry and believes that changes in any of the following areas could have a material adverse effect on the Company’s future financial position, results of operations and cash flows: changes in the overall demand for services and

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(dd) Concentration of Risks—continued

Business and economic risks—continued

products; changes in business offerings; competitive pressures due to existing and new entrants; advances and new trends in new technologies and industry standards; changes in bandwidth suppliers; changes in certain strategic relationships or customer relationships; regulatory considerations; copyright regulations; brand maintenance and enhancement; risks associated with the Company’s ability to attract and retain employees necessary to support its growth and risks related to outbreaks of epidemics, such as COVID-19.

The Company’s operations could be adversely affected by significant political, economic and social uncertainties, epidemic and trade war disruptions in the PRC.

Currency convertibility risk

Substantially all of the Company’s businesses are transacted in RMB, which is not freely convertible into foreign currencies. All foreign exchange transactions take place either through Bank of China or other banks authorized to buy and sell foreign currencies at the exchange rates quoted by the People’s Bank of China. Foreign exchange transactions, including foreign currency payments, require the approval of the People’s Bank of China and/or regulatory institutions.

Foreign currency exchange rate risk

The functional currency and the reporting currency of the Company are the USD and the RMB, respectively. The Company’s exposure to foreign currency exchange rate risk primarily relates to cash and cash equivalents, restricted cash, short-term investments, long-term investments, accounts and notes payable and convertible senior notes denominated in the USD. On June 19, 2010, the People’s Bank of China announced the end of the RMB’s de facto peg to the USD, a policy which was instituted in late 2008 in the face of the global financial crisis, to further reform the RMB exchange rate regime and to enhance the RMB’s exchange rate flexibility. On March 15, 2014, the People’s Bank of China announced the widening of the daily trading band for RMB against USD. The depreciation of the USD against the RMB was approximately 6.27% in 2020. Most of the revenues and costs of the Company are denominated in RMB, while a portion of cash and cash equivalents, restricted cash, short-term investments, long-term investments, notes payable and convertible senior notes are denominated in the USD. It is difficult to predict how market forces or PRC or U.S. government policy may impact the exchange rate between the Renminbi and the U.S. dollar in the future. Any significant fluctuation of the valuation of RMB may materially affect the Company’s cash flows, revenues, earnings and financial position, and the value of, and any dividends payable on, the ADS in USD.

(ee) Derivative Instruments

ASC Topic 815, *Derivatives and Hedging* (“ASC 815”), requires all contracts which meet the definition of a derivative to be recognized on the balance sheet as either assets or liabilities and recorded at fair value. Changes in the fair value of derivative financial instruments are either recognized periodically in earnings or in other comprehensive income (loss) depending on the use of the derivative and whether it qualifies for hedge accounting. Changes in fair values of derivatives not qualified as hedges are reported in earnings.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—continued

(ff) Recent Accounting Pronouncements

In January 2020, the FASB issued ASU No. 2020-01, *Investments—Equity Securities* (Topic 321), *Investments—Equity Method and Joint Ventures* (Topic 323), and *Derivatives and Hedging* (Topic 815)—*Clarifying the Interactions between Topic 321, Topic 323, and Topic 815 (a consensus of the FASB Emerging Issues Task Force)* (“ASU 2020-01”), which clarifies the interactions of the accounting for certain equity securities under ASC 321, investments accounted for under the equity method of accounting in ASC 323, and the accounting for certain forward contracts and purchased options accounted for under ASC 815. ASU 2020-01 could change how an entity accounts for (i) an equity security under the measurement alternative and (ii) a forward contract or purchased option to purchase securities that, upon settlement of the forward contract or exercise of the purchased option, would be accounted for under the equity method of accounting or the fair value option in accordance with ASC 825. These amendments improve current U.S. GAAP by reducing diversity in practice and increasing comparability of the accounting for these interactions. The new guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 31, 2020. Early adoption is permitted. The Company is currently in the process of evaluating the of adopting ASU 2020-01 on its consolidated financial statements and related disclosure.

In August 2020, the FASB issued ASU No. 2020-06, *Accounting for Convertible Instruments and Contracts in an Entity’s Own Equity* (“ASU 2020-06”), which focuses on amending the legacy guidance on convertible instruments and the derivatives scope exception for contracts in an entity’s own equity. ASU 2020-06 simplifies an issuer’s accounting for convertible instruments by reducing the number of accounting models that require separate accounting for embedded conversion features. ASU 2020-06 also simplifies the settlement assessment that entities are required to perform to determine whether a contract qualifies for equity classification. Further, ASU 2020-06 enhances information transparency by making targeted improvements to the disclosures for convertible instruments and earnings-per-share (EPS) guidance, i.e., aligning the diluted EPS calculation for convertible instruments by requiring that an entity use the if-converted method and that the effect of potential share settlement be included in the diluted EPS calculation when an instrument may be settled in cash or shares, adding information about events or conditions that occur during the reporting period that cause conversion contingencies to be met or conversion terms to be significantly changed. This update will be effective for the Company’s fiscal years beginning after December 15, 2021, and interim periods within those fiscal years. Early adoption is permitted, but no earlier than fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. Entities can elect to adopt the new guidance through either a modified retrospective method of transition or a fully retrospective method of transition. The Company is currently in the process of evaluating the impact of adopting ASU 2020-06 on its consolidated financial statements and related disclosure.

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

3. BUSINESS COMBINATIONS

Business combinations in 2018:

During the year ended December 31, 2018, the Company completed several business combinations, to complement its existing businesses and achieve synergies. The acquired entities individually and in aggregate were insignificant. Results of the acquired entities’ operations have been included in the Company’s consolidated financial statements since the acquisition dates.

| | RMB (In millions) |
|---|----------------------|
| Purchase consideration | 2,378 |
| Net assets acquired, excluding intangible assets and the related deferred tax liabilities | 1,545 |
| Intangible assets, net | 1,424 |
| Deferred tax liabilities | (292) |
| Pre-existing equity interests | (1,651) |
| Noncontrolling interests | (1,312) |
| Redeemable non-controlling interests (Note 19) | (698) |
| Goodwill | 3,362 |
| | <u>2,378</u> |

The aggregate purchase price allocation includes acquisition of certain acquirees, which were equity method investees of the Company prior to the acquisitions. In aggregate, a re-measurement gain relating to the Company’s pre-existing equity interest of RMB630 million was recognized during the year ended December 31, 2018. The Company applied the equity method of accounting by recognizing its share of the profit or loss in these equity method investees up to their respective dates of acquisition.

Goodwill, which is non-deductible for tax purposes, is primarily attributable to the synergies expected to be achieved from the acquisitions.

Neither the results of operations since the acquisition dates nor the pro forma results of operations of the acquirees were presented because the effects of these business combinations, individually and in the aggregate, were not significant to the Company’s consolidated results of operations.

Business combinations in 2019:

During the year ended December 31, 2019, the Company completed several business combinations, total purchase consideration in aggregate was RMB1.2 billion, among which RMB978 million was allocated to goodwill. The Company expects to achieve significant synergies from such acquisitions which it plans to complement its existing businesses. The acquired entities were considered insignificant, both individually and in aggregate. Results of the acquired entities’ operations have been included in the Company’s consolidated financial statements since the acquisition date.

| | RMB (In millions) |
|---|----------------------|
| Purchase consideration | 1,168 |
| Net assets acquired, excluding intangible assets and the related deferred tax liabilities | 229 |
| Intangible assets, net | 543 |
| Deferred tax liabilities | (134) |
| Noncontrolling interests | (266) |
| Redeemable non-controlling interests (Note 19) | (182) |
| Goodwill | 978 |
| | <u>1,168</u> |

Goodwill, which is non-deductible for tax purposes, is primarily attributable to the synergies expected to be achieved from the acquisitions.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

3. BUSINESS COMBINATIONS—continued

Business combinations in 2019—continued:

Neither the results of operations since the acquisition dates nor the pro forma results of operations of the acquirees were presented because the effects of these business combinations, individually and in the aggregate, were not significant to the Company’s consolidated results of operations.

Business combinations in 2020:

During the year ended December 31, 2020, the Company completed several business combinations, total purchase consideration in aggregate was RMB3.5 billion, among which RMB4.0 billion was allocated to goodwill. The Company expects to achieve significant synergies from such acquisitions which it plans to complement its existing businesses. The acquired entities were considered insignificant, both individually and in aggregate. Results of the acquired entities’ operations have been included in the Company’s consolidated financial statements since the acquisition date.

| | <u>RMB</u> (In millions) |
|---|-----------------------------|
| Purchase consideration | 3,499 |
| Net assets acquired, excluding intangible assets and the related deferred tax liabilities | 1,515 |
| Intangible assets, net | 1,116 |
| Deferred tax liabilities | (229) |
| Pre-existing equity interests and debt investment | (2,103) |
| Noncontrolling interests | (798) |
| Goodwill | 3,998 |
| | <u>3,499</u> |

The Company’s pre-existing equity interests in the acquired entities were remeasured to fair value at the acquisition date. For the year ended December 31, 2020, the Company recognized a net re-measurement gain of RMB123 million in “Others, net” in the consolidated statement of comprehensive income.

Goodwill, which is non-deductible for tax purposes, is primarily attributable to the synergies expected to be achieved from the acquisitions.

Neither the results of operations since the acquisition dates nor the pro forma results of operations of the acquirees were presented because the effects of these business combinations, both individually and in aggregate, were not significant to the Company’s consolidated results of operations.

The valuations used in the purchase price allocation described above were determined by the Company with the assistance of independent third-party valuation firm. The valuation reports considered generally accepted valuation methodologies such as the income, market and cost approaches. As the acquirees are all private companies, the fair value estimates of pre-existing equity interests and debt investment or noncontrolling interests are based on significant inputs considered by market participants which mainly include (a) discount rate, (b) projected terminal value based on future cash flows, (c) equity multiples or enterprise value multiples of companies in the same industries and (d) adjustment for lack of control or lack of marketability.

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

4. INVESTMENTS

Short-term Investments

As of December 31, 2018, 2019 and 2020, the Company’s short-term investments comprised of only debt securities. Short-term held-to-maturity securities were mainly deposits in commercial banks with maturities less than one year and wealth management products issued by commercial banks and other financial institutions for which the Company has the positive intent and ability to hold those securities to maturity. The short-term available-for-sale securities include wealth management products issued by commercial banks and other financial institutions which are not classified as trading securities or as held-to-maturity securities.

During the years ended December 31, 2018, 2019 and 2020, the Company recorded interest income from its short-term investments of RMB3.9 billion, RMB5.4 billion and RMB4.7 billion in the consolidated statements of comprehensive income (loss), respectively.

Short-term investments classification as of December 31, 2018, 2019 and 2020 were shown as below:

| | As of December 31, 2018 | | | | | |
|---|-------------------------|----------------------------------|-----------------------------------|------------------------|-------------------------|------------|
| | Cost or Amortized cost | Gross unrecognized holding gains | Gross unrecognized holding losses | Gross unrealized gains | Gross unrealized losses | Fair value |
| | RMB | RMB | RMB (In millions) | RMB | RMB | RMB |
| Held-to-maturity debt investments | 27,388 | 119 | — | — | — | 27,507 |
| Available-for-sale debt investments | 83,100 | — | — | 1,216 | (78) | 84,238 |
| | As of December 31, 2019 | | | | | |
| | Cost or Amortized cost | Gross unrecognized holding gains | Gross unrecognized holding losses | Gross unrealized gains | Gross unrealized losses | Fair value |
| | RMB | RMB | RMB (In millions) | RMB | RMB | RMB |
| Held-to-maturity debt investments | 107,287 | 367 | — | — | — | 107,654 |
| Available-for-sale debt investments | 5,440 | — | — | 197 | — | 5,637 |
| | As of December 31, 2020 | | | | | |
| | Cost or Amortized cost | Gross unrecognized holding gains | Gross unrecognized holding losses | Gross unrealized gains | Gross unrealized losses | Fair value |
| | RMB | RMB | RMB (In millions) | RMB | RMB | RMB |
| Held-to-maturity debt investments | 123,537 | 595 | — | — | — | 124,132 |
| Available-for-sale debt investments | 2,862 | — | — | 3 | — | 2,865 |

Long-term Investments

The following table sets forth a breakdown of the categories of long-term investments held by the Company as of the dates indicated:

| | As of December 31, | | |
|---|--------------------|----------------------|---------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB (In millions) | RMB |
| Equity investments at fair value with readily determinable fair value | 4,428 | 11,334 | 12,978 |
| Available-for-sale debt investment | 1,167 | 3,970 | 2,607 |
| Equity investments without readily determinable fair value | 29,269 | 24,686 | 24,603 |
| Equity method investments | 44,133 | 27,105 | 24,067 |
| Investments accounted for at fair value | 1,457 | 1,819 | 2,238 |
| Long-term held-to-maturity investments | — | 496 | 9,740 |
| Total | <u>80,454</u> | <u>69,410</u> | <u>76,233</u> |

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

4. INVESTMENTS—continued

Long-term Investments—continued

Equity investments at fair value with readily determinable fair value

Equity investments at fair value with readily determinable fair value represent investments in the equity securities of publicly listed companies, for which the Company does not have significant influence.

In 2017, the Company acquired equity interests in China United Network Communication Limited (“China Unicom”), a listed telecommunications company in China for cash consideration of RMB7.0 billion. The China Unicom investment was held by a non-wholly-owned subsidiary of the Company. As the China Unicom investment was subject to a three-year holding requirement, it was accounted for using the measurement alternative in 2018 and as an equity investment with readily determinable fair value in 2019 as the holding restrictions terminate within one year. In 2020, the Company partially disposed its investment in China Unicom for RMB 2.7 billion, which was subsequently distributed to noncontrolling shareholder in January 2021.

Equity investments without readily determinable fair value

In accordance with ASC 321, the Company elected to use the measurement alternative to measure such investments at cost, less any impairment, plus or minus changes resulting from observable price changes in orderly transactions for identical or similar investments of the same issuer, if any. Impairment charges recognized on equity investments without readily determinable fair value was RMB455 million, RMB778 million and RMB2.3 billion for the years ended December 31, 2018, 2019 and 2020, respectively.

The total carrying value of equity investments without readily determinable fair value held as of December 31, 2018, 2019 and 2020 were as follows:

| | As of December 31, 2018 | As of December 31, 2019 | As of December 31, 2020 |
|---|-------------------------------|-------------------------------|-------------------------------|
| | RMB | RMB (In millions) | RMB |
| Initial cost basis | 26,728 | 21,211 | 19,725 |
| Cumulative unrealized gains | 6,271 | 5,636 | 8,113 |
| Cumulative unrealized losses (including impairment) | (3,730) | (2,161) | (3,235) |
| Total carrying value | <u>29,269</u> | <u>24,686</u> | <u>24,603</u> |

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

4. INVESTMENTS—continued

Long-term Investments—continued

Equity investments without readily determinable fair value—continued

Total unrealized and realized gains and losses of equity securities without readily determinable fair values in 2018, 2019 and 2020 were as follows:

| | For the years ended December 31, | | |
|---|-------------------------------------|----------------------|--------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB (In millions) | RMB |
| Gross unrealized gains | 7,119 | 1,447 | 4,396 |
| Gross unrealized losses (including impairment) (i) | (2,867) | (1,641) | (2,679) |
| Net unrealized gains (losses) on equity securities held | 4,252 | (194) | 1,717 |
| Net realized gains on equity securities sold | 124 | 211 | 266 |
| Total net gains recognized in other income, net | <u>4,376</u> | <u>17</u> | <u>1,983</u> |

Note:

(i) Gross unrealized losses (downward adjustments excluding impairment) were RMB2.4 billion, RMB863 million and RMB378 million for the years ended December 31, 2018, 2019 and 2020, respectively.

Equity method investments

The carrying amounts of the Company’s equity method investments were RMB44.1 billion, RMB27.1 billion and RMB24.1 billion as of December 31, 2018, 2019 and 2020, respectively. For the years ended December 31, 2018, 2019 and 2020, the impairment recognized for equity method investments were RMB167 million, RMB9.2 billion and RMB297 million, respectively.

Equity Investment in Trip.com International, Ltd. (“Trip”) (formally known as Ctrip)

As of December 31, 2018, the Company held approximately 19% of Trip’s outstanding shares. The Company is considered to have significant influence over Trip and accounts for such investment as an equity method investment in accordance with ASC 323.

During 2019, the market value of Trip had significantly declined and remained below the carrying value of the investment for a prolonged period of time. Therefore, the Company concluded that the decline in market value of the investment in Trip was other-than-temporary as of September 30, 2019 and an impairment charge of RMB8.9 billion was recorded in the third quarter of 2019. The Company made a corresponding RMB 8.9 billion downward adjustment to the equity method goodwill arising from its acquisition of the Trip investment.

In October 2019, the Company disposed an aggregate of 36 million American Depositary Shares of Trip for cash consideration of US\$988 million and recognized a disposal loss of RMB43 million in the year ended December 31, 2019.

The carrying amount of the Company held the interests in Trip was RMB30.5 billion, RMB14.1 billion and RMB12.6 billion as of December 31, 2018, 2019 and 2020, respectively.

After the partial disposal of the investment in Trip the Company held approximately 12% equity interest in Trip, and the Company can actively participate in the operating and financing policies of

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

4. INVESTMENTS—continued

Long-term Investments—continued

Equity method investments—continued

Equity Investment in Trip.com International, Ltd. (“Trip”) (formally known as Ctrip)—continued

Trip through its two seats on Trip’s board of directors with a total of nine members. Accordingly, the Company continues to have significant influence over Trip and accounts for its remaining investment as an equity method investment in accordance with ASC 323. As of December 31, 2020, the Company’s investments in Trip had a fair value of RMB15.2 billion, based on the closing share price.

The following tables set forth the summarized financial information of Trip:

| | As of September 30, ⁽ⁱ⁾ | | |
|--------------------------|------------------------------------|----------------------|---------|
| | 2018 | 2019 ⁽ⁱⁱ⁾ | 2020 |
| | RMB | RMB (In millions) | RMB |
| Current assets | 84,464 | 75,578 | 65,782 |
| Non-current assets | 104,906 | 127,505 | 132,417 |
| Current liabilities | 69,065 | 74,118 | 61,360 |
| Non-current liabilities | 30,318 | 25,134 | 36,558 |
| Noncontrolling interests | 2,231 | 2,047 | 1,566 |

| | For the twelve months ended September 30, ⁽ⁱ⁾ | | |
|---|---|----------------------|---------|
| | 2018 ⁽ⁱⁱ⁾ | 2019 ⁽ⁱⁱ⁾ | 2020 |
| | RMB | RMB (In millions) | RMB |
| Total revenues | 29,944 | 34,958 | 21,704 |
| Gross profit | 24,019 | 27,627 | 16,838 |
| Income (loss) from operations | 3,302 | 4,271 | (827) |
| Net income (loss) | 2,807 | 3,764 | (2,236) |
| Net income (loss) attributable to the investees | 2,806 | 3,813 | (2,243) |

Notes:

- (i) The Company adopted a one-quarter lag in reporting its share of equity income (loss) in Trip.
- (ii) Trip adopted ASC 606, on a fully retrospective basis, and ASC 321 (collectively “new standards”) from January 1, 2018. The impact of the new standards on the Company’s financial statements was immaterial, and prior period financial information of Trip was not restated.

Disposal of financial services business

In April 2018, the Company entered into definitive agreements relating to the disposal of its wholly-owned financial services business, which provided consumer credit, wealth management and other financial services. To facilitate the divestiture, the Company conducted a series of legal restructuring and recapitalization of entities conducting the financial services business (“Du Xiaoman”), which were accounted for as transactions under common control.

In August 2018, Du Xiaoman issued preferred shares to third-party investors, which resulted in the Company becoming a minority shareholder of Du Xiaoman. Accordingly, Du Xiaoman was deconsolidated from the Group and a disposal gain of RMB5.5 billion was recognized in “Others, net” including RMB4.2 billion relates to the re-measurement of the Company’s retained equity interest in Du Xiaoman. The disposal of Du Xiaoman did not meet the definition of a discontinued operation per ASC Subtopic 205-20, *Presentation of Financial Statements—Discontinued Operations*, as the divestiture did not represent a shift in strategy nor had a major impact to the Group’s operation and financial results.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

4. INVESTMENTS—continued

Long-term Investments—continued

Equity method investments—continued

Disposal of financial services business—continued

The Company retained an equity interest of 41% on a fully diluted basis, and accounted for Du Xiaoman as an equity method investment in accordance with ASC 323, as it retained significant influence over Du Xiaoman. The carrying amount of the Du Xiaoman investment in excess of the Company’s proportionate interest in Du Xiaoman was recognized as equity method goodwill of RMB3.5 billion, intangible assets of RMB851 million and related deferred tax liabilities of RMB213 million.

Deconsolidation of one of the Company’s subsidiaries

In December 2019, the Company lost control and therefore deconsolidated one of its subsidiaries. A non-cash disposal loss of RMB801 million was recognized in “Others, net” in the consolidated statement of comprehensive loss for the year ended December 31, 2019. The Company continued to have significant influence over the entity and accounted for its remaining equity interest in the entity as an equity-method investment in accordance with ASC 323.

As of December 31, 2018, 2019 and 2020, in addition to the aforementioned equity method investments, the Company held other equity method investments through its subsidiaries or VIEs and over which had significant influence.

For the year ended December 31, 2020, equity method investments excluding Trip held by the Company in aggregate have met the significance criteria as defined under Rule 4-08(g) of Regulation S-X. Financial information for the Company’s equity method investments other than Trip are summarized as a group as follow:

| | As of September 30, | | |
|--|--|----------------------|---------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB (In millions) | RMB |
| Current assets | 100,313 | 86,713 | 96,713 |
| Non-current assets | 11,050 | 18,980 | 15,094 |
| Current liabilities | 78,935 | 65,450 | 73,842 |
| Non-current liabilities | 2,718 | 8,677 | 5,545 |
| Noncontrolling interests | 1,706 | 1,498 | 1,577 |
| | For the twelve months ended September 30, ⁽ⁱ⁾ | | |
| | 2018 | 2019 | 2020 |
| | RMB | RMB (In millions) | RMB |
| Total revenues | 4,633 | 12,598 | 13,981 |
| Gross profit | 916 | 6,247 | 5,083 |
| Loss from operations | (418) | (680) | (1,282) |
| Net loss | (372) | (638) | (832) |
| Net loss attributable to the investees | (352) | (933) | (891) |

Note:

(i) The Company adopted a one-quarter lag in reporting its share of losses in all of its equity investees.

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

4. INVESTMENTS—continued

Long-term Investments—continued

Investments accounted for at fair value

Long-term equity investments in unlisted companies held by consolidated investment companies are accounted for at fair value in accordance with ASC 946-320. These investments are carried at fair value with realized or unrealized gains and losses recorded in “Others, net” in the consolidated statements of comprehensive income (loss).

The methodology used in the determination of fair values for held-to-maturity debt investments, available-for-sale debt investments, equity investments with readily determinable fair values and other investment securities accounted for at fair value are disclosed in Note 25.

Long-term investments classification, excluding equity method investments and equity investments without readily determinable fair value, as of December 31, 2018, 2019 and 2020 are shown as below:

| | As of December 31, 2018 | | | | | |
|---|-------------------------|----------------------------------|-----------------------------------|------------------------|-------------------------|------------|
| | Cost or Amortized cost | Gross unrecognized holding gains | Gross unrecognized holding losses | Gross unrealized gains | Gross unrealized losses | Fair value |
| | RMB | RMB | RMB | RMB | RMB | RMB |
| | (In millions) | | | | | |
| Equity investments at fair value with readily determinable fair value | 5,605 | — | — | 664 | (1,841) | 4,428 |
| Available-for-sale debt investment | 1,167 | — | — | — | — | 1,167 |
| Investments accounted for at fair value . . . | 1,139 | — | — | 318 | — | 1,457 |

| | As of December 31, 2019 | | | | | |
|---|-------------------------|----------------------------------|-----------------------------------|------------------------|-------------------------|------------|
| | Cost or Amortized cost | Gross unrecognized holding gains | Gross unrecognized holding losses | Gross unrealized gains | Gross unrealized losses | Fair value |
| | RMB | RMB | RMB | RMB | RMB | RMB |
| | (In millions) | | | | | |
| Equity investments at fair value with readily determinable fair value | 11,769 | — | — | 2,195 | (2,630) | 11,334 |
| Available-for-sale debt investments | 3,913 | — | — | 138 | (81) | 3,970 |
| Investments accounted for at fair value | 1,309 | — | — | 597 | (87) | 1,819 |

| | As of December 31, 2020 | | | | | |
|---|-------------------------|----------------------------------|-----------------------------------|------------------------|-------------------------|------------|
| | Cost or Amortized cost | Gross unrecognized holding gains | Gross unrecognized holding losses | Gross unrealized gains | Gross unrealized losses | Fair value |
| | RMB | RMB | RMB | RMB | RMB | RMB |
| | (In millions) | | | | | |
| Equity investments at fair value with readily determinable fair value | 8,419 | — | — | 7,342 | (2,783) | 12,978 |
| Available-for-sale debt investments | 2,804 | — | — | 166 | (363) | 2,607 |
| Investments accounted for at fair value . . . | 1,580 | — | — | 885 | (227) | 2,238 |

Long-term held-to-maturity investments

Long-term held-to-maturity securities were mainly deposits in commercial banks with maturities of greater than one year and wealth management products issued by commercial banks and other financial institutions for which the Company has the positive intent and ability to hold those securities to maturity.

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

4. INVESTMENTS—continued

Long-term Investments—continued

During the years ended December 31, 2018, 2019 and 2020, the Company recorded interest income from its long-term held-to-maturity investments of nil, RMB2 million and RMB118 million in the consolidated statements of comprehensive income (loss), respectively.

Long-term held-to-maturity investments classification as of December 31, 2019 and 2020 were shown as below:

| | As of December 31, 2019 | | | | | Fair value |
|--|-------------------------|----------------------------------|-----------------------------------|------------------------|-------------------------|------------|
| | Cost or Amortized cost | Gross unrecognized holding gains | Gross unrecognized holding losses | Gross unrealized gains | Gross unrealized losses | |
| | RMB | RMB | RMB (In millions) | RMB | RMB | |
| Long-term held-to-maturity investments . . . | 496 | — | (5) | — | — | 491 |

| | As of December 31, 2020 | | | | | Fair value |
|--|-------------------------|----------------------------------|-----------------------------------|------------------------|-------------------------|------------|
| | Cost or Amortized cost | Gross unrecognized holding gains | Gross unrecognized holding losses | Gross unrealized gains | Gross unrealized losses | |
| | RMB | RMB | RMB (In millions) | RMB | RMB | |
| Long-term held-to-maturity investments | 9,740 | 14 | — | — | — | 9,754 |

The following table summarizes the amortized cost of long-term held-to-maturity investments with stated contractual dates, classified by the contractual maturity date of the investments:

| | As of December 31, | |
|--|--------------------|-------|
| | 2019 | 2020 |
| | RMB | RMB |
| | (In millions) | |
| Due in 1 year | — | — |
| Due in 1 year through 2 years | 496 | 9,690 |
| Due in 2 years through 3 years | — | 50 |
| Total | 496 | 9,740 |

Available-for-sale debt investments are convertible debt instruments issued by private companies and an investment in preferred shares that is redeemable at the Company’s option, which are measured at fair value. Investments in preferred shares that are redeemable at the Company’s option have no contractual maturity date.

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

4. INVESTMENTS—continued

Long-term Investments—continued

The following table summarizes the estimated fair value of available-for-sale debt investments with stated contractual dates, classified by the contractual maturity date of the investments:

| | As of December 31, | | |
|---|--------------------|--------------|--------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| Due in 1 year | — | 505 | — |
| Due in 1 year through 5 years | — | 10 | 1,587 |
| Due in 5 years through 10 years | — | 1,486 | — |
| Not due at a single maturity date | 1,167 | 1,969 | 1,020 |
| Total | <u>1,167</u> | <u>3,970</u> | <u>2,607</u> |

5. LICENSED COPYRIGHTS, NET

| | As of December 31, 2018 | | | |
|--|-------------------------|--------------------------|-------------------|--------------------|
| | Gross carrying value | Accumulated amortization | Impairment amount | Net carrying value |
| | RMB | RMB | RMB | RMB |
| | (In millions) | | | |
| Licensed copyrights | | | | |
| —Broadcasting rights | 24,569 | (16,860) | (136) | 7,573 |
| —Sublicensing rights | 3,466 | (3,234) | — | 232 |
| | <u>28,035</u> | <u>(20,094)</u> | <u>(136)</u> | <u>7,805</u> |
| Less: current portion: | | | | |
| —Broadcasting rights | 6,589 | (5,546) | (111) | 932 |
| —Sublicensing rights | 3,466 | (3,234) | — | 232 |
| | <u>10,055</u> | <u>(8,780)</u> | <u>(111)</u> | <u>1,164</u> |
| Licensed copyrights—non-current | | | | |
| —Broadcasting rights | 17,980 | (11,314) | (25) | 6,641 |
| —Sublicensing rights | — | — | — | — |
| | <u>17,980</u> | <u>(11,314)</u> | <u>(25)</u> | <u>6,641</u> |

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

5. LICENSED COPYRIGHTS, NET—continued

| | As of December 31, 2019 | | | |
|--|-------------------------|--------------------------|-------------------|--------------------|
| | Gross carrying value | Accumulated amortization | Impairment amount | Net carrying value |
| | RMB | RMB | RMB | RMB |
| | (In millions) | | | |
| Licensed copyrights | | | | |
| —Broadcasting rights | 32,038 | (24,501) | (25) | 7,512 |
| —Sublicensing rights | 4,633 | (4,633) | — | — |
| | <u>36,671</u> | <u>(29,134)</u> | <u>(25)</u> | <u>7,512</u> |
| Less: current portion: | | | | |
| —Broadcasting rights | 11,751 | (10,501) | (25) | 1,225 |
| —Sublicensing rights | 4,633 | (4,633) | — | — |
| | <u>16,384</u> | <u>(15,134)</u> | <u>(25)</u> | <u>1,225</u> |
| Licensed copyrights—non-current | | | | |
| —Broadcasting rights | 20,287 | (14,000) | — | 6,287 |
| —Sublicensing rights | — | — | — | — |
| | <u>20,287</u> | <u>(14,000)</u> | <u>—</u> | <u>6,287</u> |
| | | | | |
| | As of December 31, 2020 | | | |
| | Gross carrying value | Accumulated amortization | Impairment amount | Net carrying value |
| | RMB | RMB | RMB | RMB |
| | (In millions) | | | |
| Licensed copyrights | | | | |
| —Broadcasting rights | 37,511 | (29,688) | (353) | 7,470 |
| —Sublicensing rights | 5,963 | (5,963) | — | — |
| | <u>43,474</u> | <u>(35,651)</u> | <u>(353)</u> | <u>7,470</u> |
| Less: current portion: | | | | |
| —Broadcasting rights | 8,661 | (7,592) | (34) | 1,035 |
| —Sublicensing rights | 5,963 | (5,963) | — | — |
| | <u>14,624</u> | <u>(13,555)</u> | <u>(34)</u> | <u>1,035</u> |
| Licensed copyrights—non-current | | | | |
| —Broadcasting rights | 28,850 | (22,096) | (319) | 6,435 |
| —Sublicensing rights | — | — | — | — |
| | <u>28,850</u> | <u>(22,096)</u> | <u>(319)</u> | <u>6,435</u> |

Amortization expense of RMB12.1 billion, RMB12.7 billion and RMB11.5 billion for the years ended December 31, 2018, 2019 and 2020, respectively, was recognized as cost of revenues. Estimated amortization expense relating to the existing licensed copyrights for each of the next three years is as follows:

| | RMB |
|-----------------------|---------------|
| | (In millions) |
| Within 1 year | 3,681 |
| Between 1 and 2 years | 1,351 |
| Between 2 and 3 years | 804 |

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

5. LICENSED COPYRIGHTS, NET—continued

To supplement cash flow disclosure of investing activities in 2018 and 2019, acquisition of licensed copyrights included in current liabilities for the years ended December 31, 2018 and 2019 amounted to RMB6.3 billion and RMB5.5 billion, respectively. Acquisition of licensed copyrights from nonmonetary content exchanges for the years ended December 31, 2018 and 2019 amounted to RMB642 million and RMB968 million, respectively.

6. PRODUCED CONTENT, NET

| | <u>As of December 31,</u> <u>2018</u> |
|--|--|
| | <u>RMB</u> <u>(In millions)</u> |
| Released, less amortization | 553 |
| In production | 2,871 |
| In development | <u>312</u> |
| | <u>3,736</u> |
| | <u>As of December 31,</u> <u>2019</u> |
| | <u>RMB</u> <u>(In millions)</u> |
| Released, less amortization | 892 |
| In production | 3,075 |
| In development | <u>388</u> |
| | <u>4,355</u> |
| | <u>As of December 31,</u> <u>2020</u> |
| | <u>RMB</u> <u>(In millions)</u> |
| Released, less amortization and impairment | |
| —Predominantly monetized with other content assets | 1,857 |
| —Predominantly monetized on its own | <u>78</u> |
| | 1,935 |
| In production, less impairment | |
| —Predominantly monetized with other content assets | 3,742 |
| —Predominantly monetized on its own | <u>82</u> |
| | 3,824 |
| In development, less impairment | |
| —Predominantly monetized with other content assets | 666 |
| —Predominantly monetized on its own | <u>131</u> |
| | 797 |
| Total | <u>6,556</u> |

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

6. PRODUCED CONTENT, NET—continued

Amortization expense of RMB3,024 million and RMB1,095 million was recognized as “Cost of revenues” in the consolidated statement of comprehensive income for the year ended December 31, 2020, for produced content predominantly monetized with other content assets and for produced content predominantly monetized on its own, respectively. Amortization expense for produced content was RMB2,266 million and RMB2,977 million for the years ended December 31, 2018 and 2019, respectively. Estimated amortization expense relating to the existing produced content for each of the next three years is as follows:

| | RMB (In millions) |
|-----------------------------|----------------------|
| Due in 1 year | 827 |
| Between 1 and 2 years | 296 |
| Between 2 and 3 years | 197 |

7. ACCOUNTS RECEIVABLE

| | As of December 31, | | |
|-----------------------------------|--------------------|----------------------|--------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB (In millions) | RMB |
| Accounts receivable | 6,614 | 8,344 | 9,988 |
| Allowance for credit losses | (599) | (928) | (1,320) |
| | <u>6,015</u> | <u>7,416</u> | <u>8,668</u> |

The movements in the allowance for credit losses were as follows:

| | 2018 | 2019 | 2020 |
|-----------------------------------|------------|----------------------|--------------|
| | RMB | RMB (In millions) | RMB |
| Balance as of January 1 | 316 | 599 | 928 |
| Adoption of ASU 2016-13 | — | — | 119 |
| Amounts charged to expenses | 299 | 331 | 455 |
| Amounts written off | (16) | (2) | (182) |
| Balance as of December 31 | <u>599</u> | <u>928</u> | <u>1,320</u> |

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

8. OTHER ASSETS

| | As of December 31, | | |
|--|--------------------|----------------------|---------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB (In millions) | RMB |
| Prepaid expenses | 658 | 955 | 1,109 |
| Advances to suppliers | 1,686 | 964 | 1,053 |
| Receivables from online payment agencies | 892 | 585 | 440 |
| Deposits | 247 | 787 | 437 |
| Prepaid licensed copyrights | 1,176 | 1,225 | 1,035 |
| Contract assets, net ⁽ⁱ⁾ | 1,415 | 1,876 | 1,755 |
| VAT prepayments | 436 | 1,605 | 1,768 |
| Income tax prepayments | 2 | 499 | 130 |
| Others | 329 | 693 | 3,279 |
| Total other current assets | 6,841 | 9,189 | 11,006 |
| Long-term prepaid expenses | 5,331 | 4,176 | 3,084 |
| Others | 710 | 276 | 364 |
| Total other non-current assets | 6,041 | 4,452 | 3,448 |

Note:

- (i) The allowance for credit losses on contract assets was RMB21 million, RMB7 million and RMB27 million as of December 31, 2018, 2019 and 2020, respectively. The amounts charged to expenses for credit losses of contract assets and write-offs charged against the allowance were RMB9 million and nil, respectively, for the year ended December 31, 2020. The effect of adopting ASU 2016-13 was RMB11 million to the opening balance of contract assets, net.

9. FIXED ASSETS

| | As of December 31, | | |
|---|--------------------|----------------------|---------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB (In millions) | RMB |
| Computer equipment | 26,186 | 29,592 | 33,150 |
| Office building | 4,168 | 4,628 | 4,697 |
| Office building related facility, machinery and equipment | 2,168 | 2,317 | 2,442 |
| Vehicles | 190 | 203 | 204 |
| Office equipment | 813 | 944 | 971 |
| Leasehold improvements | 352 | 391 | 386 |
| Construction in progress | 720 | 313 | 454 |
| | 34,597 | 38,388 | 42,304 |
| Accumulated depreciation and impairment | (16,694) | (20,077) | (24,796) |
| | <u>17,903</u> | <u>18,311</u> | <u>17,508</u> |

Depreciation expense, for the years ended December 31, 2018, 2019 and 2020, was RMB3.7 billion, RMB5.6 billion and RMB5.7 billion, respectively. Impairment charges on fixed assets for the years ended December 31, 2018, 2019 and 2020 were not material.

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

10. GOODWILL AND INTANGIBLE ASSETS

Goodwill

The Company had two reporting units, Baidu Core and iQIYI, as of December 31, 2018, 2019 and 2020.

The changes in the carrying amount of goodwill for each reporting unit from 2018 to 2020 was as follows:

| | <u>Baidu Core</u> | <u>iQIYI</u> | <u>Total</u> |
|--|-------------------|--------------|---------------|
| | RMB | RMB | RMB |
| | (In millions) | | |
| Balance at December 31, 2017 | 12,530 | 3,276 | 15,806 |
| Goodwill acquired (Note 3) | 2,750 | 612 | 3,362 |
| Goodwill disposed | (569) | — | (569) |
| Foreign currency translation and other adjustments | (63) | — | (63) |
| Balance at December 31, 2018 | 14,648 | 3,888 | 18,536 |
| Goodwill acquired (Note 3) | 978 | — | 978 |
| Goodwill disposed ⁽ⁱ⁾ | (1,265) | — | (1,265) |
| Foreign currency translation and other adjustments | 1 | — | 1 |
| Balance at December 31, 2019 | 14,362 | 3,888 | 18,250 |
| Goodwill acquired (Note 3) | 3,998 | — | 3,998 |
| Balance at December 31, 2020 | <u>18,360</u> | <u>3,888</u> | <u>22,248</u> |

Note:

(i) Disposition during the year ended December 31, 2019 was primarily related to the deconsolidation of a subsidiary (Note 4).

Intangible Assets

| | As of December 31, 2018 | | | |
|-----------------------------------|-------------------------|------------------------|--------------------------|--------------------|
| | Gross carrying value | Accumulated impairment | Accumulated amortization | Net carrying value |
| | RMB | RMB | RMB | RMB |
| | (In millions) | | | |
| Trademarks | 942 | (2) | (499) | 441 |
| Technology | 607 | — | (320) | 287 |
| Intellectual property right | 1,208 | (7) | (245) | 956 |
| Online literature | 141 | — | (19) | 122 |
| Others | 2,876 | (149) | (1,993) | 734 |
| | <u>5,774</u> | <u>(158)</u> | <u>(3,076)</u> | <u>2,540</u> |

| | As of December 31, 2019 | | | |
|-----------------------------------|-------------------------|------------------------|--------------------------|--------------------|
| | Gross carrying value | Accumulated impairment | Accumulated amortization | Net carrying value |
| | RMB | RMB | RMB | RMB |
| | (In millions) | | | |
| Trademarks | 658 | (2) | (182) | 474 |
| Technology | 456 | (52) | (188) | 216 |
| Intellectual property right | 1,548 | (355) | (594) | 599 |
| Online literature | 163 | — | (40) | 123 |
| Others | 805 | (19) | (598) | 188 |
| | <u>3,630</u> | <u>(428)</u> | <u>(1,602)</u> | <u>1,600</u> |

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

10. GOODWILL AND INTANGIBLE ASSETS—continued

Intangible Assets—continued

| | As of December 31, 2020 | | | |
|---------------------------------------|-------------------------|------------------------|--------------------------|--------------------|
| | Gross carrying value | Accumulated impairment | Accumulated amortization | Net carrying value |
| | RMB | RMB (In millions) | RMB | RMB |
| Trademarks | 1,054 | (238) | (205) | 611 |
| Technology | 1,087 | (52) | (307) | 728 |
| Intellectual property right | 1,599 | (467) | (757) | 375 |
| Online literature | 151 | — | (54) | 97 |
| Others | 899 | (19) | (669) | 211 |
| | <u>4,790</u> | <u>(776)</u> | <u>(1,992)</u> | <u>2,022</u> |

The carrying amounts of intangible assets with indefinite useful lives were insignificant as of December 31, 2018, 2019 and 2020.

The Company recognized impairment losses on intangible assets of RMB5 million, RMB406 million and RMB350 million for the years ended December 31, 2018, 2019 and 2020, respectively. Impairment losses on intangible assets are recorded in cost of revenues.

Amortization expense of intangible assets were RMB385 million, RMB661 million and RMB544 million, for the years ended December 31, 2018, 2019 and 2020, respectively.

Estimated amortization expense relating to the existing intangible assets with finite lives for each of the next five years is as follow:

| | RMB (In millions) |
|-----------------------------------|----------------------|
| For the years ending December 31, | |
| 2021 | 505 |
| 2022 | 448 |
| 2023 | 375 |
| 2024 | 337 |
| 2025 | 235 |

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

11. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

| | As of December 31, | | |
|---|--------------------|----------------------|---------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB (In millions) | RMB |
| Accrued other operating expenses | 10,680 | 8,925 | 8,301 |
| Content acquisition costs | 8,873 | 7,267 | 6,734 |
| Tax payable | 2,342 | 3,115 | 3,779 |
| Accrued payroll and welfare | 1,898 | 2,407 | 3,508 |
| Payable to noncontrolling interest shareholders | — | 240 | 3,466 |
| Traffic acquisition costs | 2,911 | 2,772 | 2,467 |
| Bandwidth costs | 2,085 | 2,492 | 1,985 |
| Accruals for purchases of fixed assets | 1,890 | 1,220 | 1,270 |
| Funds collected on behalf of service providers | 353 | 498 | 523 |
| Interest payable | 382 | 310 | 487 |
| Payable to merchants | 340 | 310 | 307 |
| Users’ and third party agents’ deposits | 661 | 641 | 268 |
| Others | 2,966 | 2,504 | 3,621 |
| | <u>35,381</u> | <u>32,701</u> | <u>36,716</u> |

12. LOANS PAYABLE

Short-term Loans

Short-term loans as of December 31, 2018, 2019 and 2020 amounted to RMB3.0 billion, RMB2.6 billion and RMB3.0 billion, respectively, which consisted of RMB denominated borrowings by the Company’s subsidiaries from financial institutions in the PRC and were repayable within one year.

As of December 31, 2018, 2019, and 2020, the repayments of primarily all of the short-term loans are guaranteed by subsidiaries of iQIYI and either collateralized by an office building of one of iQIYI’s VIEs with a carrying amount of RMB575 million, RMB562 million and RMB548 million respectively, or by restricted cash balances totaling US\$316 million, US\$139 million, and US\$4 million (equivalent to RMB23 million), respectively, or by other receivables totaling nil, nil and US\$5 million (equivalent to RMB35 million), respectively.

As of December 31, 2018, 2019 and 2020, the weighted average interest rates for the outstanding borrowings were approximately 4.47%, 4.05% and 4.30%, respectively, and the aggregate amounts of unused lines of credit for short-term loans were RMB781 million, RMB1.6 billion and RMB840 million, respectively.

Structured payable arrangements

In 2020, iQIYI entered into structured payable arrangements with banks or other financial institutions (“factoring arrangements”), which extended the original payment terms. Under the factoring arrangements, the suppliers’ receivables collection process was accelerated through selling its receivables from iQIYI to the banks or other financial institutions at a discount. iQIYI was legally obligated to pay the banks or other financial institutions in the amount totaling RMB396 million, maturing within one year.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

12. LOANS PAYABLE—continued

Structured payable arrangements—continued

As a result of the factoring arrangements, the payment terms of the iQIYI’s original accounts payables were substantially modified and considered extinguished as the nature of the original liability has changed from accounts payables to loan borrowings from banks or other financial institutions. The proceeds from borrowings from banks or other financial institutions is a financing activity and is reported as “Proceeds from short-term loans” on the consolidated statements of cash flows. As of December 31, 2020, the outstanding borrowings from the factoring arrangements were RMB390 million, which is repayable within one year and are included in “Short-term loans” in the consolidated balance sheet.

Long-term Loans

Baidu

In June 2016, the Company entered into a five-year term revolving facility agreement with a group of 21 syndicated bankers, pursuant to which the Company is entitled to borrow an unsecured USD denominated floating rate loan of US\$1.0 billion with a term of five years and to borrow an unsecured USD denominated revolving loan of US\$1.0 billion for five years. The facility was priced at 110 basis points over LIBOR and is intended for the general working capital of the Company. In June 2016, the Company drew down two tranches of US\$250 million each under the facility commitment. In November 2016, the Company drew down two tranches of US\$250 million each under the facility commitment. In connection with the facility agreements, the Company entered into four interest rate swap agreements, pursuant to which the loans would be settled with a fixed annual interest rate of 2.11%, 2.10%, 2.78% and 2.78% respectively, during the respective term of the loans.

The total outstanding borrowings were RMB7.0 billion and RMB6.5 billion, which was classified as “Long-term loans” as of December 31, 2019 and reclassified to “Long-term loans, current portion” as of December 31, 2020.

The interest rate swap agreements met the definition of a derivative in accordance with ASC Topic 815, *Derivatives and Hedging* (“ASC 815”). The derivatives related to the interest rate swap agreements are accounted at fair value and included in “Other non-current assets” on the consolidated balance sheets.

iQIYI

In 2017, iQIYI borrowed a secured RMB denominated loan of RMB299 million with an interest rate of 4.47% for a three-year term from the Bank of China for its general working capital purposes. Pursuant to the agreement, the principal shall be repaid by installments from 2017 to 2020. As of December 31, 2018, 2019 and 2020, the repayment of the loan is guaranteed by a subsidiary of iQIYI and collateralized by an office building of one of iQIYI’s VIEs with a carrying amount of RMB575 million, RMB562 million and RMB548 million, respectively. Principal repayments were made on the loan when they became due and amounted to RMB10 million and RMB274 million for the years ended December 31, 2019 and 2020, respectively. The loan was fully repaid as of December 31, 2020.

In September 2019, iQIYI entered into a two-year loan agreement with JPMorgan Chase Bank, N.A., pursuant to which iQIYI is entitled to borrow a secured RMB denominated loan of RMB800 million for the general working capital of iQIYI. In 2019, iQIYI drew down RMB448 million with an interest

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

12. LOANS PAYABLE—continued

Long-term Loans—continued

iQIYI—continued

rate of 3.55%. Pursuant to the agreement, the principal shall be repaid in installments from 2019 to 2021. As of December 31, 2019 and December 31, 2020, the repayment of the loan was collateralized by long-term held-to-maturity debt securities with a stated cost of US\$71 million and US\$71 million (equivalent to RMB463 million), respectively. Principal repayments were made on the loan when they became due and amounted to RMB3 million and RMB34 million for the years ended December 31, 2019 and 2020, respectively. The amount repayable within the next twelve months are classified as “Long-term loans, current portion”.

In December 2018, iQIYI entered into a series of transactions (“reverse factoring arrangement”) in order to re-finance certain payables due to its suppliers. In the reverse factoring arrangement, iQIYI’s suppliers sold certain 2018 receivables due from iQIYI (the “2018 factored receivables”) to the financial institutions at a discount. The 2018 factored receivables were transferred to a securitization vehicle and used to securitize debt securities issued to third-party investors for gross proceeds of RMB446 million. Concurrently, iQIYI also entered into an agreement with the financial institutions to extend the repayment of the underlying payables to mirror the repayment terms for the asset-back debt securities with maturities in December 2019 and December 2020. Under such arrangement, the payable obligation between iQIYI and the suppliers was considered settled and iQIYI was legally obligated to pay the financial institutions thereafter. As the 2018 factored receivables were sold to the financial institutions and used to securitize the debt securities, the factored receivables are viewed as collateral for raising loans through the issuance of 2018 asset-backed debt securities. The borrowings have an effective interest rate of 7.00%.

In November 2019, the Company entered into a similar reverse factoring arrangement whereby iQIYI’s suppliers sold certain 2019 receivables due from iQIYI (the “2019 factored receivables”) amounting to RMB587 million to the financial institutions at a discount. The 2019 factored receivables were transferred to a securitization vehicle and used to securitize debt securities issued to third-party investors for gross proceeds of RMB500 million. Concurrently, iQIYI also entered into an agreement with the financial institutions to extend the repayment of the underlying payables to mirror the repayment terms for the 2019 asset-back debt securities which mature in November 2021. The borrowings have an effective interest rate of 5.97%.

The securitization vehicle was designed by iQIYI with the sole purpose to acquire receivable balances from iQIYI’s suppliers in order to securitize the senior asset-backed securities with guaranteed returns sold to third-party investors. iQIYI has a variable interest in the securitization vehicle through its interest in the subordinated asset-backed securities issued by the securitization vehicle which bear the residual loss. As a result, iQIYI considers itself the primary beneficiary and consolidates the securitization vehicle given iQIYI has (i) the power to govern the activities that most significantly impact its economic performance, and (ii) is obligated to absorb losses that could potentially be significant to the securitization vehicle.

As a result of the series of transactions described above, the payment terms of iQIYI’s original trade payables were substantially modified and considered extinguished as the nature of the original liability has changed from that of a trade payable to loan borrowings from third-party investors.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

12. LOANS PAYABLE—continued

Long-term Loans—continued

iQIYI—continued

As of December 31, 2018, 2019 and 2020, the outstanding borrowings as a result of the reverse factoring arrangements were RMB444 million, RMB898 million and RMB498 million, respectively. RMB75 million and RMB371 million of 2018 asset-backed debt securities were repaid when they became due in December 2019 and December 2020, respectively. RMB30 million of 2019 asset-backed debt securities was repaid when it became due in October 2020. RMB498 million of asset-backed debt securities is repayable within one year and are included in “Long-term loans, current portion”.

13. NOTES PAYABLE

Baidu, Inc.

The Company issued and publicly sold unsecured senior notes, and the details of the tranches are shown below:

| | Issue date | Principal amount (US\$ million) | Mature date | Effective interest rate |
|--------------------------------|-------------------|------------------------------------|--------------------|-------------------------|
| 2022 Ten-year Notes | November 28, 2012 | 750 | November 28, 2022 | 3.59% |
| 2018 Notes | August 6, 2013 | 1,000 | August 6, 2018 | 3.39% * |
| 2019 Notes | June 9, 2014 | 1,000 | June 9, 2019 | 3.00% * |
| 2020 Notes | June 30, 2015 | 750 | June 30, 2020 | 3.13% * |
| 2025 Ten-year Notes | June 30, 2015 | 500 | June 30, 2025 | 4.22% |
| 2022 Five-year Notes | July 6, 2017 | 900 | July 6, 2022 | 3.08% |
| 2027 Notes | July 6, 2017 | 600 | July 6, 2027 | 3.73% |
| 2023 Notes | March 29, 2018 | 1,000 | September 29, 2023 | 3.99% |
| 2028 March Notes | March 29, 2018 | 500 | March 29, 2028 | 4.50% |
| 2024 Notes | November 14, 2018 | 600 | May 14, 2024 | 4.51% |
| 2024 Notes | December 10, 2018 | 250 | May 14, 2024 | 4.54% |
| 2028 November Notes | November 14, 2018 | 400 | November 14, 2028 | 4.99% |
| 2025 Five-year Notes | April 7, 2020 | 600 | April 7, 2025 | 3.22% |
| 2030 April Notes | April 7, 2020 | 400 | April 7, 2030 | 3.54% |
| 2026 Notes | October 9, 2020 | 650 | April 9, 2026 | 1.81% |
| 2030 October Notes | October 9, 2020 | 300 | October 9, 2030 | 2.43% |

Note:

* The 2018 Notes, 2019 Notes and 2020 Notes were fully repaid when they became due.

The notes listed above are collectively referred to as the “Notes.”

The 2022 Ten-year Notes bear interest at the rate of 3.500% per annum. Interest is payable semi-annually in arrears on and of each year, beginning on May 28, 2013.

The 2018 Notes bear interest at the rate of 3.25% per annum. Interest is payable semi-annually in arrears on and of each year, beginning on February 6, 2014.

The 2019 Notes bear interest at the rate of 2.750% per annum. Interest is payable semi-annually in arrears on and of each year, beginning on December 9, 2014.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

13. NOTES PAYABLE—continued

Baidu, Inc.—continued

The 2020 Notes bear interest at the rate of 3.000% per annum and the 2025 Ten-year Notes bear interest at the rate of 4.125% per annum. Interest is payable semi-annually in arrears on and of each year, beginning on December 30, 2015.

The 2022 Five-year Notes bear interest at the rate of 2.875% per annum and the 2027 Notes bear interest at the rate of 3.625% per annum. Interest is payable semi-annually in arrears on and of each year, beginning on January 6, 2018.

The 2023 Notes bear interest at the rate of 3.875% per annum and the 2028 March Notes bear interest at the rate of 4.375% per annum. Interest is payable semi-annually in arrears on and of each year, beginning on September 29, 2018.

The 2024 Notes including US\$600 million issued in November and US\$250 million in December 2018, respectively, bear interest at the rate of 4.375% per annum and the 2028 November Notes bear interest at the rate of 4.875% per annum. Interest is payable semi-annually in arrears on and of each year, beginning on May 14, 2019.

The 2025 Five-year Notes bear interest at the rate of 3.075% per annum and the 2030 April Notes bear interest at the rate of 3.425% per annum. Interest is payable semi-annually in arrears on and of each year, beginning on October 7, 2020.

The 2026 Notes bear interest at the rate of 1.720% per annum and the 2030 October Notes bear interest at the rate of 2.375% per annum. Interest is payable semi-annually in arrears on and of each year, beginning on April 9, 2021.

At maturity, the Notes are payable at their principal amount plus accrued and unpaid interest thereon.

The Notes do not contain any financial covenants or other significant restrictions. In addition, the Notes are unsecured and rank lower than any secured obligation of the Group and have the same liquidation priority as any other unsecured liabilities of the Group, but senior to those expressly subordinated obligations, if any. The Company may, at its discretion, redeem all or any portion of the Notes at any time, at the greater of the principal amount and the make whole amount plus accrued and unpaid interest. In addition, for the 2023 Notes, 2028 March Notes, 2024 Notes and 2028 November Notes, 2025 Five-year Notes, 2030 April Notes, 2026 Notes and 2030 October Notes, the Company may at its discretion, redeem all or any portion of the Notes at one or three months before the maturity date of respective notes, at a price equal to the greater of 100% of the principal amount of such Notes plus accrued and unpaid interest, if any, to (but not including) the redemption date. As of December 31, 2020, the Company does not intend to redeem any portion of the Notes prior to the stated maturity dates. For certain Notes, the Company has the obligation to redeem the Notes if a change in control occurs as defined in the indenture of the Notes.

The outstanding Notes were issued at a discount amounting to US\$20 million (equivalent to RMB131 million). The total issuance costs of US\$36 million (equivalent to RMB234 million) were presented as a direct deduction from the principal amount of the outstanding Notes on the consolidated balance sheets. Both the discount and the issuance costs are amortized as interest expense using the effective interest rate method through the maturity dates of the Notes.

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

13. NOTES PAYABLE—continued

Baidu, Inc.—continued

The principal amount and unamortized discount and debt issuance costs as of December 31, 2018, 2019 and 2020 were as follows:

| | As of December 31, | | |
|--|--------------------|---------------|---------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| Principal amount | 49,867 | 43,519 | 48,638 |
| Unamortized discount and debt issuance costs | (261) | (210) | (230) |
| | <u>49,606</u> | <u>43,309</u> | <u>48,408</u> |

The following table summarizes the aggregate required repayments of the principal amounts of the Company’s long-term debts (including the notes payable and loans payable (Note 12) but excluding convertible notes (Note 14)), in the succeeding five years and thereafter:

| | RMB |
|-----------------------------------|---------------|
| | (In millions) |
| For the years ending December 31, | |
| 2021 | 7,465 |
| 2022 | 10,766 |
| 2023 | 6,525 |
| 2024 | 5,546 |
| 2025 | 7,178 |
| Thereafter | 18,596 |

14. CONVERTIBLE NOTES

iQIYI 2023 Convertible Notes

In December 2018, iQIYI issued US\$750 million convertible senior notes due 2023 (“iQIYI 2023 Convertible Notes”). The iQIYI 2023 Convertible Notes are senior, unsecured obligations of iQIYI, and interest is payable semi-annually in cash at a rate of 3.75% per annum with a maturity date of December 1, 2023, unless redeemed, repurchased or converted prior to such date. The initial conversion rate of the iQIYI 2023 Convertible Notes is 37.1830 of iQIYI’s ADSs per US\$1,000 principal amount of the iQIYI 2023 Convertible Notes. Upon conversion, iQIYI will pay or deliver to such converting holders, as the case may be, cash, ADSs, or a combination of cash and ADSs, at its election.

Concurrently with the issuance of the iQIYI 2023 Convertible Notes, iQIYI purchased capped call options on iQIYI’s ADS with certain counterparties at a price of US\$68 million. The capped call exercise price is equal to the initial conversion price of the iQIYI 2023 Convertible Notes and the cap price is US\$38.42 per ADS, subject to certain adjustments under the terms of the capped call transaction. The cost of the capped call was recorded as a reduction of the Company’s additional paid-in capital and non-controlling interests on the consolidated balance sheets with no subsequent remeasurements to fair value.

As the conversion option may be settled entirely or partially in cash at iQIYI’s option, the Company separated the iQIYI 2023 Convertible Notes into liability and equity components in accordance with

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

14. CONVERTIBLE NOTES—continued

iQIYI 2023 Convertible Notes—continued

ASC Subtopic 470-20, *Debt with Conversion and Other Options*. The carrying amount of the liability component was calculated by measuring the fair value of a similar liability that did not have an associated conversion feature. The carrying amount of the equity component representing the conversion option was determined by deducting the fair value of the liability component from the initial proceeds and recorded as additional paid-in capital. Debt issuance costs were allocated to the liability and equity components based on the same proportion as the recognized amounts bifurcated based on gross proceeds from the iQIYI 2023 Convertible Notes. The difference between the principal amount of the iQIYI 2023 Convertible Notes and the liability component was considered debt discount and amortized at an effective interest rate of 7.04% to accrete the discounted carrying value of the iQIYI 2023 Convertible Notes to its face value on December 1, 2021, the put date of the iQIYI 2023 Convertible Notes. The holders may require iQIYI to repurchase all or portion of the iQIYI 2023 Convertible Notes for cash on December 1, 2021, or upon a fundamental change, at a repurchase price equal to 100% of the principal amount, plus accrued and unpaid interest.

iQIYI 2025 Convertible Notes

In March 2019, iQIYI issued US\$1.2 billion convertible senior notes due 2025 (“iQIYI 2025 Convertible Notes”). The iQIYI 2025 Convertible Notes are senior, unsecured obligations of iQIYI, and interest is payable semi-annually in cash at a rate of 2.00% per annum with a maturity date of April 1, 2025, unless redeemed, repurchased or converted prior to such date. The initial conversion rate of the iQIYI 2025 Convertible Notes is 33.0003 of iQIYI’s ADSs per US\$1,000 principal amount of the iQIYI 2025 Convertible Notes. Upon conversion, iQIYI will pay or deliver to such converting holders, as the case may be, cash, ADSs, or a combination of cash and ADSs, at its election.

Concurrently with the issuance of the iQIYI 2025 Convertible Notes, iQIYI purchased capped call options on iQIYI’s ADS with certain counterparties at a price of US\$85 million. The capped call exercise price is equal to the initial conversion price of the iQIYI 2025 Convertible Notes and the cap price is US\$40.02 per ADS, subject to certain adjustments under the terms of the capped call transaction. The cost of the capped call was recorded as a reduction of the Company’s additional paid-in capital and non-controlling interests on the consolidated balance sheets with no subsequent remeasurements to fair value.

The accounting of iQIYI 2025 Convertible Notes is similar to that of iQIYI 2023 Convertible Notes. The difference between the principal amount of the iQIYI 2025 Convertible Notes and the liability component was considered debt discount and amortized at an effective interest rate of 6.01% to accrete the discounted carrying value of the iQIYI 2025 Convertible Notes to its face value on April 1, 2023, the put date of the iQIYI 2025 Convertible Notes. The holders may require iQIYI to repurchase all or portion of the iQIYI 2025 Convertible Notes for cash on April 1, 2023, or upon a fundamental change, at a repurchase price equal to 100% of the principal amount, plus accrued and unpaid interest.

iQIYI 2026 Convertible Notes

In December 2020, iQIYI issued US\$800 million convertible senior notes (“iQIYI 2026 Convertible Notes”). The iQIYI 2026 Convertible Notes are senior, unsecured obligations of iQIYI, and interest is payable semi-annually in cash at a rate of 4.00% per annum with a maturity date of December 15, 2026, unless redeemed, repurchased or converted prior to such date. The initial conversion rate of

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

14. CONVERTIBLE NOTES—continued

iQIYI 2026 Convertible Notes—continued

iQIYI 2026 Convertible Notes is 44.8179 of iQIYI’s ADSs per US\$1,000 principal amount of the iQIYI 2026 Convertible Notes. Upon conversion, iQIYI will pay or deliver to such converting holders, as the case may be, cash, ADSs, or a combination of cash and ADSs, at its election.

The accounting of iQIYI 2026 Convertible Notes is similar to that of iQIYI 2023 Convertible Notes. The difference between the principal amount of the iQIYI 2026 Convertible Notes and the liability component was considered debt discount and amortized at an effective interest rate of 6.94% to accrete the discounted carrying value of the iQIYI 2026 Convertible Notes to its face value on August 1, 2024, the put date of the iQIYI 2026 Convertible Notes. The holders may require iQIYI to repurchase all or portion of the iQIYI 2026 Convertible Notes for cash on August 1, 2024, or upon a fundamental change, at a repurchase price equal to 100% of the principal amount, plus accrued and unpaid interest.

The iQIYI 2023 Convertible Notes, the iQIYI 2025 Convertible Notes and the iQIYI 2026 Convertible Notes are collectively referred to the Convertible Notes.

The carrying amount of the Convertible Notes as of December 31, 2018, 2019 and 2020 were as follows:

| | As of December 31, | | |
|---------------------------------------|--------------------|---------------|---------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| Liability component: | | | |
| Principal | 5,158 | 13,578 | 17,954 |
| Less: unamortized debt discount | 446 | 1,281 | 1,275 |
| Net carrying amount | <u>4,712</u> | <u>12,297</u> | <u>16,679</u> |
| Equity component: | | | |
| Carrying amount | <u>362</u> | <u>1,349</u> | <u>1,744</u> |

For the years ended December 31, 2018, 2019 and 2020, the amount of interest cost recognized relating to both the contractual interest coupon and amortization of the discount on the liability component were RMB24 million, RMB670 million and RMB799 million, respectively. As of December 31, 2020, the liability component of the iQIYI 2023 Convertible Notes, the iQIYI 2025 Convertible Notes and the iQIYI 2026 Convertible Notes would be accreted up to the principal amount of US\$750 million, US\$1.2 billion and US\$800 million over a remaining period of 0.92 years, 2.25 years and 3.59 years, respectively. The amount repayable within the next twelve months are classified as “Convertible senior notes, current portion” in the consolidated balance sheets.

The aggregate scheduled maturities of RMB4.9 billion, RMB7.8 billion and RMB5.2 billion of the Convertible Notes will be repaid when they become due in 2023, 2025 and 2026, respectively, assuming there is no conversion of the Convertible Notes, no redemption of the Convertible Notes prior to their maturities and the convertible senior notes bondholders hold the Convertible Notes until their maturities and iQIYI elects to fully settle the Convertible Notes in cash.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

15. LEASES

The Company’s operating leases mainly related to land, office facilities, IDC facilities and vehicles. For leases with terms greater than 12 months, the Company records the related asset and lease liability at the present value of lease payments over the term. Certain leases include rental escalation clauses, renewal options and/or termination options that are factored into the Company’s determination of lease payments when appropriate. As of December 31, 2019 and 2020, finance leases were insignificant.

As of December 31, 2020, the weighted average remaining lease term was 16.2 years and weighted average discount rate was 4.53% for the Group’s operating leases.

Operating lease cost was RMB2.7 billion and RMB3.0 billion for the years ended December 31, 2019 and 2020, respectively, which excluded cost of short-term contracts. Short-term lease cost was RMB434 million and RMB427 million for the years ended December 31, 2019 and 2020, respectively. Variable lease cost was immaterial for the years ended December 31, 2019 and 2020. For the year ended December 31, 2019 and 2020, no lease cost for operating or finance leases was capitalized.

Supplemental cash flow information related to operating leases was as follows:

| | For the years ended December 31, | |
|---|----------------------------------|-------|
| | 2019 | 2020 |
| | RMB | RMB |
| | (In millions) | |
| Cash payments for operating leases | 2,631 | 5,187 |
| ROU assets obtained in exchange for operating lease liabilities | 3,896 | 2,841 |

Future lease payments under operating leases as of December 31, 2020 were as follows:

| | Operating leases |
|---|------------------|
| | RMB |
| | (In millions) |
| Year ending December 31, | |
| 2021 | 2,430 |
| 2022 | 1,856 |
| 2023 | 1,433 |
| 2024 | 1,032 |
| 2025 | 464 |
| Thereafter | 624 |
| Total future lease payments | 7,839 |
| Less: Imputed interest | 780 |
| Total lease liability balance | <u>7,059</u> |

As of December 31, 2020, additional operating leases that have not yet commenced were immaterial.

16. INCOME TAXES

Cayman Islands and BVI

Under the current laws of the Cayman Islands and BVI, the Company is not subject to tax on income or capital gains. Additionally, upon payment of dividends by the Company to its shareholders, no Cayman Islands withholding tax will be imposed.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

16. INCOME TAXES—continued

Hong Kong

Subsidiaries in Hong Kong are subject to Hong Kong Profits Tax rate at 16.5%, and foreign-derived income is exempted from income tax. There are no withholding taxes in Hong Kong on remittance of dividends.

Japan

As a result of the Japanese tax regulations amendments, the effective income tax rate are approximately 31%, 31% and 31% for the years ended December 31, 2018, 2019 and 2020, respectively.

China

Under the PRC Enterprise Income Tax (“EIT”) Law, which has been effective since January 1, 2008, domestic enterprises and Foreign Investment Enterprises (the “FIE”) are subject to a unified 25% enterprise income tax rate, except for certain entities that are entitled to preferential tax treatments. Preferential EIT rates at 15% and 10% are available for qualified “High and New Technology Enterprises” (“HNTEs”) and “Key Software Enterprise” (“KSE”), respectively. The HNTE certificate is effective for a period of three years and the KSE is subject to relevant governmental authorities’ annual assessment based on self-assessment supporting documents filed with the tax authorities each year.

Baidu Online, Baidu China and Baidu International enjoyed a reduced tax rate of 10% as qualified KSEs in 2018 and 2019. Certain other PRC subsidiaries and VIEs, including Baidu Netcom, are qualified HNTEs and enjoy a reduced tax rate of 15% for the years presented, which will expire in 2022 and 2023. Certain entities must file required supporting documents with the tax authorities before using the preferential rates. Whether the entity is entitled to enjoy a preferential rate as a KSE is subject to relevant governmental authorities’ assessment each year. An entity could re-apply for the HNTE certificate when the prior certificate expires. Historically, all of the Company’s subsidiaries and VIEs successfully re-applied for the certificates when the prior ones expired.

A certificate for the current year might be obtained in the following year as a result of the stringent inspection and approval process by the governmental authorities. The Company would record an income tax reversal in the year when the certificate is obtained for the over-paid or over-accrued provisional tax in connection with the grant of a more favorable tax rate for the prior year.

Under the current EIT Law, dividends for earnings derived from January 1, 2008 and onwards paid by PRC entities to any of their foreign non-resident enterprise investors are subject to a 10% withholding tax. A lower tax rate will be applied if tax treaty or arrangement benefits are available. Under the tax arrangement between the PRC and Hong Kong, the reduced withholding tax rate for dividends paid by PRC entities is 5% provided the Hong Kong investors meet the requirements as stipulated by relevant PRC tax regulations, such as the beneficiary owner test. Capital gains derived from PRC are also subject to a 10% PRC withholding tax.

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

16. INCOME TAXES—continued

China—continued

Income (loss) before income taxes consists of:

| | For the years ended December 31, | | |
|---------------|-------------------------------------|--------------|---------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| PRC | 23,524 | 13,076 | 19,711 |
| Non-PRC | 3,801 | (13,416) | 3,379 |
| | <u>27,325</u> | <u>(340)</u> | <u>23,090</u> |

Except for the investment related gain recognized, the pre-tax losses from non-PRC operations consist primarily of operating costs, administration expenses, interest expenses and share-based compensation expenses.

Income taxes consist of:

| | For the years ended December 31, | | |
|---|----------------------------------|--------------|--------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| Current income tax | 6,184 | 3,564 | 4,668 |
| Income tax refund due to reduced tax rate | (680) | (920) | (719) |
| Adjustments of deferred tax assets due to change in tax rates | — | 9 | (5) |
| Deferred income tax (benefit) expense | (761) | (705) | 120 |
| | <u>4,743</u> | <u>1,948</u> | <u>4,064</u> |

The reconciliation of the actual income taxes to the amount of tax computed by applying the aforementioned statutory income tax rate to pre-tax income is as follows:

| | For the years ended December 31, | | |
|---|--|---------------|--------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions, except for per share data) | | |
| Expected taxation at PRC statutory tax rate | 6,831 | (85) | 5,773 |
| Effect of differing tax rates in different jurisdictions | 493 | 3,299 | 208 |
| Non-taxable income | (1,555) | (419) | (995) |
| Non-deductible expenses | 935 | 2,124 | 3,416 |
| Research and development super-deduction | (1,047) | (1,245) | (1,549) |
| Effect of PRC preferential tax rates and tax holiday | (2,250) | (1,327) | (2,891) |
| Effect of tax rate changes on deferred taxes | — | 9 | (5) |
| Reversal of prior year’s EIT | (616) | (1,134) | (951) |
| PRC withholding tax | 553 | (224) | 122 |
| Addition to valuation allowance | 1,399 | 950 | 936 |
| Taxation for the year | <u>4,743</u> | <u>1,948</u> | <u>4,064</u> |
| Effective tax rate | <u>17%</u> | <u>(573%)</u> | <u>18%</u> |
| Effect of preferential tax rates inside the PRC on basic earnings per Class A and Class B ordinary share (Note) | <u>0.81</u> | <u>0.49</u> | <u>1.06</u> |

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

16. INCOME TAXES—continued

China—continued

Note: Effect of preferential tax rates inside the PRC on basic earnings per Class A and Class B ordinary share for the years ended December 31, 2018, 2019 and 2020 have been retrospectively adjusted for the Share Subdivision that became effective on March 1, 2021, as detailed in Note 2.(a) and Note 21.

The tax effects of temporary differences that gave rise to the deferred tax balances at December 31, 2018, 2019 and 2020 are as follows:

| | As of December 31, | | |
|---|--------------------|--------------|--------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | 2020 |
| | (In millions) | | |
| Deferred tax assets: | | | |
| Allowance for credit loss | 252 | 332 | 452 |
| Accrued expenses, payroll and others | 4,284 | 4,820 | 5,456 |
| Fixed assets depreciation | 60 | 151 | 106 |
| Net operating loss carry-forward | 1,609 | 1,733 | 1,811 |
| Less: valuation allowance | (3,881) | (4,843) | (5,895) |
| Deferred tax assets, net | <u>2,324</u> | <u>2,193</u> | <u>1,930</u> |
| | | | |
| | As of December 31, | | |
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| Deferred tax liabilities: | | | |
| Long-lived assets arising from acquisitions | 360 | 275 | 406 |
| Withholding tax on PRC subsidiaries’ undistributed earnings | 619 | 1,621 | 1,381 |
| Tax on capital gains | 2,778 | 1,159 | 943 |
| Other | 342 | 218 | 593 |
| | <u>4,099</u> | <u>3,273</u> | <u>3,323</u> |

The Group offset deferred tax liabilities and assets pertaining to a particular tax-paying component of the Group within a particular jurisdiction. The total income tax expenses were RMB4,743 million, RMB1,948 million and RMB4,064 million for the the years ended December 31, 2018, 2019 and 2020, respectively. The change in income tax expense is mainly due to changes of overall profits before tax. The effective tax rate for the the year ended December 31, 2020 is lower than the PRC statutory EIT rate of 25% mainly due to international income tax rate and preferential income tax rate impact, research and development super-deduction, and change in withhold rate and Key Software Enterprise status obtained.

As of December 31, 2020, the Company had tax losses of approximately RMB9.7 billion deriving from entities in the PRC, Hong Kong and Japan. The tax losses in Japan can be carried forward for nine years to offset future taxable profit. The tax losses in PRC can be carried forward for five years to offset future taxable profit, and the period was extended to 10 years for entities qualified as HNTE in 2019 and thereafter. The tax losses of entities in the PRC and Japan will expire from 2021 to 2030, if not utilized. The tax losses in Hong Kong can be carried forward with no expiration date.

The Company evaluated its income tax uncertainty under ASC 740. ASC 740 clarifies the accounting for uncertainty in income taxes by prescribing the recognition threshold a tax position is required to

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

16. INCOME TAXES—continued

China—continued

meet before being recognized in the financial statements. The Company elects to classify interest and penalties related to an uncertain tax position, if and when required, as part of income tax expense in the consolidated statements of comprehensive income (loss). The Company does not expect the amount of unrecognized tax benefits to increase significantly in the next 12 months. In general, the PRC tax authorities have up to five years to conduct examinations of the tax filings of the Company’s PRC subsidiaries. Accordingly, the PRC subsidiaries’ tax years of 2015 – 2020 remain open to examination by the respective tax authorities. The Company may also be subject to the examination of the tax filings in other jurisdictions, which are not material to the consolidated financial statements.

As of December 31, 2020, dividend distribution withholding tax for the potential remittance of earnings from the PRC subsidiaries to offshore entities was RMB1.4 billion. The Company believes that the underlying dividends will be distributed in the future for offshore use, such as merger and acquisition activities. The Company did not provide for additional deferred income taxes and foreign withholding taxes on the undistributed earnings of foreign subsidiaries during the years presented on the basis of its intent to permanently reinvest its foreign subsidiaries’ earnings. As of December 31, 2020, the total amount of undistributed earnings from the PRC subsidiaries and the VIEs for which no withholding tax has been accrued was RMB154.1 billion. Determination of the amount of unrecognized deferred tax liability related to these earnings is not practicable. Under the PRC tax regulations, dividends from PRC companies to their overseas parents in respect of earnings derived from January 1, 2008 onwards are subject to PRC dividend withholding tax at 10%. Such rate could be reduced to 5% should tax treaty benefits be applicable.

17. EMPLOYEE DEFINED CONTRIBUTION PLAN

Full time employees of the Group in the PRC participate in a government mandated multi-employer defined contribution plan pursuant to which certain pension benefits, medical care, unemployment insurance, employee housing fund and other welfare benefits are provided to employees. Chinese labor regulations require that the Group make contributions to the government for these benefits based on certain percentages of the employees’ salaries. The Group has no legal obligation for the benefits beyond the contributions. Total amounts for such employee benefits, which were expensed as incurred, were RMB2.9 billion, RMB3.2 billion and RMB2.7 billion for the years ended December 31, 2018, 2019 and 2020, respectively.

18. COMMITMENTS AND CONTINGENCIES

Capital Commitments

The Group’s capital commitments primarily relate to commitments in connection with the expansion and improvement of its network infrastructure and its plan to build additional office buildings and cloud computing based data centers. Total capital commitments contracted but not yet reflected in the financial statements amounted to RMB754 million as of December 31, 2020. Almost all of the commitments relating to the network infrastructure, office building and cloud computing based data centers are to be fulfilled within one year.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

18. COMMITMENTS AND CONTINGENCIES—continued

Commitments for bandwidth and property management fees

Future minimum payments under non-cancelable agreements for bandwidth and property management fees consist of the following as of December 31, 2020:

| | <u>RMB</u> (In millions) |
|------------------|-----------------------------|
| 2021 | 742 |
| 2022 | 323 |
| 2023 | 135 |
| 2024 | 81 |
| 2025 | 45 |
| Thereafter | <u>47</u> |
| | <u>1,373</u> |

Future minimum lease payments for operating lease commitments as of December 31, 2020 are disclosed in Note 15.

Licensed Copyrights and Produced Content Commitments

Future minimum payments under non-cancelable agreements for licensed copyrights and produced content consist of the following as of December 31, 2020:

| | <u>RMB</u> (In millions) |
|------------------|-----------------------------|
| 2021 | 10,480 |
| 2022 | 6,239 |
| 2023 | 3,421 |
| 2024 | 1,286 |
| 2025 | 345 |
| Thereafter | — |
| | <u>21,771</u> |

Investment Commitments

The Group’s investment commitments primarily relate to capital contribution obligations under certain arrangements which do not have contractual maturity date. The total investment commitments contracted but not yet reflected in the consolidated financial statements amounted to RMB1.5 billion.

Guarantees

The Group accounts for guarantees in accordance with ASC Topic 460, *Guarantees* (“ASC 460”). Accordingly, the Company evaluates its guarantees if any to determine whether (a) the guarantee is specifically excluded from the scope of ASC 460, (b) the guarantee is subject to ASC 460 disclosure requirements only, but not subject to the initial recognition and measurement provisions, or (c) the guarantee is required to be recorded in the financial statements at fair value.

The corporate by-laws require that the Company indemnify its officers and directors, as well as those who act as directors and officers of other entities at the Company’s request, against expenses,

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

18. COMMITMENTS AND CONTINGENCIES—continued

Guarantees—continued

judgments, fines, settlements and other amounts actually and reasonably incurred in connection with any proceedings arising out of their services to the Company. In addition, the Company entered into separate indemnification agreements with each director and each executive officer of the Company that provide for indemnification of these directors and officers under similar circumstances and under additional circumstances. The indemnification obligations are more fully described in the by-laws and the indemnification agreements. The Company purchases standard directors and officers insurance to cover claims or a portion of the claims made against its directors and officers. Since a maximum obligation is not explicitly stated in the Company’s by-laws or in the indemnification agreements and will depend on the facts and circumstances that arise out of any future claims, the overall maximum amount of the obligations cannot be reasonably estimated.

Historically, the Company was not required to make payments related to these obligations, and the fair value for these obligations was nil on the consolidated balance sheets as of December 31, 2018, 2019 and 2020.

Litigation

The Group was involved in certain cases pending in various PRC, U.S. and Brazil courts and arbitration as of December 31, 2020. These cases include copyright infringement cases, unfair competition cases, and defamation cases, among others. Adverse results in these lawsuits may include awards of damages and may also result in, or even compel, a change in the Company’s business practices, which could result in a loss of revenue or otherwise harm the business of the Company.

Starting in April 2020, the Group and certain of its officers were named as defendants in putative securities class actions filed in federal court. The case was purportedly brought on behalf of a class of persons who allegedly suffered damages as a result of alleged misstatements and omissions in the Group’s public disclosure documents related to Baidu Feed, which they believe did not comply with “PRC laws and regulations in all material respects”. In addition, the Group received a complaint alleging that between April 8, 2016 and August 13, 2020, the Group made material misrepresentations in disclosures filed with the SEC by misrepresenting the financial and business condition of iQIYI and failing to disclose that iQIYI had inadequate controls. Both of those cases remain in preliminary stage, the likelihood of any unfavorable outcome or the amount or range of any potential loss cannot be reasonably estimated at the issuance date of the consolidated financial statements. As a result, as of December 31, 2020, the Group did not record any liabilities for the loss contingencies pertaining to the cases described above.

For many proceedings, the Company is currently unable to estimate the reasonably possible loss or a range of reasonably possible losses as the proceedings are in the early stages, and/or there is a lack of clear or consistent interpretation of laws specific to the industry-specific complaints among different jurisdictions. As a result, there is considerable uncertainty regarding the timing or ultimate resolution of such matters, which includes eventual loss, fine, penalty or business impact, if any, and therefore, an estimate for the reasonably possible loss or a range of reasonably possible losses cannot be made. However, the Company believes that such matters, individually and in the aggregate, when finally resolved, are not reasonably likely to have a material adverse effect on the Company’s consolidated results of operations, financial position and cash flows. With respect to the limited number of

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

18. COMMITMENTS AND CONTINGENCIES—continued

Litigation—continued

proceedings for which the Company was able to estimate the reasonably possible losses or the range of reasonably possible losses, such loss estimates were insignificant.

19. REDEEMABLE NONCONTROLLING INTERESTS

| | <u>2018</u> | <u>2019</u> | <u>2020</u> |
|---|-----------------|--------------|--------------|
| | RMB | RMB | RMB |
| | (In millions) | | |
| Balance as of January 1 | 11,022 | 716 | 1,109 |
| Business combinations (Note 3) | 698 | 182 | — |
| Issuance of subsidiary shares | — | 100 | 1,866 |
| Accretion of redeemable noncontrolling interests | 146 | 111 | 127 |
| Conversion of iQIYI preferred shares recognized as redeemable noncontrolling interests to ordinary shares | <u>(11,150)</u> | <u>—</u> | <u>—</u> |
| Balance as of December 31 | <u>716</u> | <u>1,109</u> | <u>3,102</u> |

In October 2018, the Company acquired additional shares of a former equity method investee, resulting in the investee becoming a subsidiary of the Company. The subsidiary had issued 159,820,917 outstanding preferred shares to certain shareholders, which could be redeemed by such shareholders upon the occurrence of certain events that are not solely within the control of the subsidiary. Therefore, these preferred shares were accounted for as redeemable noncontrolling interests (Note 3).

In September 2020, the Company entered into definitive agreements to issue Series A preferred shares of the Group’s smart living business, or Smart Living Group (“SLG”). SLG had issued 61,666,667 outstanding preferred shares to certain shareholders, which could be redeemed by such shareholders upon the occurrence of certain events that are not solely within the control of the subsidiary. Therefore, these preferred shares were accounted for as redeemable noncontrolling interests.

The Company accounts for the changes in accretion to the redemption value in accordance with ASC Topic 480, *Distinguishing Liabilities from Equity*. The Company elects to use the effective interest method to account for the changes of redemption value over the period from the date of issuance to the earliest redemption date of the noncontrolling interest.

20. SHAREHOLDERS’ EQUITY

Ordinary Shares

The authorized share capital consisted of 69,632,000,000 ordinary shares (previously 870,400,000 ordinary shares before the Share Subdivision as detailed in Note 2.(a)) at a par value of US\$0.000000625 per share (previously US\$0.00005 per share before the Share Subdivision as detailed in Note 2.(a)), of which 66,000,000,000 shares were designated as Class A ordinary shares, 2,832,000,000 as Class B ordinary shares, and 800,000,000 shares designated as preferred shares (previously of which 825,000,000 shares were designated as Class A ordinary shares, 35,400,000 as Class B ordinary shares, and 10,000,000 shares designated as preferred shares before the Share Subdivision as detailed in Note 2.(a) Note 21). The rights of the holders of Class A and Class B ordinary shares are identical, except with respect to voting and conversion rights. Each share of Class A ordinary shares is entitled to one vote per share and is not convertible into Class B ordinary

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

20. SHAREHOLDERS’ EQUITY—continued

Ordinary Shares—continued

shares under any circumstances. Each share of Class B ordinary shares is entitled to ten votes per share and is convertible into one Class A ordinary share at any time by the holder thereof. Upon any transfer of Class B ordinary shares by a holder thereof to any person or entity that is not an affiliate of such holder, such Class B ordinary shares would be automatically converted into an equal number of Class A ordinary shares. The number of Class B ordinary shares transferred to Class A ordinary shares was nil, nil and 4,200,000 in the years ended December 31, 2018, 2019 and 2020, respectively.

As of December 31, 2020, there were 2,107,228,720 and 571,900,320 Class A and Class B ordinary shares outstanding (previously 26,340,359 and 7,148,754 Class A and Class B ordinary shares before the Share Subdivision as detailed in Note 2.(a)), respectively. As of December 31, 2018, 2019 and 2020, there were no preferred shares issued and outstanding.

On June 27, 2018, the Company announced a share repurchase program under which the Company proposed to acquire up to an aggregate of US\$1.0 billion of its ordinary shares over the next 12 months in the open market or through privately negotiated transactions, depending on market conditions and in accordance with applicable rules and regulations.

On May 16, 2019, the Company announced a share repurchase program under which the Company proposed to acquire up to an aggregate of US\$1.0 billion of its ordinary shares, effective until July 1, 2020 in the open market or through privately negotiated transactions, depending on market conditions and in accordance with applicable rules and regulations.

On May 13, 2020, the Company announced a share repurchase program (“2020 share repurchase program”) under which the Company proposed to acquire up to an aggregate of US\$1.0 billion of its ordinary shares, effective until July 1, 2021 in the open market or through privately negotiated transactions, depending on market conditions and in accordance with applicable rules and regulations. In August 2020, the board of directors approved a change to the 2020 share repurchase program, increasing the repurchase authorization from US\$1.0 billion to US\$3.0 billion, and in December 2020, the repurchase authorization was further increased from US\$3.0 billion to US\$4.5 billion, which is effective through December 31, 2022.

The Company repurchased 16,573,200, 53,162,720 and 126,096,000 Class A ordinary shares (previously 207,165, 664,534 and 1,576,200 Class A ordinary shares before the Share Subdivision as detailed in Note 2.(a)) from the open market with an aggregate purchase price of RMB3.3 billion, RMB5.0 billion and RMB13.1 billion during the years ended December 31, 2018, 2019 and 2020. The repurchased shares were cancelled under Cayman Islands law upon repurchase and the difference between the par value and the repurchase price was debited to retained earnings.

Retained Earnings

In accordance with the Regulations on Enterprises with Foreign Investment of China and their articles of association, the Company’s PRC subsidiaries, being foreign invested enterprises established in China, are required to make appropriations to certain statutory reserves, namely a general reserve fund, an enterprise expansion fund, a staff welfare fund and a bonus fund, all of which are appropriated from net profit as reported in their PRC statutory accounts. Each of the Company’s PRC subsidiaries is

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

20. SHAREHOLDERS’ EQUITY—continued

Retained Earnings—continued

required to allocate at least 10% of its after-tax profits to a general reserve fund until such fund has reached 50% of its respective registered capital. Appropriations to the enterprise expansion fund and staff welfare and bonus funds are at the discretion of the Company’s subsidiaries.

In accordance with the China Company Laws, the Company’s VIEs must make appropriations from their after-tax profits as reported in their PRC statutory accounts to non-distributable reserve funds, namely a statutory surplus fund, a statutory public welfare fund and a discretionary surplus fund. Each of the Company’s VIEs is required to allocate at least 10% of its after-tax profits to the statutory surplus fund until such fund has reached 50% of its respective registered capital. Appropriations to the statutory public welfare fund and the discretionary surplus fund are made at the discretion of the Company’s VIEs.

General reserve and statutory surplus funds are restricted to set-off against losses, expansion of production and operation and increasing registered capital of the respective company. Staff welfare and bonus fund and statutory public welfare funds are restricted to capital expenditures for the collective welfare of employees. The reserves are not allowed to be transferred to the Company in the form of cash dividends, loans or advances, nor are they allowed for distribution except under liquidation.

| | As of December 31, | | |
|--|--------------------|----------------|----------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | | (In millions) | |
| PRC statutory reserve funds | 515 | 626 | 806 |
| Unreserved retained earnings | 128,731 | 125,642 | 134,478 |
| Total retained earnings | <u>129,246</u> | <u>126,268</u> | <u>135,284</u> |

Under PRC laws and regulations, there are restrictions on the Company’s PRC subsidiaries and VIEs with respect to transferring certain of their net assets to the Company either in the form of dividends, loans, or advances. Amounts of net assets restricted include paid in capital and statutory reserve funds of the Company’s PRC subsidiaries and the net assets of the VIEs in which the Company has no legal ownership, totaling RMB25.7 billion, RMB40.8 billion and RMB45.0 billion as of December 31, 2018, 2019 and 2020, respectively.

Furthermore, cash transfers from the Company’s PRC subsidiaries to their parent companies outside of China are subject to PRC government control of currency conversion. Shortages in the availability of foreign currency may restrict the ability of the PRC subsidiaries and consolidated affiliated entities to remit sufficient foreign currency to pay dividends or other payments to the Company, or otherwise satisfy their foreign currency denominated obligations.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

20. SHAREHOLDERS’ EQUITY—continued

Accumulated Other Comprehensive Income (Loss)

The changes in accumulated other comprehensive income (loss) by component, net of tax, were as follows:

| | Foreign currency translation adjustment | Unrealized gains on available-for-sale investments | Total |
|---|--|---|----------------|
| | RMB | RMB (In millions) | RMB |
| Balance at December 31, 2017 | (888) | 1,818 | 930 |
| Cumulative effect of accounting change* | — | (1,854) | (1,854) |
| Other comprehensive income before reclassification | 114 | 4,117 | 4,231 |
| Amounts reclassified from accumulated other comprehensive income | 80 | (2,171) | (2,091) |
| Net current-period other comprehensive income | 194 | 92 | 286 |
| Other comprehensive income attribute to noncontrolling interests and redeemable noncontrolling interests | (1,006) | — | (1,006) |
| Balance at December 31, 2018 | (1,700) | 1,910 | 210 |
| Other comprehensive income before reclassification | 207 | 1,981 | 2,188 |
| Amounts reclassified from accumulated other comprehensive income | (989) | (2,689) | (3,678) |
| Net current-period other comprehensive loss | (782) | (708) | (1,490) |
| Other comprehensive loss attribute to noncontrolling interests and redeemable noncontrolling interests | (102) | (1) | (103) |
| Balance at December 31, 2019 | (2,584) | 1,201 | (1,383) |
| Other comprehensive income before reclassification | 1,936 | 380 | 2,316 |
| Amounts reclassified from accumulated other comprehensive income | — | (541) | (541) |
| Net current-period other comprehensive income (loss) | 1,936 | (161) | 1,775 |
| Other comprehensive loss attribute to noncontrolling interests and redeemable noncontrolling interests | (192) | (1) | (193) |
| Balance at December 31, 2020 | (840) | 1,039 | 199 |

Note:

* Adjustment of net unrealized gains related to available-for-sale equity investments from accumulated other comprehensive income to opening retained earnings as a result of the adoption of ASU 2016-13 on January 1, 2018.

The amounts reclassified out of accumulated other comprehensive income represent realized foreign currency translation adjustments, which mainly arise from the disposal of partial interests in Trip and realized gains on the sales of available-for-sale investments, which were recorded in “Others, net” in the consolidated statements of comprehensive income (loss). The amounts reclassified were determined on the basis of specific identification. Losses on intracompany foreign currency transactions that are of a long-term-investment nature in the amount of nil, nil and RMB1.2 billion were included in the foreign currency translation adjustment for the years ended December 31, 2018, 2019 and 2020, respectively.

In October 2019, the Company completed a partial disposal of its investment in Trip and the corresponding accumulated other comprehensive income of RMB989 million was reclassified to

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

20. SHAREHOLDERS’ EQUITY—continued

Accumulated Other Comprehensive Income (Loss)—continued

income and recorded as “Others, net” in the consolidated statement of comprehensive loss for the year ended December 31, 2019.

The following table sets forth the tax benefit (expense) allocated to each component of other comprehensive income (loss) for the years ended December 31, 2018, 2019 and 2020:

| | For the years ended December 31, | | |
|--|-------------------------------------|------------|-----------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| Unrealized gains on available-for-sale investments | | | |
| Other comprehensive income before reclassification | (409) | (280) | (59) |
| Amounts reclassified from accumulated other comprehensive income | 328 | 402 | 83 |
| Net current-period other comprehensive income (loss) | <u>(81)</u> | <u>122</u> | <u>24</u> |

21. EARNINGS PER SHARE (“EPS”)

Following the Share Subdivision as detailed in Note 2.(a), each ordinary share was subdivided into eighty ordinary shares and each ADS represents eight Class A ordinary shares. The weighted average number of ordinary shares used for the calculation of basic and diluted earnings per share/ADS for the years ended December 31, 2018, 2019 and 2020 have been retrospectively adjusted.

A reconciliation of net income attributable to Baidu, Inc. in the consolidated statements of comprehensive income (loss) to the numerator for the computation of basic and diluted earnings per share for the years ended December 31, 2018, 2019 and 2020 is as follows:

| | For the years ended December 31, | | |
|---|-------------------------------------|--------------|---------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| Net income attributable to Baidu, Inc. | 27,573 | 2,057 | 22,472 |
| Accretion of the redeemable noncontrolling interests | (130) | (77) | (88) |
| Numerator for basic EPS computation | 27,443 | 1,980 | 22,384 |
| Impact of subsidiaries’ and investees’ diluted earnings per share | — | (28) | — |
| Numerator for diluted EPS computation | <u>27,443</u> | <u>1,952</u> | <u>22,384</u> |

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

21. EARNINGS PER SHARE (“EPS”)—continued

The following table sets forth the computation of basic and diluted earnings per Class A and Class B ordinary share and basic and diluted earnings per ADS:

| | For the years ended December 31, | | | | | |
|--|----------------------------------|----------------|----------------|----------------|----------------|----------------|
| | 2018 | | 2019 | | 2020 | |
| | Class A RMB | Class B RMB | Class A RMB | Class B RMB | Class A RMB | Class B RMB |
| (In millions, including number of shares and ADS, except for per share and per ADS data) | | | | | | |
| Earnings per share—basic: | | | | | | |
| Numerator | | | | | | |
| Allocation of net income attributable to Baidu, Inc. | 21,780 | 5,663 | 1,571 | 409 | 17,683 | 4,701 |
| Denominator | | | | | | |
| Weighted average ordinary shares outstanding (Note) | 2,216 | 576 | 2,211 | 576 | 2,158 | 574 |
| Denominator used for basic EPS (Note) | 2,216 | 576 | 2,211 | 576 | 2,158 | 574 |
| Earnings per share—basic (Note) | 9.83 | 9.83 | 0.71 | 0.71 | 8.19 | 8.19 |
| Earnings per share—diluted: | | | | | | |
| Numerator | | | | | | |
| Allocation of net income attributable to Baidu, Inc. for diluted computation | 21,824 | 5,619 | 1,549 | 403 | 17,723 | 4,661 |
| Reallocation of net income attributable to Baidu, Inc. as a result of conversion of Class B to Class A shares | 5,619 | — | 403 | — | 4,661 | — |
| Numerator for diluted EPS calculation | 27,443 | 5,619 | 1,952 | 403 | 22,384 | 4,661 |
| Denominator | | | | | | |
| Weighted average ordinary shares outstanding (Note) | 2,216 | 576 | 2,211 | 576 | 2,158 | 574 |
| Conversion of Class B to Class A ordinary shares (Note) | 576 | — | 576 | — | 574 | — |
| Share-based awards (Note) | 22 | — | 4 | — | 24 | — |
| Denominator used for diluted EPS (Note) | 2,814 | 576 | 2,791 | 576 | 2,756 | 574 |
| Earnings per share—diluted (Note) | 9.75 | 9.75 | 0.70 | 0.70 | 8.12 | 8.12 |
| Earnings per ADS (1 ADS equals 8 Class A ordinary shares): | | | | | | |
| Denominator used for earnings per ADS—basic (Note) . . . | 277 | | 276 | | 270 | |
| Denominator used for earnings per ADS—diluted (Note) | 352 | | 349 | | 344 | |
| Earnings per ADS—basic (Note) | 78.64 | | 5.68 | | 65.54 | |
| Earnings per ADS—diluted (Note) | 78.03 | | 5.60 | | 64.98 | |

Note: Basic and diluted net income per ordinary share, weighted average number of shares and the adjustments for dilutive restricted share and share options for the years ended December 31, 2018, 2019 and 2020 have been retrospectively adjusted for the Share Subdivision and the ADS Ratio Change that became effective on March 1, 2021, as detailed in Note 2.(a)

The Company did not include certain stock options, restricted shares and the effect of convertible senior notes issued by iQIYI in the computation of diluted earnings per share for the years ended December 31, 2018, 2019 and 2020 because those stock options, restricted shares and convertible senior notes were anti-dilutive for earnings per share for the respective years.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

22. SHARE-BASED AWARDS PLAN

Baidu, Inc.

2008 Share Incentive plan

In December 2008, the Company adopted a share incentive plan (the “2008 Plan”), which provides for the granting of share incentives, including incentive share options (“ISOs”), restricted shares and any other form of award pursuant to the 2008 Plan, to members of the board, employees, consultants and non-employees of the Company. The Company reserved 274,302,160 Class A ordinary shares (previously 3,428,777 Class A ordinary shares before the Share Subdivision as detailed in Note 2.(a)) for issuance under the 2008 Plan, which expired in the year 2018. The vesting schedule, time and condition to exercise options is determined by the Company’s compensation committee. The term of the options may not exceed ten years from the date of the grant, except that five years is the maximum term of an ISO granted to an employee who holds more than 10% of the voting power of the Company’s share capital.

Under the 2008 Plan, the exercise price of an option may be amended or adjusted at the discretion of the compensation committee, the determination of which would be final, binding and conclusive. To the extent not prohibited by applicable laws or exchange rules, a downward adjustment of the exercise prices would be effective without the approval of the Company’s shareholders or the approval of the affected grantees. If the Company grants an ISO to an employee who, at the time of that grant, owns shares representing more than 10% of the voting power of all classes of the Company’s share capital, the exercise price cannot be less than 110% of the fair market value of the Company’s ordinary shares on the date of that grant.

2018 Share Incentive Plan

In July 2018, the Company adopted a share incentive plan (the “2018 Plan”), which provides for the granting of share incentives, including ISOs, restricted shares and any other form of award pursuant to the 2018 Plan, to members of the board, employees, consultants, and non-employees of the Company. The 2018 Plan has a ten-year term and a maximum number of 275,516,000 Class A ordinary shares (previously 3,443,950 Class A ordinary shares before the Share Subdivision as detailed in Note 2.(a)) available for issuance pursuant to all awards under the 2018 Plan.

Under the 2018 Plan, the exercise price of an option may be amended or adjusted at the discretion of the compensation committee, the determination of which would be final, binding and conclusive. To the extent not prohibited by applicable laws or exchange rules, a downward adjustment of the exercise prices would be effective without the approval of the Company’s shareholders or the approval of the affected grantees. If the Company grants an ISO to an employee who, at the time of that grant, owns shares representing more than 10% of the voting power of all classes of the Company’s share capital, the exercise price cannot be less than 110% of the fair market value of the Company’s ordinary shares on the date of that grant.

Following the Share Subdivision that became effective on March 1, 2021 as detailed in Note 2.(a), each ordinary share was subdivided into eighty ordinary shares and each ADS represents eight ordinary shares. Prior and subsequent to March 1, 2021, one ordinary share was and will be issuable upon the vesting of one outstanding restricted share or the exercise of one outstanding share option, respectively. Therefore, following the Share Subdivision, each share option and restricted share is subdivided into eighty share options and eighty restricted shares, the weighted average grant date fair

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

22. SHARE-BASED AWARDS PLAN—continued

Baidu, Inc.—continued

2018 Share Incentive Plan—continued

value per restricted share and the weighted average exercise price per share option is diluted by eighty times. The number of restricted shares and share options, the weighted average grant date fair value per restricted share and the weighted average exercise price per share option has been retrospectively adjusted for the Share Subdivision in the following tables.

Incentive share options

The following table summarizes the option activity for the years ended December 31, 2018, 2019 and 2020:

| | Number of share options <i>(Note)</i> | Weighted average exercise price (US\$) <i>(Note)</i> | Weighted average remaining contractual life (Years) | Aggregate intrinsic value (US\$ in millions) |
|--|--|---|---|--|
| Incentive share options | | | | |
| Outstanding, December 31, 2017 | 25,231,760 | 22 | 8 | 186 |
| Granted | 6,812,720 | 22 | | |
| Exercised | (5,338,160) | 20 | | |
| Forfeited/Cancelled | (8,651,600) | 23 | | |
| Outstanding, December 31, 2018 | <u>18,054,720</u> | <u>22</u> | <u>7</u> | <u>40</u> |
| Vested and expected to vest at December 31, 2018 | <u>15,344,880</u> | <u>21</u> | <u>7</u> | <u>38</u> |
| Exercisable at December 31, 2018 | <u>8,691,120</u> | <u>19</u> | <u>6</u> | <u>31</u> |
| Outstanding, December 31, 2018 | 18,054,720 | 22 | 7 | 40 |
| Granted | 18,492,160 | 12 | | |
| Exercised | (947,920) | 3 | | |
| Forfeited/Cancelled | (5,744,480) | 21 | | |
| Outstanding, December 31, 2019 | <u>29,854,480</u> | <u>17</u> | <u>8</u> | <u>72</u> |
| Vested and expected to vest at December 31, 2019 | <u>23,836,480</u> | <u>17</u> | <u>8</u> | <u>53</u> |
| Exercisable at December 31, 2019 | <u>9,834,640</u> | <u>22</u> | <u>5</u> | <u>7</u> |
| Outstanding, December 31, 2019 | 29,854,480 | 17 | 8 | 72 |
| Granted | 1,028,240 | 11 | | |
| Exercised | (3,516,400) | 13 | | |
| Forfeited/Cancelled | (3,147,280) | 17 | | |
| Outstanding, December 31, 2020 | <u>24,219,040</u> | <u>17</u> | <u>7</u> | <u>245</u> |
| Vested and expected to vest at December 31, 2020 | <u>19,756,080</u> | <u>18</u> | <u>7</u> | <u>186</u> |
| Exercisable at December 31, 2020 | <u>12,098,400</u> | <u>21</u> | <u>5</u> | <u>78</u> |

Note: The number of share options and weighted average exercise price have been retrospectively adjusted for the Share Subdivision that became effective on March 1, 2021 as detailed in Note 2.(a) and Note 21.

The aggregate intrinsic value in the table above represents the difference between the Company’s closing stock price on the last trading day in 2020 and the exercise price.

Total intrinsic value of options exercised for the years ended December 31, 2018, 2019 and 2020 was RMB474 million, RMB77 million and RMB157 million, respectively. The total fair value of options

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

22. SHARE-BASED AWARDS PLAN—continued

Baidu, Inc.—continued

Incentive share options—continued

vested during the years ended December 31, 2018, 2019 and 2020 was RMB956 million, RMB216 million and RMB261 million, respectively.

Share options are usually subject to vesting schedules ranging from two to four years. As of December 31, 2020, RMB215 million of unrecognized share-based compensation cost related to share options is expected to be recognized over a weighted-average vesting period of 1.8 years. To the extent the actual forfeiture rate is different from the original estimate, actual share-based compensation costs related to these awards may be different from expectation.

The fair value of each option award was estimated on the date of grant using the Black-Scholes-Merton valuation model. The volatility assumption was estimated based on historical volatility of the Company’s share price applying the guidance provided by ASC 718. Assumptions of the expected term were based on the vesting and contractual terms and employee demographics. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

The following table presents the assumptions used to estimate the fair values of the share options granted in the years presented:

| | For the years ended December 31, | | |
|-------------------------------------|----------------------------------|---------------|---------------|
| | 2018 | 2019 | 2020 |
| Risk-free interest rate | 2.57% | 1.58%~2.49% | 1.51~1.52% |
| Dividend yield | — | — | — |
| Expected volatility range | 34.47%~35.36% | 34.62%~35.14% | 34.83%~34.92% |
| Expected life (in years) | 4.89~6.25 | 5.83~6.03 | 5.90~6.01 |

In addition, the Company recognizes share-based compensation expense net of estimated forfeiture rates, to recognize compensation cost for shares expected to vest over the service period of the award. Estimated forfeiture rates are primarily based on historical experience of employee turnover. To the extent the Company revises this estimate in the future, share-based compensation expense could be materially impacted in the year of revision, as well as in the following years.

The exercise price of options granted during the years ended December 31, 2018, 2019 and 2020 equaled the market price of the ordinary shares on the grant date. The weighted-average grant-date fair value of options granted during the years ended December 31, 2018, 2019, and 2020 was US\$13, US\$5, and US\$9, respectively.

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ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

22. SHARE-BASED AWARDS PLAN—continued

Baidu, Inc.—continued

Restricted Shares

Restricted Shares activity for the years ended December 31, 2018, 2019, and 2020 was as follow:

| | Number of restricted shares <i>(Note)</i> | Weighted average grant date fair value (US\$) <i>(Note)</i> |
|-----------------------------|---|--|
| Restricted Shares | | |
| Unvested, December 31, 2017 | 65,573,600 | 24 |
| Granted | 34,211,360 | 28 |
| Vested | (20,732,160) | 24 |
| Forfeited/Cancelled | <u>(15,737,280)</u> | <u>24</u> |
| Unvested, December 31, 2018 | 63,315,520 | 26 |
| Granted | 89,828,560 | 16 |
| Vested | (24,049,120) | 25 |
| Forfeited/Cancelled | <u>(15,490,640)</u> | <u>23</u> |
| Unvested, December 31, 2019 | 113,604,320 | 19 |
| Granted | 73,900,080 | 14 |
| Vested | (35,078,640) | 20 |
| Forfeited/Cancelled | <u>(21,924,240)</u> | <u>17</u> |
| Unvested, December 31, 2020 | <u>130,501,520</u> | <u>16</u> |

Note: The number of restricted shares and weighted average grant date fair value have been retrospectively adjusted for the Share Subdivision that became effective on March 1, 2021 as detailed in Note 2.(a) and Note 21.

The total fair value of the Restricted Shares vested during the years ended December 31, 2018, 2019 and 2020 was RMB3.4 billion, RMB4.1 billion, RMB4.6 billion, respectively. The weighted-average grant-date fair value of the Restricted Shares granted during the years ended December 31, 2018, 2019, and 2020 was US\$28, US\$16, and US\$14, respectively.

As of December 31, 2020, there was RMB6.4 billion of unrecognized share-based compensation cost related to Restricted Shares, which is expected to be recognized over a weighted-average vesting period of 3.0 years. To the extent the actual forfeiture rate is different from the original estimate, the actual share-based compensation costs related to these awards may be different from expectation. To the extent the Company revises this estimate in the future, share-based compensation expense could be materially impacted in the year of revision, as well as in the following years.

Subsidiaries-iQIYI

2010 Equity Incentive Plan

In October 2010, iQIYI adopted its 2010 Equity Incentive Plan (the “iQIYI 2010 Plan”), which permits the grant of restricted shares, options and share appreciation rights to the employees, directors, officers and consultants to purchase iQIYI’s ordinary shares. The 2010 Plan is valid and effective for an original term of ten years, and further extended to twenty years on September 15, 2020 commencing from its adoption. Except for service conditions, there were no other vesting conditions for all the awards under the 2010 Plan. As of December 31, 2020, the share option pool under the iQIYI 2010

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

22. SHARE-BASED AWARDS PLAN—continued

Subsidiaries-iQIYI—continued

2010 Equity Incentive Plan—continued

Plan approved by the Board of Directors of iQIYI was 589,729,714 iQIYI’s ordinary shares. All options granted vest over a four-year period, with 25% of the awards vesting on the first anniversary, and the remaining 75% of the awards vesting on a quarterly basis thereafter.

The following table sets forth the summary of employee option activity under the iQIYI’s 2010 Plan:

| | Number of share options | Weighted average exercise price (US\$) | Weighted average remaining contractual life (Years) | Aggregate intrinsic value (US\$ in millions) |
|--|----------------------------|--|--|---|
| Outstanding, December 31, 2017 | 306,266,366 | 0.45 | | |
| Granted | 112,846,527 | 0.51 | | |
| Forfeited | (13,474,664) | 0.51 | | |
| Exercised | (25,059,198) | 0.42 | | |
| Outstanding, December 31, 2018 | <u>380,579,031</u> | <u>0.47</u> | <u>9</u> | <u>630</u> |
| Vested and expected to vest at | | | | |
| December 31, 2018 | 382,422,243 | 0.46 | 7 | 635 |
| Exercisable at December 31, 2018 | <u>184,247,256</u> | <u>0.42</u> | <u>6</u> | <u>314</u> |
| Outstanding, December 31, 2018 | 380,579,031 | 0.47 | 9 | 630 |
| Granted | 94,625,573 | 0.51 | | |
| Forfeited | (8,855,266) | 0.51 | | |
| Exercised | (59,436,720) | 0.37 | | |
| Outstanding, December 31, 2019 | <u>406,912,618</u> | <u>0.48</u> | <u>7</u> | <u>1,031</u> |
| Vested and expected to vest | | | | |
| at December 31, 2019 | 385,280,004 | 0.48 | 7 | 977 |
| Exercisable at December 31, 2019 | <u>211,537,760</u> | <u>0.45</u> | <u>6</u> | <u>542</u> |
| Outstanding, December 31, 2019 | 406,912,618 | 0.48 | 7 | 1,031 |
| Granted | 88,611,584 | 0.51 | | |
| Forfeited | (12,111,374) | 0.51 | | |
| Exercised | (62,714,554) | 0.44 | | |
| Outstanding, December 31, 2020 | <u>420,698,274</u> | <u>0.49</u> | <u>7</u> | <u>846</u> |
| Vested and expected to vest at | | | | |
| December 31, 2020 | 401,055,919 | 0.48 | 7 | 807 |
| Exercisable at December 31, 2020 | <u>245,054,484</u> | <u>0.47</u> | <u>7</u> | <u>498</u> |

As of December 31, 2020, there was RMB2.2 billion of unrecognized share-based compensation cost related to share options granted by iQIYI. That deferred cost is expected to be recognized over a weighted-average vesting period of 2.7 years.

2017 Share Incentive Plan

In November 2017, iQIYI adopted its 2017 Share Incentive Plan (the “iQIYI 2017 Plan”). Under the iQIYI 2017 Plan, iQIYI is authorized to grant options, restricted shares and restricted share units to members of the board, employees, consultants and other individuals for which the maximum aggregate number of ordinary shares which may be issued pursuant to all awards is 720,000 iQIYI’s ordinary

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

22. SHARE-BASED AWARDS PLAN—continued

Subsidiaries-iQIYI—continued

2017 Share Incentive Plan—continued

shares. The iQIYI 2017 Plan is valid and effective for a term of ten years commencing from its adoption. Except for service conditions, there are no other vesting conditions for all the awards issued under the 2017 Plan. As of December 31, 2020, the unrecognized share-based compensation cost related to its Restricted Shares is insignificant.

The following table summarizes the share-based compensation cost recognized by iQIYI:

| | For the years ended December 31, | | |
|---|-------------------------------------|--------------|--------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| Expensed as cost of revenues | 83 | 171 | 202 |
| Expensed as selling, general and administrative | 369 | 676 | 851 |
| Expensed as research and development | 104 | 238 | 317 |
| | <u>556</u> | <u>1,085</u> | <u>1,370</u> |

The following table summarizes the total share-based compensation cost recognized by the Group:

| | For the years ended December 31, | | |
|---|-------------------------------------|--------------|--------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| Expensed as cost of revenues | 224 | 327 | 360 |
| Expensed as selling, general and administrative | 1,725 | 1,768 | 1,897 |
| Expensed as research and development | 2,727 | 3,531 | 4,471 |
| | <u>4,676</u> | <u>5,626</u> | <u>6,728</u> |

23. RELATED PARTY TRANSACTIONS

Related party transactions primarily related to online marketing services, cloud services and other services provided by the Company to certain investees. The following table summarizes the revenue received from major related parties in fiscal year 2018, 2019 and 2020.

| | For the years ended December 31, | | |
|---------------------------|-------------------------------------|--------------|--------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| | (In millions) | | |
| Revenues: | | | |
| Trip | 774 | 627 | 204 |
| Du Xiaoman | 256 | 731 | 678 |
| Investee C ⁽ⁱ⁾ | 143 | 280 | 949 |
| Others | 421 | 1,394 | 1,015 |
| Total | <u>1,594</u> | <u>3,032</u> | <u>2,846</u> |

Note:

(i) Investee C is one of the Company’s investees, over which the Company has significant influence.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

23. RELATED PARTY TRANSACTIONS—continued

The Group purchased produced content and licensed copyrights, traffic acquisition and other services from equity investees in an amount of RMB297 million, RMB3.0 billion and RMB1.9 billion for the years ended December 31, 2018, 2019 and 2020, respectively. Other related party transactions were insignificant for each of the years presented, which included reimbursements to Robin Li’s use of an aircraft beneficially owned by his family member used for the Company’s business purposes.

Except for the non-trade balances disclosed below, amounts due from/due to related parties as of December 31, 2018, 2019 and 2020 relate to transactions arising from the ordinary and usual course of business of the Group and were trade in nature.

| | As of December 31, | | |
|---|--------------------|----------------------|--------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB (In millions) | RMB |
| Amounts due from related parties, current: | | | |
| Trip ⁽ⁱ⁾ | 58 | 96 | 22 |
| Du Xiaoman ⁽ⁱⁱ⁾ | 77 | 737 | 306 |
| Investee A ⁽ⁱⁱⁱ⁾ | 325 | 345 | — |
| Investee C ^(iv) | — | 115 | 212 |
| Other related parties ^(v) | 325 | 301 | 186 |
| Total | <u>785</u> | <u>1,594</u> | <u>726</u> |
| Amounts due from related parties, non-current: | | | |
| Du Xiaoman ⁽ⁱⁱ⁾ | 3,884 | 3,391 | 3,398 |
| Other related parties ^(vi) | 413 | 173 | 40 |
| Total | <u>4,297</u> | <u>3,564</u> | <u>3,438</u> |
| Amounts due to related parties, current: | | | |
| Trip ^(vii) | 12 | 49 | 50 |
| Du Xiaoman ^(viii) | 934 | 973 | 489 |
| Investee A ^(ix) | 488 | 476 | — |
| Investee B ^(x) | 186 | 249 | 175 |
| Other related parties ^(xi) | 107 | 484 | 610 |
| Total | <u>1,727</u> | <u>2,231</u> | <u>1,324</u> |
| Amounts due to related parties, non-current: | | | |
| Du Xiaoman ^(xii) | 3,729 | 3,430 | 3,216 |
| Investee B ^(x) | 631 | 410 | 325 |
| Other related parties ^(xiii) | — | 6 | 2 |
| Total | <u>4,360</u> | <u>3,846</u> | <u>3,543</u> |

Notes:

- (i) The balances mainly represent amounts arising from services the Company provided to Trip.
- (ii) The balances represent non-trade long-term loans due from Du Xiaoman with interest rates ranging from 0.00% to 0.50% in 2020, and amounts arising from services the Company provided to Du Xiaoman.
- (iii) The balance mainly represents a non-trade interest-bearing loan provided to Investee A, which was an equity investee as of December 31, 2019. The Company acquired Investee A on July 16, 2020, and accordingly, all corresponding outstanding balance has been eliminated in the consolidated balance sheet.
- (iv) The balances mainly represent amounts arising from services including online marketing services and cloud services the Company provided to Investee C.
- (v) The balances mainly represent amounts arising from services the Company provided to its investees in ordinary course of business.
- (vi) The balance consists of amount due from the Company’s investees in the ordinary course of business.
- (vii) The balances mainly represent amounts arising from services provided by Trip.

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

23. RELATED PARTY TRANSACTIONS—continued

- (viii) The balance represents amount due to Du Xiaoman arising from services provided by Du Xiaoman to the Company in the ordinary course of business and non-trade loans provided by Du Xiaoman with interest rates of nil in 2020.
- (ix) The balances mainly represent amounts arising from hardware products purchased from Investee A, and a non-trade interest-bearing loan provided by the Investee A, as of December 31, 2019. The Company acquired Investee A on July 16, 2020, and accordingly, all corresponding outstanding balances have been eliminated in the consolidated balance sheet.
- (x) The balances mainly represent deferred revenue relating to the future services to be provided by the Company to Investee B which is an equity method investee.
- (xi) The balances mainly represent amounts arising from services including advertising services and licensing of content assets provided by the Company’s investees and non-trade amounts payable for acquiring the equity interest of the Company’s investees.
- (xii) The balances mainly represent non-trade interest-free long-term loans provided by Du Xiaoman.
- (xiii) The balance represents mainly deferred revenue relating to the future services to be provided by the Company to investees.

24. SEGMENT REPORTING

The Company’s operations are organized into two segments, consisting of Baidu Core and iQIYI. Within Baidu Core, the Company’s product and services offerings are categorized as follows—Mobile Ecosystem, Baidu Cloud and Apollo Intelligent Driving & Other Growth Initiatives. iQIYI is an innovative market-leading online entertainment service iQIYI produces, aggregates, and distributes a wide variety of professionally produced content (PPC), as well as a broad spectrum of other video content in a variety of formats.

The Company derives the results of the segments directly from its internal management reporting system. The CODM reviews the performance of each segment based on its operating results and uses these results to evaluate the performance of, and to allocate resources to, each of the segments. Because substantially all of the Group’s long-lived assets and revenues are located in and derived from the PRC, geographical segments are not presented. The Company does not allocate assets to its segments as the CODM does not evaluate the performance of segments using asset information.

The table below provides a summary of the Group’s operating segment operating results for the year ended December 31, 2018.

| | For the year ended December 31, 2018 | | | |
|--|--------------------------------------|----------------|---|---------------------|
| | Baidu Core RMB | iQIYI RMB | Intersegment eliminations & adjustments RMB (In millions) | Consolidated RMB |
| Total revenues | 78,271 | 24,989 | (983) | 102,277 |
| Operating costs and expenses: | | | | |
| Cost of revenues | 25,370 | 27,133 | (759) | 51,744 |
| Selling, general and administrative | 15,310 | 4,168 | (247) | 19,231 |
| Research and development | 13,783 | 1,994 | (5) | 15,772 |
| Total operating costs and expenses | 54,463 | 33,295 | (1,011) | 86,747 |
| Operating profit (loss) | 23,808 | (8,306) | 28 | 15,530 |
| Total other income (loss), net | 13,169 | (676) | (698) | 11,795 |
| Income (loss) before income taxes | 36,977 | (8,982) | (670) | 27,325 |
| Income taxes | 4,664 | 79 | — | 4,743 |
| Net income (loss) | 32,313 | (9,061) | (670) | 22,582 |
| Less: net income (loss) attributable to noncontrolling interests | (1,292) | 49 | (3,748) | (4,991) |
| Net income (loss) attributable to Baidu, Inc. | 33,605 | (9,110) | 3,078 | 27,573 |

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

24. SEGMENT REPORTING—continued

The table below provides a summary of the Group’s operating segment operating results for the year ended December 31, 2019.

| | For the year ended December 31, 2019 | | | |
|--|--------------------------------------|-----------------|---------------------------|----------------|
| | Baidu Core | iQIYI | Intersegment eliminations | Consolidated |
| | RMB | RMB | RMB | RMB |
| | (In millions) | | | |
| Total revenues | 79,711 | 28,994 | (1,292) | 107,413 |
| Operating costs and expenses: | | | | |
| Cost of revenues | 34,019 | 30,348 | (1,517) | 62,850 |
| Selling, general and administrative | 14,733 | 5,237 | (60) | 19,910 |
| Research and development | 15,698 | 2,667 | (19) | 18,346 |
| Total operating costs and expenses | 64,450 | 38,252 | (1,596) | 101,106 |
| Operating profit (loss) | 15,261 | (9,258) | 304 | 6,307 |
| Total other income (loss), net | (5,680) | (967) | — | (6,647) |
| Income (loss) before income taxes | 9,581 | (10,225) | 304 | (340) |
| Income taxes | 1,896 | 52 | — | 1,948 |
| Net income (loss) | 7,685 | (10,277) | 304 | (2,288) |
| Less: net income (loss) attributable to noncontrolling interests | 105 | 46 | (4,496) | (4,345) |
| Net income (loss) attributable to Baidu, Inc. | 7,580 | (10,323) | 4,800 | 2,057 |

The table below provides a summary of the Group’s operating segment operating results for the year ended December 31, 2020.

| | For the year ended December 31, 2020 | | | |
|--|--------------------------------------|----------------|---------------------------|----------------|
| | Baidu Core | iQIYI | Intersegment eliminations | Consolidated |
| | RMB | RMB | RMB | RMB |
| | (In millions) | | | |
| Total revenues | 78,684 | 29,707 | (1,317) | 107,074 |
| Operating costs and expenses: | | | | |
| Cost of revenues | 28,368 | 27,884 | (1,094) | 55,158 |
| Selling, general and administrative | 12,931 | 5,188 | (56) | 18,063 |
| Research and development | 16,847 | 2,676 | (10) | 19,513 |
| Total operating costs and expenses | 58,146 | 35,748 | (1,160) | 92,734 |
| Operating profit (loss) | 20,538 | (6,041) | (157) | 14,340 |
| Total other income (loss), net | 9,693 | (943) | — | 8,750 |
| Income (loss) before income taxes | 30,231 | (6,984) | (157) | 23,090 |
| Income taxes | 4,041 | 23 | — | 4,064 |
| Net income (loss) | 26,190 | (7,007) | (157) | 19,026 |
| Less: net income (loss) attributable to noncontrolling interests | (334) | 31 | (3,143) | (3,446) |
| Net income (loss) attributable to Baidu, Inc. | 26,524 | (7,038) | 2,986 | 22,472 |

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

24. SEGMENT REPORTING—continued

The following table presents the Company’s revenues disaggregated by segment and by types of products or services:

| | For the years ended | | |
|--|----------------------|----------------------|----------------------|
| | December 31, 2018 | December 31, 2019 | December 31, 2020 |
| | RMB | RMB (In millions) | RMB |
| Online marketing services | 72,645 | 70,038 | 66,283 |
| Cloud services (Note 1) | 3,005 | 6,370 | 9,173 |
| Interest income earned from provision of financial services | 1,724 | — | — |
| Others (Note 1) | 897 | 3,303 | 3,228 |
| Baidu Core subtotal | 78,271 | 79,711 | 78,684 |
| Membership services (Note 1) | 10,623 | 14,436 | 16,491 |
| Online advertising services (Note 2) | 9,329 | 8,271 | 6,822 |
| Content distribution (Note 1) | 2,163 | 2,544 | 2,660 |
| Others (Note 1) | 2,874 | 3,743 | 3,734 |
| iQIYI subtotal | 24,989 | 28,994 | 29,707 |
| Intersegment eliminations | (983) | (1,292) | (1,317) |
| Total revenues | 102,277 | 107,413 | 107,074 |

Note 1: The revenues were presented as “Others” in the consolidated statements of comprehensive income (loss)

Note 2: The revenues were presented as “Online marketing revenues” in the consolidated statements of comprehensive income (loss)

25. FAIR VALUE MEASUREMENTS

ASC 820 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

Level 1 – Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 – Include observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets and liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data.

Level 3 – Unobservable inputs which are supported by little or no market activity.

ASC 820 describes three main approaches to measuring the fair value of assets and liabilities: (1) market approach; (2) income approach and (3) cost approach. The market approach uses prices and other relevant information generated from market transactions involving identical or comparable assets or liabilities. The income approach uses valuation techniques to convert future amounts to a single present value amount. The measurement is based on the value indicated by current market expectations about those future amounts. The cost approach is based on the amount that would currently be required to replace an asset.

Assets and Liabilities Measured or Disclosed at Fair Value on a recurring basis

In accordance with ASC 820, the Company measures equity investments with readily determinable fair value, investments accounted for at fair value, available-for-sale debt investments and derivatives

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

25. FAIR VALUE MEASUREMENTS—continued

Assets and Liabilities Measured or Disclosed at Fair Value on a recurring basis—continued

instruments at fair value on a recurring basis. The fair value of time deposits are determined based on the prevailing interest rates in the market. The fair values of the Company’s held-to-maturity debt investments as disclosed are determined based on the discounted cash flow model using the discount curve of market interest rates. The fair value of the Company’s short-term available-for-sale debt investments are measured using the income approach, based on quoted market interest rates of a similar instrument and other significant inputs derived from or corroborated by observable market data. The fair values of the Company’s investments in equity securities of publicly listed companies are measured using quoted market prices. The fair value of derivative instruments of interest rate swaps are based on broker quotes. The fair value of financial liability is estimated based on the quoted market price of a similar asset to the underlying assets. Investments accounted for at fair value are equity investments in unlisted companies held by consolidated investment companies, these investments and long-term available-for-sale debt investments do not have readily determinable market value, which were categorized as Level 3 in the fair value hierarchy. The Company uses a combination of valuation methodologies, including market and income approaches based on the Company’s best estimate, which is determined by using information including but not limited to the pricing of recent rounds of financing of the investees, future cash flow forecasts, liquidity factors and multiples of a selection of comparable companies.

The fair value of the Company’s notes payable are extracted directly from their quoted market prices. The fair value of the convertible senior notes are based on broker quotes. The Company carries the convertible senior notes at face value less unamortized debt discount and issuance costs on its consolidated balance sheets and presents the fair value for disclosure purposes only.

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

25. FAIR VALUE MEASUREMENTS—continued

Assets and Liabilities Measured or Disclosed at Fair Value on a recurring basis—continued

Assets and liabilities measured on a recurring basis or disclosed at fair value are summarized below:

| | Total fair value at December 31, 2018 | Fair value measurement or disclosure at December 31, 2018 using | | |
|--|--|---|--|--|
| | | Quoted prices in active markets for identical assets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) |
| | | RMB (In millions) | RMB | RMB |
| <i>Fair value disclosure</i> | | | | |
| Cash equivalents | | | | |
| Time deposits | 4,264 | | 4,264 | |
| Money market funds | 3,723 | 3,723 | | |
| Short-term investments | | | | |
| Held-to-maturity debt investments | 27,507 | | 27,507 | |
| Long-term notes payable | 68,763 | | 68,763 | |
| Convertible senior notes | 4,923 | | 4,923 | |
| <i>Fair value measurements on a recurring basis</i> | | | | |
| Short-term investments | | | | |
| Available-for-sale debt investments | 84,238 | | 84,238 | |
| Long-term investments | | | | |
| Equity investments at fair value with readily determinable fair value | 4,428 | 4,428 | | |
| Investments accounted for at fair value | 1,457 | | | 1,457 |
| Available-for-sale debt investments | 1,167 | | | 1,167 |
| Other non-current assets | | | | |
| Derivative instruments | 193 | | 187 | 6 |
| Total assets measured at fair value | 86,803 | 4,428 | 79,745 | 2,630 |
| Accounts payable and accrued liabilities | | | | |
| Derivative instruments | 123 | | | 123 |
| Amounts due to related parties, non-current | | | | |
| Financial liability | 341 | | 341 | |
| Total liabilities measured at fair value | 464 | — | 341 | 123 |

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

25. FAIR VALUE MEASUREMENTS—continued

Assets and Liabilities Measured or Disclosed at Fair Value on a recurring basis—continued

| | Total fair value at December 31, 2019 | Fair value measurement or disclosure at December 31, 2019 using | | |
|--|--|---|--|--|
| | | Quoted prices in active markets for identical assets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) |
| | | RMB | RMB | RMB |
| | | (In millions) | | |
| <i>Fair value disclosure</i> | | | | |
| Cash equivalents: | | | | |
| Time deposits | 10,848 | | 10,848 | |
| Money market funds | 1,719 | 1,719 | | |
| Short-term investments: | | | | |
| Held-to-maturity debt investments | 107,654 | | 107,654 | |
| Long-term investments: | | | | |
| Held-to-maturity debt investment | 491 | | 491 | |
| Long-term notes payable | 45,282 | | 45,282 | |
| Convertible senior notes | 14,142 | | 14,142 | |
| <i>Fair value measurements on a recurring basis</i> | | | | |
| Short-term investments: | | | | |
| Available-for-sale debt investments | 5,637 | | 5,637 | |
| Long-term investments: | | | | |
| Equity investments at fair value with readily determinable fair value | 11,334 | 11,334 | | |
| Investments accounted for at fair value | 1,819 | | | 1,819 |
| Available-for-sale debt investments | 3,970 | | | 3,970 |
| Other non-current assets: | | | | |
| Derivative instruments | 24 | | 24 | |
| Total assets measured at fair value | 22,784 | 11,334 | 5,661 | 5,789 |
| Accounts payable and accrued liabilities: | | | | |
| Derivative instruments | 125 | | | 125 |
| Amounts due to related parties, non-current: | | | | |
| Financial liability | 401 | | 401 | |
| Total liabilities measured at fair value | 526 | — | 401 | 125 |

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ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

25. FAIR VALUE MEASUREMENTS—continued

Assets and Liabilities Measured or Disclosed at Fair Value on a recurring basis—continued

| | Fair value measurement or disclosure at December 31, 2020 using | | | |
|---|---|--|---|---|
| | Total fair value at December 31, 2020 | Quoted prices in active markets for identical assets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) |
| | RMB | RMB | RMB | RMB |
| | (In millions) | | | |
| <i>Fair value disclosure</i> | | | | |
| Cash equivalents: | | | | |
| Time deposits | 16,133 | | 16,133 | |
| Money market funds | 198 | 198 | | |
| Short-term investments: | | | | |
| Held-to-maturity debt investments | 124,132 | | 124,132 | |
| Convertible senior notes, current portion | 4,967 | | 4,967 | |
| Long-term investments: | | | | |
| Held-to-maturity debt investment | 9,754 | | 9,754 | |
| Long-term notes payable | 52,575 | | 52,575 | |
| Convertible senior notes, non-current portion | 12,078 | | 12,078 | |
| <i>Fair value measurements on a recurring basis</i> | | | | |
| Short-term investments: | | | | |
| Available-for-sale debt investments | 2,865 | | 2,865 | |
| Long-term investments: | | | | |
| Equity investments at fair value with readily determinable fair value | 12,978 | 12,978 | | |
| Investments accounted for at fair value | 2,238 | | | 2,238 |
| Available-for-sale debt investments | 2,607 | | | 2,607 |
| Total assets measured at fair value | 20,688 | 12,978 | 2,865 | 4,845 |
| Accounts payable and accrued liabilities: | | | | |
| Derivative instruments | 40 | | 40 | |
| Amounts due to related parties, current: | | | | |
| Financial liability | 327 | | 327 | |
| Total liabilities measured at fair value | 367 | — | 367 | — |

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ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

25. FAIR VALUE MEASUREMENTS—continued

Assets and Liabilities Measured or Disclosed at Fair Value on a recurring basis—continued

Reconciliations of assets categorized within Level 3 under the fair value hierarchy are as follow:

Investments accounted for at fair value:

| | <u>Amounts</u> |
|---|----------------------|
| | <u>RMB</u> |
| | <u>(In millions)</u> |
| Balance at December 31, 2017 | 321 |
| Additions | 822 |
| Disposals | (5) |
| Net unrealized fair value increase recognized in earning | 293 |
| Foreign currency translation adjustments | 26 |
| Balance at December 31, 2018 | 1,457 |
| Additions | 282 |
| Disposals | (128) |
| Net unrealized fair value increase recognized in earnings | 197 |
| Foreign currency translation adjustments | 11 |
| Balance at December 31, 2019 | 1,819 |
| Additions | 371 |
| Disposals | (63) |
| Net unrealized fair value increase recognized in earnings | 151 |
| Foreign currency translation adjustments | (40) |
| Balance at December 31, 2020 | 2,238 |

Available-for-sale debt investments:

| | <u>Amounts</u> |
|---|----------------------|
| | <u>RMB</u> |
| | <u>(In millions)</u> |
| Balance at December 31, 2017 | — |
| Additions | 1,167 |
| Balance at December 31, 2018 | 1,167 |
| Additions | 2,785 |
| Disposals | (20) |
| Net unrealized fair value increase recognized in other comprehensive income | 91 |
| Accrued interest | 48 |
| Impairment | (81) |
| Foreign currency translation adjustments | (20) |
| Balance at December 31, 2019 | 3,970 |
| Additions | 5 |
| Disposals | (500) |
| Reclassification | 412 |
| Conversion to equity investment | (1,355) |
| Share of losses in excess of equity method investment in ordinary shares | (82) |
| Net unrealized fair value increase recognized in other comprehensive income | 153 |
| Accrued interest | 68 |
| Foreign currency translation adjustments | (64) |
| Balance at December 31, 2020 | 2,607 |

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

25. FAIR VALUE MEASUREMENTS—continued

Assets measured at fair value on a non-recurring basis

The Company measures certain non-financial assets on a nonrecurring basis

For equity securities accounted for under the measurement alternative, when there are observable price changes in orderly transactions for identical or similar investments of the same issuer, the investments are re-measured to fair value (Note 4). The non-recurring fair value measurements to the carrying amount of an investment usually requires management to estimate a price adjustment for the different rights and obligations between a similar instrument of the same issuer with an observable price change in an orderly transaction and the investment held by the Company. These non-recurring fair value measurements were measured as of the observable transaction dates. The valuation methodologies involved require management to use the observable transaction price at the transaction date and other unobservable inputs (level 3) such as expected volatility and probability of exit events as it relates to liquidation and redemption preferences. When there is impairment of equity securities accounted for under the measurement alternative and equity method investments, the non-recurring fair value measurements are measured at the date of impairment. The fair values of the Company’s equity method investments in publicly listed companies are measured using quoted market prices. Estimating the fair value of investees without observable market prices is highly judgmental due to the subjectivity of the unobservable inputs (level 3) used in the valuation methodologies used to determine fair value, especially considering the increased market volatility in the global financial markets after the COVID-19 outbreak. The Company uses valuation methodologies, primarily the market approach, which requires management to use unobservable inputs (level 3) such as selection of comparable companies and multiples, expected volatility, discount for lack of marketability and probability of exit events as it relates to liquidation and redemption preferences when applicable. These unobservable inputs and resulting fair value estimates may be affected by unexpected changes in future market or economic conditions. The fair value information presented is not as of the period’s end, and is sensitive to changes in the unobservable inputs used to determine fair value and such changes could result in the fair value at the reporting date to be different from the fair value presented.

Other non-financial assets, intangible assets, licensed copyrights and produced content, would be measured at fair value whenever events or changes in circumstances indicate the carrying value of an asset may not be recoverable. The fair values of non-financial long-lived assets were measured under income approach, based on the Company’s best estimation. Significant inputs used in the income approach primarily included future estimated cash flows and discount rate.

APPENDIX IA

ACCOUNTANTS’ REPORT

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

25. FAIR VALUE MEASUREMENTS—continued

Assets measured at fair value on a non-recurring basis—continued

The following table summarizes the Company’s financial assets held as of December 31, 2018, 2019 and 2020 for which a non-recurring fair value measurement was recorded during the years ended December 31, 2018, 2019 and 2020:

| | Total Balance | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable inputs (Level 2) | Significant unobservable inputs (Level 3) | Fair value adjustment | Impairment |
|--|---------------|---|---|--|--------------------------|------------|
| | RMB | RMB | RMB | RMB | RMB | RMB |
| | (In millions) | | | | | |
| <i>Fair value measurements on a non-recurring basis</i> | | | | | | |
| As of December 31, 2018 | | | | | | |
| Long-term investments | 19,739 | — | 4,983 | 14,756 | 3,512 | (622) |
| Intangible assets | — | — | — | — | — | (5) |
| As of December 31, 2019 | | | | | | |
| Long-term investments | 22,778 | 14,105 | 358 | 8,315 | (230) | (9,989) |
| Intangible assets | 76 | — | — | 76 | — | (406) |
| As of December 31, 2020 | | | | | | |
| Long-term investments (i) | 14,205 | 367 | — | 13,838 | 3,725 | (1,862) |
| Intangible assets (i) | 62 | — | — | 62 | — | (350) |
| Mainland China film group—Licensed copyrights as of March 31, 2020 (ii) | 7,186 | — | — | 7,186 | — | (390) |
| Mainland China film group – Produced contents as of March 31, 2020 (ii) | 4,124 | — | — | 4,124 | — | (210) |
| Produced content monetized on its own (ii) | 40 | — | — | 40 | — | (205) |

Notes:

- (i) Due to factors such as the outbreak of coronavirus (COVID-19) resulting in declined financial performances and changes in business circumstances of certain investees, the Company recognized impairment charges of long-term investments as of March 31, 2020, June 30, 2020 and December 31, 2020. For equity securities accounted for under the measurement alternative, when there are observable price changes in orderly transactions for identical or similar investments of the same issuer, the investments are re-measured to fair value. The Company also recognized impairment loss on intangible assets as of March 31, 2020.
- (ii) The outbreak of COVID-19 during the first quarter of 2020 also has resulted in a downward adjustment to forecasted advertising revenues for the Mainland China film group. As a result, the Company performed an assessment to determine whether the fair value of the Mainland China film group was less than its unamortized film costs as of March 31, 2020 with the assistance of a third-party valuation firm. The Company uses a discounted cash flow approach to estimate the fair value. The Company estimated the most likely future cash flows based on historical results, economic useful lives or license periods and perception of future performance. The Company has incorporated those cash outflows necessary to generate the cash inflows, including future production, operation, exploitation and administrative costs, which were estimated at 32%-37% of revenue in aggregate. The discount rate was determined to be the weighted average cost of capital of the Mainland China film group at 15%. As of March 31, 2020, the fair value of the Mainland China film group was less than its corresponding carrying value and resulted in the Company recognizing an impairment charge of RMB390 million related to licensed copyrights and RMB210 million related to produced content, respectively. The impairment charge was recognized as cost of revenues in the condensed consolidated statement of comprehensive income for the year ended December 31, 2020. In addition, due to adverse changes in the expected performance of certain produced content and the reduced amount of ultimate revenue expected to be recognized, an impairment charge of RMB205 million was recognized for produced content predominantly monetized on its own and was recognized as “Cost of revenues” in the consolidated statement of comprehensive income for the year ended December 31, 2020.

26. SUBSEQUENT EVENTS

Acquisition of YY Live

In November 2020, the Company entered into definitive agreements with JOYY Inc. (“JOYY”), subsequently amended in February 2021, to acquire JOYY’s domestic video-based entertainment live streaming business in China (“YY Live”) for total cash consideration of US\$3.3 billion (equivalent to

II NOTES TO HISTORICAL FINANCIAL INFORMATION—continued

26. SUBSEQUENT EVENTS—continued

Acquisition of YY Live—continued

approximately RMB21,532 million), subject to certain adjustments, as well as contingent cash consideration of up to US\$300 million (equivalent to approximately RMB2.0 billion) if certain conditions are met post-acquisition. The acquisition has been substantially completed, with certain customary matters remaining to be completed in the near future.

The transaction will be accounted for as a business combination. The initial accounting for the business combination is incomplete as the Company is still in the process of measuring the fair value of the consideration transferred, identifiable intangible assets and other assets and liabilities to be recognized upon acquisition, including deferred tax liabilities. Based on information available at this time, the Company determined a preliminary purchase price allocation based on the following provisional amounts: total consideration transferred of RMB22.1 billion which is mainly allocated to intangible assets of RMB6.8 billion, deferred tax liabilities of RMB1.0 billion, and resulting provisional goodwill of RMB16.2 billion, respectively.

iQIYI 2026 Notes and follow-on public offering of ADSs

In connection with the issuance of the iQIYI 2026 Convertible Notes on December 21, 2020, an additional US\$100 million of principal amount was issued on January 8, 2021 pursuant to the underwriters’ exercise of their option to purchase additional notes. The net proceeds received by iQIYI for this additional issuance was US\$98 million (equivalent to RMB641 million).

In connection with iQIYI’s follow-on offering on December 21, 2020, the underwriters had partially exercised their option to purchase additional ADSs of iQIYI. The net proceeds received by iQIYI for this issuance of additional Class A ordinary shares was US\$78 million (equivalent to RMB510 million).

Unsecured US\$ floating rate term loan and revolving loan of the Company

In February 2021, the Company entered into a non-binding term sheet for a term and revolving facility with a group of five mandated lead arrangers, bookrunners and underwriters, pursuant to which the Company plans to borrow an unsecured US\$ denominated floating rate term loan of US\$1.5 billion with a term of 5 years and to borrow an unsecured US\$ denominated revolving loan of US\$1.5 billion for 5 years. The facility is intended for the Company’s general working capital use.

27. DIVIDENDS

No dividends have been paid or declared by the Company during the years ended December 31, 2018, 2019 and 2020.

III SUBSEQUENT FINANCIAL STATEMENTS

No audited financial statements have been prepared by the Company, in respect of any period subsequent to December 31, 2020. Except as disclosed elsewhere in this report, no dividends or distributions have been declared or made by the Company in respect of any period subsequent to December 31, 2020.

APPENDIX IB

ACCOUNTANT’S REPORT OF YY LIVE

The following is the text of a report set out on pages [IB-1 to IB-2], received from the Company’s reporting accountant, PricewaterhouseCoopers, Certified Public Accountants, Hong Kong, for the purpose of incorporation in this [REDACTED]. It is prepared and addressed to the directors of the Company and to the Joint Sponsors pursuant to the requirements of HKSIR 200, Accountants’ Reports on Historical Financial Information in Investment Circulars issued by the Hong Kong Institute of Certified Public Accountants.

[Letterhead of PricewaterhouseCoopers]

[DRAFT]

ACCOUNTANT’S REPORT ON HISTORICAL FINANCIAL INFORMATION TO THE DIRECTORS OF BAIDU, INC. AND MERRILL LYNCH (ASIA PACIFIC) LIMITED, CLSA CAPITAL MARKETS LIMITED AND GOLDMAN SACHS (ASIA) L.L.C.

Introduction

We report on the historical financial information of the domestic video-based live streaming business of JOYY Inc. (the “Target Business”) set out on pages [IB-3 to IB-40], which comprises the combined balance sheets as at December 31, 2018, 2019 and 2020, and the combined statements of comprehensive income, the combined statements of changes in parent company deficit and the combined statements of cash flows for each of the years ended December 31, 2018, 2019 and 2020 (the “Track Record Period”) and a summary of significant accounting policies and other explanatory information (together, the “Historical Financial Information”). The Historical Financial Information set out on pages [IB-3 to IB-40] forms an integral part of this report, which has been prepared for inclusion in the [REDACTED] of Baidu, Inc. (the “Company”) dated [Date] (the [REDACTED]) in connection with the [REDACTED] of shares of the Company on the Main Board of The Stock Exchange of Hong Kong Limited.

Directors and Management’s responsibility for the Historical Financial Information

The directors of the Company are responsible for the preparation of Historical Financial Information that gives a true and fair view in accordance with the basis of presentation and preparation set out in Notes 1(c) and 2(a) to the Historical Financial Information.

The financial statements of the Target Business for the Track Record Period (“Underlying Financial Statements”), on which the Historical Financial Information is based, were prepared by the management of the Target Business. The management of the Target Business are responsible for the preparation of the Underlying Financial Statements in accordance with the basis of presentation and preparation set out therein which conform with accounting principles generally accepted in the United States of America, and for such internal control as the management of the Target Business determine is necessary to enable the preparation of Underlying Financial Statements that are free from material misstatement, whether due to fraud or error.

Reporting accountant’s responsibility

Our responsibility is to express an opinion on the Historical Financial Information and to report our opinion to you. We conducted our work in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 200, *Accountants’ Reports on Historical Financial Information in*

APPENDIX IB

ACCOUNTANT’S REPORT OF YY LIVE

Investment Circulars issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”). This standard requires that we comply with ethical standards and plan and perform our work to obtain reasonable assurance about whether the Historical Financial Information is free from material misstatement.

Our work involved performing procedures to obtain evidence about the amounts and disclosures in the Historical Financial Information. The procedures selected depend on the reporting accountant’s judgement, including the assessment of risks of material misstatement of the Historical Financial Information, whether due to fraud or error. In making those risk assessments, the reporting accountant considers internal control relevant to the entity’s preparation of Historical Financial Information that gives a true and fair view in accordance with the basis of presentation and preparation set out in Notes 1(c) and 2(a) to the Historical Financial Information in order to design procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal control. Our work also included evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the Historical Financial Information.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion

In our opinion, the Historical Financial Information gives, for the purposes of the accountant’s report, a true and fair view of the combined financial position of the Target Business as at December 31, 2018, 2019 and 2020 and of its combined financial performance and its combined cash flows for the Track Record Period in accordance with the basis of presentation and preparation set out in Notes 1(c) and 2(a) to the Historical Financial Information.

Report on matters under the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”) and the Companies (Winding Up and Miscellaneous Provisions) Ordinance

Adjustments

In preparing the Historical Financial Information, no adjustments to the Underlying Financial Statements as defined on page [IB-3] have been made.

[PricewaterhouseCoopers]
Certified Public Accountants
Hong Kong
[Date]

APPENDIX IB

ACCOUNTANT’S REPORT OF YY LIVE

I HISTORICAL FINANCIAL INFORMATION OF THE TARGET BUSINESS

Preparation of Historical Financial Information

Set out below is the Historical Financial Information which forms an integral part of this accountant’s report.

The financial statements of the Target Business for the Track Record Period, on which the Historical Financial Information is based, were audited by PricewaterhouseCoopers Zhong Tian LLP, in accordance with auditing standards generally accepted in the United States of America (“Underlying Financial Statements”).

The Historical Financial Information is presented in Renminbi (“RMB”) and United States Dollars (“US\$”). All values are rounded to the nearest thousand except when otherwise indicated.

COMBINED BALANCE SHEETS AS OF DECEMBER 31, 2018, 2019 AND 2020

(All amounts in thousands)

| | Note | As of December 31, | | | |
|--|------|--------------------|----------------|----------------|----------------------------|
| | | 2018 RMB | 2019 RMB | 2020 RMB | 2020 US\$ (Note2(d)) |
| Assets | | | | | |
| Current assets | | | | | |
| Cash and cash equivalents | 4 | 48,238 | 69,722 | 206,191 | 31,600 |
| Short-term investments | 16 | — | 70,327 | — | — |
| Accounts receivable, net | 5 | 74,253 | 79,430 | 206,580 | 31,660 |
| Amounts due from related parties | | 1,537 | 1,087 | 456 | 70 |
| Prepayments and other current assets | 6 | 25,785 | 39,205 | 45,001 | 6,897 |
| Total current assets | | <u>149,813</u> | <u>259,771</u> | <u>458,228</u> | <u>70,227</u> |
| Non-current assets | | | | | |
| Deferred tax assets | 13 | 71 | 16,021 | 7,767 | 1,190 |
| Property and equipment, net | 7 | 49,228 | 80,590 | 59,900 | 9,180 |
| Intangible assets, net | 8 | 7,059 | 52,519 | 48,042 | 7,363 |
| Other non-current assets | | 4,357 | 13,174 | 24,260 | 3,718 |
| Total non-current assets | | <u>60,715</u> | <u>162,304</u> | <u>139,969</u> | <u>21,451</u> |
| Total assets | | <u>210,528</u> | <u>422,075</u> | <u>598,197</u> | <u>91,678</u> |
| Liabilities and Parent Company deficit | | | | | |
| Current liabilities | | | | | |
| Deferred revenue (including deferred revenue of the combined VIEs without recourse to the Parent Company of RMB425,226, RMB355,549 and RMB326,702 as of December 31, 2018, 2019 and 2020, respectively) | 9 | 425,226 | 355,549 | 326,702 | 50,069 |
| Advances from customers (including advances from customers of the combined VIEs without recourse to the Parent Company of RMB80,504, RMB97,928 and RMB80,761 as of December 31, 2018, 2019 and 2020, respectively) | | 80,504 | 97,928 | 80,761 | 12,377 |

APPENDIX IB

ACCOUNTANT’S REPORT OF YY LIVE

COMBINED BALANCE SHEETS AS OF DECEMBER 31, 2018, 2019 AND 2020—continued

(All amounts in thousands)

| | Note | As of December 31, | | | |
|---|------|--------------------|------------------|------------------|----------------------------|
| | | 2018 RMB | 2019 RMB | 2020 RMB | 2020 US\$ (Note2(d)) |
| Income taxes payable (including income taxes payable of the combined VIEs without recourse to the Parent Company of nil, RMB3,459 and RMB21,014 as of December 31, 2018, 2019 and 2020, respectively) | | — | 3,459 | 21,014 | 3,221 |
| Accrued liabilities and other current liabilities (including accrued liabilities and other current liabilities of the combined VIEs without recourse to the Parent Company of RMB935,409, RMB887,338 and RMB753,214 as of December 31, 2018, 2019 and 2020, respectively) | 10 | 936,667 | 904,918 | 907,692 | 139,110 |
| Total current liabilities | | <u>1,442,397</u> | <u>1,361,854</u> | <u>1,336,169</u> | <u>204,777</u> |
| Non-current liabilities | | | | | |
| Deferred revenue (including deferred revenue of the combined VIEs without recourse to the Parent Company of RMB6,243, RMB58,210 and RMB28,807 as of December 31, 2018, 2019 and 2020, respectively) | 9 | 6,243 | 58,210 | 28,807 | 4,415 |
| Total non-current liabilities | | <u>6,243</u> | <u>58,210</u> | <u>28,807</u> | <u>4,415</u> |
| Total liabilities | | <u>1,448,640</u> | <u>1,420,064</u> | <u>1,364,976</u> | <u>209,192</u> |
| Commitments and contingencies (Note 17) | | | | | |
| Parent Company deficit | | | | | |
| JOYY Inc. (“Parent Company” or “JOYY”) deficit | | (1,238,112) | (997,989) | (766,779) | (117,514) |
| Total Parent Company deficit | | <u>(1,238,112)</u> | <u>(997,989)</u> | <u>(766,779)</u> | <u>(117,514)</u> |
| Total liabilities and Parent Company deficit | | <u>210,528</u> | <u>422,075</u> | <u>598,197</u> | <u>91,678</u> |

APPENDIX IB

ACCOUNTANT’S REPORT OF YY LIVE

COMBINED STATEMENTS OF COMPREHENSIVE INCOME FOR THE YEARS ENDED DECEMBER 31, 2018, 2019 AND 2020

(All amounts in thousands)

| | Note | For the year ended December 31, | | | |
|--|------|---------------------------------|--------------------|--------------------|----------------------------|
| | | 2018 RMB | 2019 RMB | 2020 RMB | 2020 US\$ (Note2(d)) |
| Net revenues | | | | | |
| Live streaming | | 10,073,347 | 10,721,295 | 9,664,816 | 1,481,198 |
| Others | | 199,349 | 241,243 | 285,470 | 43,750 |
| Total net revenues | | <u>10,272,696</u> | <u>10,962,538</u> | <u>9,950,286</u> | <u>1,524,948</u> |
| Cost of revenues ⁽¹⁾ | 11 | <u>(5,357,786)</u> | <u>(5,703,255)</u> | <u>(5,342,372)</u> | <u>(818,754)</u> |
| Gross profit | | <u>4,914,910</u> | <u>5,259,283</u> | <u>4,607,914</u> | <u>706,194</u> |
| Operating expenses ⁽¹⁾ | | | | | |
| Research and development expenses | | (412,046) | (393,100) | (362,406) | (55,541) |
| Sales and marketing expenses | | (498,211) | (506,605) | (581,091) | (89,056) |
| General and administrative expenses | | (203,678) | (198,450) | (152,866) | (23,428) |
| Total operating expenses | | <u>(1,113,935)</u> | <u>(1,098,155)</u> | <u>(1,096,363)</u> | <u>(168,025)</u> |
| Other income | 12 | 67,018 | 203,408 | 166,272 | 25,482 |
| Operating income | | <u>3,867,993</u> | <u>4,364,536</u> | <u>3,677,823</u> | <u>563,651</u> |
| Interest income and investment income | | 1,565 | 2,455 | 2,899 | 444 |
| Income before income tax expenses | | <u>3,869,558</u> | <u>4,366,991</u> | <u>3,680,722</u> | <u>564,095</u> |
| Income tax expenses | 13 | <u>(580,935)</u> | <u>(666,311)</u> | <u>(539,435)</u> | <u>(82,672)</u> |
| Net income | | <u>3,288,623</u> | <u>3,700,680</u> | <u>3,141,287</u> | <u>481,423</u> |
| Other comprehensive income | | — | — | — | — |
| Comprehensive income | | <u>3,288,623</u> | <u>3,700,680</u> | <u>3,141,287</u> | <u>481,423</u> |
| Earnings per share | | | | | |
| —Basic and diluted earnings per share | 14 | <u>N/A</u> | <u>N/A</u> | <u>N/A</u> | <u>N/A</u> |

Note:

(1) Share-based compensation was allocated in cost of revenues and operating expenses as follows:

| | For the year ended December 31, | | | |
|---|---------------------------------|-------------|-------------|----------------------------|
| | 2018 RMB | 2019 RMB | 2020 RMB | 2020 US\$ (Note2(d)) |
| Cost of revenues | 17,494 | 8,655 | 11,241 | 1,723 |
| Research and development expenses | 97,945 | 56,960 | 45,861 | 7,029 |
| Sales and marketing expenses | 2,473 | 1,799 | 1,276 | 196 |
| General and administrative expenses | 75,284 | 72,913 | 34,344 | 5,263 |

APPENDIX IB

ACCOUNTANT’S REPORT OF YY LIVE

COMBINED STATEMENTS OF CHANGES IN PARENT COMPANY DEFICIT FOR THE YEARS ENDED DECEMBER 31, 2018, 2019 AND 2020

(All amounts in thousands)

| | Parent Company deficit |
|--|---------------------------------------|
| | RMB |
| Balance as of January 1, 2018 | <u>(996,326)</u> |
| Contributions to the Parent Company | (3,723,605) |
| Share-based compensation | 193,196 |
| Income and total comprehensive income for the year | <u>3,288,623</u> |
| Balance as of December 31, 2018 and January 1, 2019 | <u>(1,238,112)</u> |
| Contributions to the Parent Company | (3,600,884) |
| Share-based compensation | 140,327 |
| Income and total comprehensive income for the year | <u>3,700,680</u> |
| Balance as of December 31, 2019 and January 1, 2020 | <u>(997,989)</u> |
| Adoption of ASC326 | (785) |
| Contributions to the Parent Company | (3,002,014) |
| Share-based compensation | 92,722 |
| Income and total comprehensive income for the year | <u>3,141,287</u> |
| Balance as of December 31, 2020 | <u><u>(766,779)</u></u> |

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION

(All amount in thousands, unless otherwise stated)

1. General information

(a) Organization and principal activities

JOYY Inc. (“Parent Company”, “JOYY” or “YY”), together with its subsidiaries, its variable interest entities (“VIEs”) (also referred to as VIEs and their subsidiaries as a whole, where appropriate) (collectively, the “JOYY Group”), is a leading global social media platform, offering users around the world a uniquely engaging and immersive experience across various video-based products and services, such as live streaming, short-form videos and video communication.

In November 2020, JOYY entered into definitive agreements (“Agreements”) with Baidu, Inc. (Nasdaq: BIDU) (“Baidu”). Pursuant to the Agreements, Baidu will acquire JOYY’s domestic video-based live streaming business (“Target Business”) which includes the YY mobile app, YY.com website and PC YY, among others, for an aggregate purchase price of approximately US\$3.6 billion in cash, subject to certain adjustments (the “Transaction”).

Pursuant to the Agreements, JOYY will transfer all equity interest of Runderfo Inc., (“Runderfo”), together with the equity interest of certain other subsidiaries and VIEs of JOYY (collectively, the “Target Group”) to Baidu. Assets, business contracts and employee contracts which are necessary for the operation of the Target Business were transferred to the Target Group before the equity interests of the companies within the Target Group are transferred to Baidu. As a result, Baidu obtained the Target Business by acquiring the equity interests of the Target Group.

(b) Reorganization

Runderfo is an exempted company with limited liability incorporated in the Cayman Islands on November 4, 2020 in connection with a group reorganization (the “Reorganization”) of the Target Business. The Target Business is carried out by various subsidiaries and VIEs of JOYY (the “Predecessor Operations”) prior to the Reorganization. In connection with the Reorganization, the Target Business was transferred to the Target Group. As of the report date, the Reorganization was completed.

(c) Basis of preparation and presentation

The combined financial statements represent the Target Business owned by JOYY during the three years ended December 31, 2018, 2019 and 2020. Throughout the years presented in the combined financial statements, the Target Business did not exist as a separate legal entity. The combined financial information of the Target Business has therefore been derived from the consolidated financial statements of JOYY and its subsidiaries and VIEs which include all revenues derived from the Target Business and all the costs of doing business to represent the financial position and performance of the Target Business as if it is on a standalone basis throughout the periods. Management of JOYY determined that this presentation presents the Target Business most appropriately based on several factors, including the scope of the Target Business is clearly defined within the Agreements.

The combined financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) and comprise an aggregation of the financial position, results or operation and cash flows of the Target Business after making such adjustments as were considered appropriate and reasonable in relation to the items set out below.

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

1. General information—continued

(c) Basis of preparation and presentation—continued

- (i) The assets and liabilities have been stated at historical carrying amounts. Only those assets and liabilities that are specifically identifiable to the Target Business are included.
- (ii) Revenues, costs of revenue, research and development expenses, sales and marketing expenses and general administrative expenses generated or incurred solely by the Target Business are carved out directly from the consolidated financial statements of JOYY, and other indirect costs and expenses incurred in operation are allocated to the Target Business as principles described in (iv) below. These combined financial statements reflect all the costs of doing business.
- (iii) Any funding received from/paid to JOYY and its subsidiaries and VIEs other than the companies within the Target Group (“JOYY Group Entities”) in the periods covered by these combined financial statements are treated as deemed capital contributions from/to Parent Company.
- (iv) Certain common costs and expenses incurred by the Target Business in conjunction with other businesses of JOYY, including salaries and welfare of employees of support functions and bandwidth and server custody costs of certain shared functions are allocated to the combined financial statements primarily based on the following allocation methodology which management believes as reasonable:
 - 1) Salaries and welfares of employees of certain shared functions and other expenses related to these employees (e.g. office rental expenses and depreciation and amortization incurred by the office areas occupied by these employees) were allocated to the Target Business based on the proportion of number of staff in different business lines.
 - 2) Bandwidth and server custody costs were allocated to the Target Business based on the proportion of specifically identifiable consumption of the resources by different business lines.
- (v) Income tax expenses as well as deferred tax assets are calculated based on a separate return basis as if the entities of the Target Business had filed separate tax returns.

However, such presentation may not necessarily reflect the financial position, the results of operation or the cash flows of the Target Business had it actually existed on a stand-alone basis during the Track Record Period or for future periods.

The following table sets forth the cost of revenues, research and development expenses, sales and marketing expenses, and general and administrative expenses allocated from YY for the years ended December 31, 2018, 2019 and 2020.

| | For the year ended December 31, | | |
|-------------------------------------|---------------------------------|------------------|------------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Cost of revenues | 4,923,681 | 5,056,383 | 4,608,416 |
| Research and development expenses | 412,043 | 384,222 | 284,758 |
| Sales and marketing expenses | 494,902 | 505,823 | 576,655 |
| General and administrative expenses | 198,267 | 178,582 | 136,187 |
| Total | <u>6,028,893</u> | <u>6,125,010</u> | <u>5,606,016</u> |

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

1. General information—continued

(c) Basis of preparation and presentation—continued

The Target Business was operated within JOYY for the periods presented before the completion of the Reorganization. The Parent Company deficit balance within the combined financial statements represents the excess of total liabilities over total assets. The movements in Parent Company deficits throughout the years are analyzed within the combined statements of changes in Parent Company deficit. Given the nature of the combined financial statements, it is not possible to establish a separate balance for the retained earnings/accumulated deficits within the Parent Company deficit balance as of January 1, 2018 and so no such split is provided. For purposes of presentation in the combined statements of cash flows, the cash flows from the Target Business to the Parent Company is presented as contribution to the Parent Company, which is included in cash flows from financing activities.

(d) Principal subsidiaries and VIEs

The details of the principal subsidiaries and VIE through which the Parent Company conducts the Target Business operations as of December 31, 2020 are set out below:

| Name | Place of incorporation | Date of incorporation or acquisition | % of direct or indirect economic ownership | Principal activities |
|--|---|--------------------------------------|--|--|
| Principal subsidiaries | | | | |
| Duowan Entertainment Corporation (“Duowan BVI”) | British Virgin Islands (“BVI”) | November 6, 2007 | 100% | Investment holding |
| Huanju Shidai Technology (Beijing) Co., Ltd. (“Beijing Huanju Shidai”) | The Peoples’s Republic of China (“The PRC”) | March 19, 2008 | 100% | Investment holding |
| Guangzhou Huanju Shidai Information Technology Co., Ltd. (“Guangzhou Huanju Shidai”) | The PRC | December 2, 2010 | 100% | Software development |
| Principal VIE | | | | |
| Guangzhou Huaduo Network Technology Co., Ltd. (“Guangzhou Huaduo”) (*) | The PRC | April 11, 2005 | 100% | Holder of internet content provider licenses and operations of internet value added services |

Note:

* Guangzhou Huaduo controls a number of subsidiaries and these subsidiaries are also treated as VIEs of the Target Business.

(e) Variable Interest Entities

(i) VIE agreements amongst Beijing Huanju Shidai, Guangzhou Huaduo and its nominee shareholders

In order to comply with the PRC laws and regulations which prohibit or restrict foreign control of companies involved in provision of internet content, the Target Business was carried out in the PRC through Guangzhou Huaduo, a VIE of JOYY. JOYY obtained control over Guangzhou Huaduo through a wholly owned subsidiary (“WFOE”) by entering into a series of contractual arrangements with Guangzhou Huaduo and its nominee shareholders. To comply with PRC laws and regulations which prohibit or restrict foreign ownership of internet content, the nominee shareholders are legal owners of an entity. However, the rights of those nominee shareholders have been transferred to the WFOE of JOYY through such contractual arrangements. These contractual arrangements include exclusive purchase option agreement, exclusive technology support and technology services

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

1. General information—continued

(e) Variable Interest Entities—continued

(i) VIE agreements amongst Beijing Huanju Shidai, Guangzhou Huaduo and its nominee shareholders—continued

agreement, exclusive business cooperation agreement, equity pledge agreement and powers of attorney. These contractual arrangements can be extended at the option of the WFOE of JOYY, prior to the expiration date. Management concluded that the WFOE of YY, through the contractual arrangements, has the power to direct the activities that most significantly impact Guangzhou Huaduo’s economic performance, bears the risks of and enjoys the rewards normally associated with ownership of Guangzhou Huaduo, and therefore Guangzhou Huaduo is a VIE of the WFOE of YY, of which JOYY is the ultimate primary beneficiary. As such, JOYY consolidated the financial statements of Guangzhou Huaduo. Consequently, the financial results of Guangzhou Huaduo directly attributable to the Target Business were included in the combined financial statements in accordance with the basis of presentation as stated in Note 1(c).

● **Exclusive Technology Support and Technology Services Agreement**

Under the exclusive technology support and technology services agreement between Beijing Huanju Shidai and Guangzhou Huaduo, Beijing Huanju Shidai has the exclusive right to provide to Guangzhou Huaduo technology support and technology services related to all technologies needed for its business. Beijing Huanju Shidai owns the exclusive intellectual property rights created as a result of the performance of this agreement. The service fee payable by Guangzhou Huaduo to Beijing Huanju Shidai is determined by various factors, including the expenses Beijing Huanju Shidai incurs for providing such services and Guangzhou Huaduo’s revenues. The term of this agreement will expire in 2028 and may be extended with Beijing Huanju Shidai’s written confirmation prior to the expiration date. Beijing Huanju Shidai is entitled to terminate the agreement at any time by providing 30 days’ prior written notice to Guangzhou Huaduo.

● **Exclusive Business Cooperation Agreement**

Under the exclusive business cooperation agreement between Beijing Huanju Shidai and Guangzhou Huaduo, Beijing Huanju Shidai has the exclusive right to provide to Guangzhou Huaduo technology support, business support and consulting services related to the services provided by Guangzhou Huaduo, the scope of which is to be determined by Beijing Huanju Shidai from time to time. Beijing Huanju Shidai owns the exclusive intellectual property rights created as a result of the performance of this agreement. The service fee payable by Guangzhou Huaduo to Beijing Huanju Shidai is a certain percentage of its earnings. The term of this agreement will expire in 2038 and may be extended with Beijing Huanju Shidai’s written confirmation prior to the expiration date. Beijing Huanju Shidai is entitled to terminate the agreement at any time by providing 30 days’ prior written notice to Guangzhou Huaduo.

● **Exclusive Option Agreement**

The parties to the exclusive option agreement are Beijing Huanju Shidai, Guangzhou Huaduo and each of the shareholders of Guangzhou Huaduo. Under the exclusive option agreement, each of the shareholders of Guangzhou Huaduo irrevocably granted Beijing Huanju Shidai or its designated

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

1. General information—continued

(e) Variable Interest Entities—continued

(i) VIE agreements amongst Beijing Huanju Shidai, Guangzhou Huaduo and its nominee shareholders—continued

● Exclusive Option Agreement—continued

representative(s) an exclusive option to purchase, to the extent permitted under PRC law, all or part of his or its equity interests in Guangzhou Huaduo. Beijing Huanju Shidai or its designated representative(s) have sole discretion as to when to exercise such options, either in part or in full. Without Beijing Huanju Shidai’s prior written consent, Guangzhou Huaduo’s shareholders shall not sell, transfer, mortgage or otherwise dispose their equity interests in Guangzhou Huaduo. The term of this agreement is ten years and may be extended at Beijing Huanju Shidai’s sole discretion.

● Powers of Attorney

Pursuant to the irrevocable power of attorney executed by each shareholder of Guangzhou Huaduo, each such shareholder appointed Beijing Huanju Shidai as its attorney-in-fact to exercise such shareholders’ rights in Guangzhou Huaduo, including, without limitation, the power to vote on its behalf on all matters of Guangzhou Huaduo requiring shareholder approval under PRC laws and regulations and the articles of association of Guangzhou Huaduo. Each power of attorney will remain in force until the shareholder ceases to hold any equity interest in Guangzhou Huaduo.

● Share Pledge Agreement

Pursuant to the share pledge agreement between Beijing Huanju Shidai and the shareholders of Guangzhou Huaduo, the shareholders of Guangzhou Huaduo have pledged all of their equity interests in Guangzhou Huaduo to Beijing Huanju Shidai to guarantee the performance by Guangzhou Huaduo and its shareholders’ performance of their respective obligations under the exclusive business cooperation agreement, exclusive option agreement, exclusive technology support and technology services agreement and powers of attorney. If Guangzhou Huaduo and/or its shareholders breach their contractual obligations under those agreements, Beijing Huanju Shidai, as pledgee, will be entitled to certain rights, including the right to sell the pledged equity interests.

In accordance with the aforementioned agreements, the Parent Company has power to direct activities of the VIEs, and can have assets transferred out of the VIEs. Therefore the Parent Company considers that there is no asset in the VIEs that can be used only to settle obligations of the VIEs, except for registered capital and PRC statutory reserves of the VIEs. As the VIE was incorporated as limited liability companies under the PRC Company Law, the creditors do not have recourse to the general credit of the Parent Company for all the liabilities of the VIEs.

Currently there is no contractual arrangement that could require the Parent Company to provide additional financial support to the VIEs. As the Parent Company is conducting its PRC internet value-added services business through the VIE, the Parent Company will, if needed, provide such support on a discretionary basis in the future, which could expose the Parent Company to a loss.

Please refer to Note 3 for the combined financial information of the Target Business’ VIEs as of December 31, 2020.

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

2. Principal accounting policies

(a) Basis of presentation

The combined financial statements of the Target Business have been prepared in accordance with the U.S. GAAP to reflect the financial position, results of operations and cash flows of the Target Business. Significant accounting policies followed by the Target Business in the preparation of the combined financial statements are summarized below.

(b) Use of estimates

The preparation of the combined financial statements of the Target Business in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period in the combined financial statements and accompanying notes. Actual results could differ materially from such estimates. Management believes that the assessment of whether the Target Business acts as a principal or an agent in different revenue streams, the determination of estimated selling prices of multiple elements revenue contracts, income taxes, allowances for doubtful accounts, determination of share-based compensation expenses represent critical accounting policies that reflect more significant judgments and estimates used in the preparation of its combined financial statements.

Management bases the estimates on historical experience and on various other assumptions that are believed to be reasonable, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Actual results could differ from these estimates.

(c) Foreign currency translation

The Target Business uses RMB as its reporting currency. The functional currency of Runderfo is US\$, while the functional currency of the PRC entities and VIEs in the Target Business is RMB, which is their respective local currency. In the combined financial statements, the financial information of Runderfo has been translated into RMB. Assets and liabilities are translated at the exchange rates on the balance sheet date, equity amounts are translated at historical exchange rates, and revenues, expenses, gains, and losses are translated using the average exchange rate for the period. Translation adjustments arising from these are reported as foreign currency translation adjustments and are shown as a component of other comprehensive income or loss in the combined statements of comprehensive income.

Foreign currency transactions denominated in currencies other than functional currency are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are remeasured at the applicable rates of exchange in effect at that date. Foreign exchange gains and losses resulting from the settlement of such transactions and from remeasurement at year-end are recognized in foreign currency exchange gains/losses, net in the combined statements of comprehensive income.

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

2. Principal accounting policies—continued

(d) Convenience translation

Translations of amounts from RMB into US\$ for the convenience of the reader were calculated at the noon buying rate of US\$1.00 = RMB 6.5250 on December 31, 2020 as set forth in the H.10 statistical release of the U.S. Federal Reserve Board. No representation is made that the RMB amounts could have been, or could be, converted into US\$ at such rate.

(e) Cash and cash equivalents

Cash includes currency on hand and deposits held by financial institutions that can be added to or withdrawn without limitation. Cash equivalents represent short-term and highly liquid investments placed with banks, which have both of the following characteristics:

- i) Readily convertible to known amounts of cash throughout the maturity period;
- ii) So near their maturity that they present insignificant risk of changes in value because of changes in interest rates.

Management considers all highly liquid investments with original maturities of three months or less as cash equivalents.

(f) Short-term investments

For investments in financial instruments with a variable interest rate indexed to the performance of underlying assets, management elected the fair value method at the date of initial recognition and carried these investments subsequently at fair value. Changes in fair values are reflected in the combined statements of comprehensive income.

(g) Accounts receivable

Accounts receivable are presented net of allowance for doubtful accounts. Management uses specific identification in providing for bad debts when facts and circumstances indicate that collection is doubtful and a loss is probable and estimable. If the financial conditions of its customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowance may be required.

Management maintains an allowance for doubtful accounts which reflects its best estimate of amounts that potentially will not be collected. Management determines the allowance for doubtful accounts on an individual basis taking into consideration various factors including but not limited to historical collection experience and credit-worthiness of the debtors as well as the age of the individual receivables balance. Additionally, management makes specific bad debt provisions based on any specific knowledge management has acquired that might indicate that an account is uncollectible. The facts and circumstances of each account may require management to use substantial judgment in assessing its collectability.

On January 1, 2020, the Company adopted ASC326, “Financial Instruments—Credit Losses” using modified-retrospective transition approach.

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

2. Principal accounting policies—continued

(h) Property and equipment

Property and equipment are stated at historical cost less accumulated depreciation and impairment loss, if any. Depreciation is calculated using the straight-line method over their estimated useful lives. Residual rate is determined based on the economic value of the property and equipment at the end of the estimated useful lives as a percentage of the original cost.

| | <u>Estimated useful lives</u> | <u>Residualrate</u> |
|--|-------------------------------|---------------------|
| Servers, computers and equipment | 3-5 years | 0%-5% |

Expenditures for maintenance and repairs are expensed as incurred. The gain or loss on the disposal of property and equipment is the difference between the net sales proceeds and the carrying amount of the relevant assets and is recognized in the combined statements of comprehensive income.

All direct and indirect costs that are related to the construction of property and equipment and incurred before the assets are ready for their intended use are capitalized as construction in progress. Construction in progress is transferred to specific property and equipment items and depreciation of these assets commences when they are ready for their intended use.

(i) Intangible assets

Intangible assets mainly consist of license and domain names. Identifiable intangible assets are carried at acquisition cost less accumulated amortization and impairment loss, if any. Finite-lived intangible assets are tested for impairment if impairment indicators arise. Amortization of finite-lived intangible assets is computed using the straight-line method over their estimated useful lives, which are as follows. Management determined the useful lives of intangible assets by estimating the economic life during which the Target Business is expected to benefit from the intangible assets.

| | <u>Estimated useful lives</u> |
|--------------------|-------------------------------|
| License | 15 years |
| Domain names | 15 years |

(j) Impairment of long-lived assets

For long-lived assets other than investments and goodwill whose impairment policy is discussed elsewhere in the combined financial statements, management evaluates for impairment whenever events or changes (triggering events) indicate that the carrying amount of an asset may no longer be recoverable. Management assesses the recoverability of the long-lived assets by comparing the carrying value of the long-lived assets to the estimated undiscounted future cash flows expected to receive from use of the assets and their eventual disposition. Such assets are considered to be impaired if the sum of the expected undiscounted cash flows is less than the carrying amount of the assets. The impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Management tests impairment of long-lived assets at the reporting unit level when impairment indicator appears and recognizes impairment in the event that the carrying value exceeds the fair value of each reporting unit.

No impairment charges of long-lived assets recorded in general and administrative expenses had been recognized during the Track Record Period.

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

2. Principal accounting policies—continued

(k) Revenue

Revenue recognition and significant judgments

Revenues from live streaming are mainly generated from YY mobile app, YY.com website and PC YY.

Revenues are recognized when control of the promised virtual items or services is transferred to the Target Business’ customers, in an amount that reflects the consideration the Target Business expects to be entitled to in exchange for those virtual items or services.

The Target Business has a recharge system for users to purchase the Target Business’ virtual currency. Users can recharge via various online payment platforms provided by third parties. Virtual currency is non-refundable and without expiry. As the virtual currency is often consumed soon after it is purchased based on history of turnover, the Target Business considers the impact of the breakage amount for virtual currency coupons is insignificant. Unconsumed virtual currency is recorded as deferred revenue. Virtual currencies used to purchase virtual items are recognized as revenue according to the prescribed revenue recognition policies of virtual items addressed below unless otherwise stated.

(i) Live streaming

Live streaming mainly consists of YY mobile app, YY.com website and PC YY . It generates revenue from sales of virtual items to registered users in the platforms. Users can access the platforms and view the live streaming content showed by the performers. In providing these services, the Target Business has cooperated with talent agencies to assist in performer recruitment, live streaming training and support, promotion strategies development and content management and maintaining discipline of the performers. The Target Business shares a portion of the sales proceeds of virtual items (“revenue sharing fee”) with performers and talent agencies in accordance with their revenue sharing arrangements. Those performers who do not have revenue sharing arrangements with the Target Business are not entitled to any revenue sharing fee.

Management evaluates and determines that it is the principal and views users to be its customers. The Target Business reports live streaming revenues on a gross basis. Accordingly, the amounts billed to users are recorded as revenues and revenue sharing fee paid to performers and talent agencies are recorded as cost of revenues. Where the Target Business is the principal, it controls the virtual items before they are transferred to users. Its control is evidenced by the Target Business’ sole ability to monetize the virtual items before they are transferred to users, and is further supported by the Target Business being primarily responsible to users and having a level of discretion in establishing pricing.

The Target Business designs, creates and offers various virtual items for sales to users with pre-determined selling price. Sales proceeds are recorded as deferred revenue and recognized as revenue based on the consumption of the virtual items. Virtual items are categorized as consumable and time-based items. Consumable items are consumed upon purchase and use while time-based items could be used for a fixed period of time. Users can purchase and present consumable items to performers to show support for their favorite performers, or purchase time-based virtual items for one or multiple months for a monthly fee, which provide users with recognized status, such as priority speaking rights or special symbols over a period of time. Accordingly, live streaming revenue is recognized immediately when the consumable virtual item is used, or in the case of time-based virtual

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

2. Principal accounting policies—continued

(k) Revenue—continued

Revenue recognition and significant judgments—continued

(i) Live streaming—continued

items, revenue is recognized ratably over the fixed period on a straight-line basis. The Target Business does not have further obligations to the user after the virtual items are consumed immediately or after the stated period of time for time-based items.

The Target Business may also enter into contracts that can include various combinations of virtual items, which are generally capable of being distinct and accounted for as separate performance obligations, such as the noble member program. Judgments are required as follow: 1) determining whether those virtual items are considered distinct performance obligations that should be accounted for separately versus together, 2) determining the standalone selling price for each distinct performance obligation, and 3) allocating of the arrangement consideration to the separate accounting of each distinct performance obligation based on their relative standalone selling prices. Certain virtual items are provided to customers over time and have the same pattern of transfer to customers. Management exercises judgement in determining the number of distinct performance obligations by accounting for services that have the same pattern of transfer to customers as a single performance obligation. In instances where standalone selling price is not directly observable as the Target Business does not sell the virtual item separately, management determines the standalone selling price based on pricing strategies, market factors and strategic objectives. The Target Business recognizes revenue for each of the distinct performance obligations identified in accordance with the applicable revenue recognition method relevant for that obligation.

As the live streaming virtual items are generally sold without right of return and the Target Business does not provide any other credit and incentive to its users, therefore accounting of variable consideration when estimating the amount of revenue to recognize is not applicable to the live streaming business.

(ii) Membership

The Target Business operates a membership subscription program where subscription members can have enhanced user privileges when using YY Client and live streaming channels. The membership fee is collected up-front from subscribers. The receipt of the revenue is initially recorded as deferred revenue and revenue is recognized ratably over the period of the subscription when services are rendered. Unrecognized portion beyond 12 months from balance sheet date is classified as long-term deferred revenue.

(iii) Advertising revenues

The Target Business primarily generates advertising revenues from sales of various forms of advertising and provision of promotion campaigns on the live streaming platforms by way of advertisement display or integrated promotion activities in shows and programs on the live streaming platforms. Advertisements on the platforms are generally charged on the basis of duration, and advertising contracts are signed to establish the fixed price and the advertising services to be provided.

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

2. Principal accounting policies—continued

(k) Revenue—continued

Revenue recognition and significant judgments—continued

(iii) Advertising revenues—continued

Where the service is transferred to customers, advertising revenues from advertising contracts are recognized ratably over the contract period of display.

The Target Business enters into advertising contracts directly with advertisers or third-party advertising agencies that represent advertisers. Payment terms and conditions vary by contract type, although the terms generally include a requirement of payment within 1 to 3 months. Both third-party advertising agencies and direct advertisers are generally billed at the end of the display period and payments are due usually within 3 months. In instances where the timing of revenue recognition differs from the timing of billing, management has determined the advertising contracts generally do not include a significant financing component. The primary purpose of the credits terms is to provide customers with simplified and predictable ways of purchasing the advertising services, not to receive financing from the customers or to provide customers with financing.

Certain customers may receive sales incentives in the forms of discounts and rebates to advertisers or advertising agencies based on purchase volume, which is accounted for as variable consideration. Management estimates these amounts based on the expected amount to be provided to customers considering the contracted rebate rates and estimated sales volume based on historical experience, and reduce revenues recognized. Management believes that there will not be significant changes to its estimates of variable consideration.

Contract balances

The Target Business collects accounts receivable from various online payment platforms and advertising customers. The allowance for doubtful accounts reflects the management’s best estimate of probable losses inherent in the accounts receivable balance. Management determines the allowance based on known troubled accounts, historical experience, and other currently available evidence. The activity in the allowance for doubtful accounts for the periods presented is disclosed and detailed in Note 5.

The opening balance of accounts receivable was RMB65,683 as of January 1, 2018. As of December 31, 2018, 2019 and 2020, accounts receivable were RMB74,253, RMB79,430 and RMB206,580, respectively. During the years ended December 31, 2018, 2019 and 2020, the Target Business recognized an addition of RMB475, nil and RMB248 of allowance for accounts receivable, respectively, and a reversal of nil, RMB75 and nil of allowance for accounts receivable, respectively, and a write-off of nil, RMB400 and nil of allowance for accounts receivable, respectively.

Contract liabilities primarily consists of deferred revenue for unconsumed virtual items and unamortized revenue from virtual items in the Target Business’ platforms, where there is still an obligation to be provided by the Target Business, which will be recognized as revenue when all of the revenue recognition criteria are met.

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

2. Principal accounting policies—continued

(k) Revenue—continued

Contract balances—continued

The opening balance of deferred revenue related to live streaming business as of January 1, 2018 was RMB393,348. As of December 31, 2018, 2019 and 2020, deferred revenue related to live streaming business were RMB374,750, RMB264,658 and RMB277,823 respectively. During the years ended December 31, 2018, 2019 and 2020, the Target Business recognized revenue of live streaming business amounted to RMB393,294, RMB374,750 and RMB264,658, respectively, that was included in the corresponding contract liability balance at the beginning of the periods.

The opening balance of deferred revenue related to other revenue as of January 1, 2018 was RMB61,529. As of December 31, 2018, 2019 and 2020, deferred revenue related to other revenue were RMB56,719, RMB149,101 and RMB77,686, respectively. During the years ended December 31, 2018, 2019 and 2020, the Target Business recognized other revenue amounted to RMB54,610, RMB50,476 and RMB90,891, respectively, that was included in the corresponding contract liability balance at the beginning of the periods.

During the Track Record Period, the Target Business did not have any arrangement where the performance obligations have already been satisfied in the past year, but the corresponding revenue was recognized in the succeeding year.

As of December 31, 2020, the aggregate amount of the transaction price allocated to the remaining performance obligations was RMB355,509. Management expects to recognize RMB326,702 performance obligation as revenue in 2021, the remaining performance obligation is expected to be recognized as revenue in 2022 and after years. However, the amount and timing of revenue recognition is largely driven by customer usage, which can extend beyond the original contractual term.

(l) Advances from customers and deferred revenue

Advances from customers primarily consist of prepayments from users in the form of the Target Business’ virtual currency that are not yet consumed, and upon the consumption or conversion, are recognized as revenue according to the prescribed revenue recognition policies described above.

Deferred revenue primarily consists of the unamortized prepaid subscriptions under the membership program and unamortized revenue from virtual items in various channels in the Target Business’ platforms, where there is still an implied obligation to be provided by the Target Business, which will be recognized as revenue when all of the revenue recognition criteria are met.

(m) Cost of revenues

Amounts recorded as cost of revenue relate to direct expenses incurred in order to generate revenue. Such costs are recorded as incurred. Cost of revenues primarily consists of (i) revenue sharing fees and content costs, including payments to various talent agencies and performers, and content providers, (ii) bandwidth costs, (iii) payment handling costs, (iv) salary and welfare, (v) technical service fee, (vi) depreciation and amortization expense for servers, other equipment and intangibles directly related

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

2. Principal accounting policies—continued

(m) Cost of revenues—continued

to operating the platform, (vii) share-based compensation, (viii) other taxes and surcharges, and (ix) other costs.

The Target Business was subject to surcharges of value added taxes (“VAT”), which was calculated based on 12% of the VAT paid for the years ended December 31, 2018, 2019 and 2020.

The Target Business reported other taxes and surcharges in cost of revenues.

Based on the JOYY’s corporate structure and the contractual arrangements among the Target Business’ PRC subsidiaries, the VIEs and their shareholders, the Target Business was effectively subject to 6% or 13% VAT and related surcharges on revenues generated by the Target Business’ PRC subsidiaries based on the contractual arrangements entered into with the VIEs.

(n) Research and development expenses

Research and development expenses primarily consist of (i) salary and welfare for research and development personnel, (ii) share-based compensation for research and development personnel, (iii) depreciation of office premise and servers utilized by research and development personnel, and (iv) rental expenses. Costs incurred during the research stage are expensed as incurred. Costs incurred in the development stage, prior to the establishment of technological feasibility, which is when a working model is available, are expensed when incurred.

Management recognizes internal use software development costs in accordance with guidance on intangible assets and internal use software. This requires capitalization of qualifying costs incurred during the software’s application development stage and to expense costs as they are incurred during the preliminary project and post implementation/operation stages. The Target Business had not capitalized any costs related to internal use software during the Track Record Period.

(o) Sales and marketing expenses

Sales and marketing expenses primarily consist of (i) advertising and market promotion expenses, (ii) salary and welfare for sales and marketing personnel. The advertising and market promotion expenses amounted to approximately RMB474,261, RMB488,286 and RMB563,760 during the years ended December 31, 2018, 2019 and 2020, respectively.

(p) General and administrative expenses

General and administrative expenses primarily consist of (i) share-based compensation for management and administrative personnel, (ii) salary and welfare for general and administrative personnel, (iii) impairment charge, and (iv) professional service fees.

(q) Employee social security and welfare benefits

Employees of the Target Business in the PRC are entitled to staff welfare benefits including pension, work-related injury benefits, maternity insurance, medical insurance, unemployment benefit and

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

2. Principal accounting policies—continued

(q) Employee social security and welfare benefits—continued

housing fund plans through a PRC government-mandated multi-employer defined contribution plan. The Target Business is required to accrue for these benefits based on certain percentages of the employees’ salaries, up to a maximum amount specified by the local government. The Target Business is required to make contributions to the plans out of the amounts accrued. The PRC government is responsible for the medical benefits and the pension liability to be paid to these employees and the Target Business’ obligations are limited to the amounts contributed and no legal obligation beyond the contributions made. Employee social security and welfare benefits included as expenses in the accompanying combined statements of comprehensive income amounted to RMB82,199, RMB85,878 and RMB66,393 for the years ended December 31, 2018, 2019 and 2020, respectively.

(r) Share-based compensation

The Target Business grants stock-based award, such as, but not limited to, share options, restricted shares, restricted share units of the Parent Company, share option, restricted share units and ordinary shares of the Parent Company’s subsidiaries to eligible employees, officers, directors, and non-employee consultants.

Awards granted to employees, officers, and directors are initially accounted for as equity-classified awards. The related share-based compensation expenses are measured at the grant date fair value of the award and are recognized using the graded vesting method, net of estimated forfeiture rates, over the requisite service period, which is generally the vesting period. Forfeitures are estimated at the time of grant based on historical forfeiture rates and will be revised in the subsequent periods if actual forfeitures differ from those estimates.

For an award with a performance and/or service condition that affects vesting, the performance and/or service condition is not considered in determining the award’s fair value on the grant date. Performance and service conditions should be considered when management is estimating the quantity of awards that will vest. Compensation cost will reflect the number of awards that are expected to vest and will be adjusted to reflect those awards that do ultimately vest. The Target Business recognizes compensation cost for awards with performance conditions if and when management concludes that it is probable that the performance condition will be achieved, net of an estimate of pre-vesting forfeitures over the requisite service period. Management reassesses the probability of vesting at each reporting period for awards with performance conditions and adjusts compensation cost based on its probability assessment, unless on certain situations, management may not be able to determine that it is probable that a performance condition will be satisfied until the event occurs.

ASU 2017-09, Compensation—Stock Compensation (Topic 718), Scope of Modification Accounting, provides guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718.

An entity should account for the effects of a modification unless all the followings are met:

- The fair value (or calculated value or intrinsic value, if such an alternative measurement method is used) of the modified award is the same as the fair value (or calculated value or intrinsic value, if such

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

2. Principal accounting policies—continued

(r) Share-based compensation—continued

an alternative measurement method is used) of the original award immediately before the original award is modified. If the modification does not affect any of the inputs to the valuation technique that the entity uses to value the award, the entity is not required to estimate the value immediately before and after the modification.

—The vesting conditions of the modified award are the same as the vesting conditions of the original award immediately before the original award is modified.

—The classification of the modified award as an equity instrument or a liability instrument is the same as the classification immediately before the original award is modified.

The current disclosure requirements in Topic 718 apply regardless of whether an entity is required to apply modification accounting under the amendments in this ASU 2017-09.

The Target Business adopted these amendments to Subtopic 718-10 and there was no impact on the combined financial statements for the years presented.

The Target Business’ share-based awards mainly include share-based awards of JOYY. Fair value determination of these share-based awards is summarized as below:

(1) Restricted share units

In determining the fair value of restricted share units granted, the fair value of the underlying shares of JOYY on the grant dates is applied. The grant date fair value of restricted share units is based on stock price of YY in the Nasdaq Global Select Market.

(2) Share options

In determining the fair value of share options granted, a binomial option-pricing model is applied. The determination of the fair value is affected by the stock price of YY in the Nasdaq Global Select Market, as well as assumptions regarding a number of complex and subjective variables, including risk-free interest rates, exercise multiples, expected forfeiture rates, the expected share price volatility rates, and expected dividends.

(s) Other income

Other income primarily consists of government grants which represent cash subsidies received from the PRC government by the Target Business entities. Government grants are originally recorded as deferred revenue when received upfront. After all of the conditions specified in the grants have been met, the grants are recognized as operating income.

(t) Leases

The Target Business leases facilities in the PRC under non-cancellable operating leases expiring on different dates. On January 1, 2019, management adopted ASU No. 2016-02 (Topic 842) “Leases”

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

2. Principal accounting policies—continued

(t) Leases—continued

using the optional transition method. Results and disclosure requirements for reporting periods beginning after January 1, 2019 are presented under Topic 842, while prior period amounts have not been adjusted and continue to be reported in accordance with the Target Business’s historical accounting under Topic 840. Under Topic 840, each lease is classified at the inception date as either a capital lease or an operating lease. For the lessee, a lease is a capital lease if any of the following conditions exist: a) ownership of the leased property is transferred to the lessee by the end of the lease term, b) there is a bargain purchase option, c) the lease term is at least 75% of the leased property’s estimated remaining economic life or d) the present value of the minimum lease payments at the beginning of the lease term is 90% or more of the fair value of the leased property to the lessor at the inception date. A capital lease is accounted for as if there was an acquisition of an asset and an incurrence of an obligation at the inception of the lease. All other leases are accounted for as operating leases. Payments made under operating lease are charged to the combined statement of comprehensive income on a straight-line basis over the term of underlying lease. The Group has no capital lease for the year ended December 31, 2018. Under Topic 842, lessees are required to recognize assets and liabilities on the balance sheet for most leases. A contract is or contains a lease if the contract conveys the right to control the use of identified property, plant, or equipment (an identified asset) for a period of time in exchange for consideration. Management determines whether a contract conveys the right to control the use of an identified asset for a period of time by assessing whether the Target Business has both the right to obtain substantially all of the economic benefits from use of the identified asset and the right to direct the use of the identified asset.

Management accounts for short-term leases with terms less than 12 months in accordance with ASC 842-20-25-2 to recognize the lease payments in profit or loss on a straight-line basis over the lease term and variable lease payments in the period in which the obligation for those payments is incurred. The adoption of the standard did not have a significant impact on the combined financial statements.

For the years ended December 31, 2018, 2019 and 2020, short-term lease cost amounted to RMB12,804, RMB11,292 and RMB12,677, respectively. There were no other lease cost other than short-term lease cost for the years ended December 31, 2018, 2019 and 2020.

(u) Income taxes

Separate return method is applied in the preparation of the combined financial statements. Current income taxes are provided on the basis of net income for financial reporting purposes, adjusted for income and expense items which are not assessable or deductible for income tax purposes, in accordance with the regulations of the relevant tax jurisdictions. Deferred income taxes are accounted for using an asset and liability method. Under this method, deferred income taxes are recognized for the tax consequences of temporary differences by applying enacted statutory rates applicable to future years to differences between the combined financial statement carrying amounts and the tax bases of existing assets and liabilities. The tax base of an asset or liability is the amount attributed to that asset or liability for tax purpose. The effect on deferred taxes of a change in tax rates is recognized in statement of comprehensive income in the period of change. A valuation allowance is provided to reduce the amount of deferred tax assets if it is considered more likely than not that some portion of, or all of the deferred tax assets will not be realized.

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

2. Principal accounting policies—continued

(u) Income taxes—continued

Uncertain tax positions

The guidance on accounting for uncertainties in income taxes prescribes a more likely than not threshold for combined financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Guidance was also provided on derecognition of income tax assets and liabilities, classification of current and deferred income tax assets and liabilities, accounting for interest and penalties associated with tax positions, accounting for income taxes in interim periods, and income tax disclosures. Significant judgment is required in evaluating the Target Business’ uncertain tax positions and determining its provision for income taxes. Management recognizes interests and penalties, if any, under accrued expenses and other current liabilities on its balance sheet and under other expenses in its statements of comprehensive income. Management did not recognize any significant interest and penalties associated with uncertain tax positions for the years ended December 31, 2018, 2019 and 2020. As of December 31, 2018, 2019 and 2020, the Target Business did not have any significant unrecognized uncertain tax positions.

Adoption of ASU 2016-16

In October 2016, the FASB issued ASU 2016-16, Income Taxes: Intra-Entity Transfers of Assets Other Than Inventory (Topic 740). This standard will require entities to recognize the income tax consequences of intra-entity transfers of assets other than inventory at the time of transfer. This standard requires a modified retrospective approach to adoption. The Target Business adopted ASU 2016-16 from January 1, 2018 using a modified retrospective transition method. There was no material impact to the combined financial statements.

(v) Related parties

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 operating decisions. Parties are also considered to be related if they are subject to common control or significant influence, such as a family member or relative, shareholder, or a related corporation.

(w) Comprehensive income

Comprehensive income is defined as the change in equity of the Target Business during a period arising from transactions and other events and circumstances excluding transactions resulting from investments by shareholders and distributions to shareholders. Comprehensive income is reported in the combined statements of comprehensive income.

(x) Recently issued accounting pronouncements

In December 2019, the FASB issued ASU 2019-12, “Simplifying the Accounting for Income Taxes” to remove specific exceptions to the general principles in Topic 740 and to simplify accounting for income taxes. The standard is effective for public companies for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2020. For all other entities, the standard is effective for fiscal years beginning after December 15, 2021, and interim periods within fiscal years

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

2. Principal accounting policies—continued

(x) Recently issued accounting pronouncements—continued

beginning after December 15, 2022. Early adoption is permitted. The standard is effective for the fiscal year beginning January 1, 2022. Management is currently evaluating the impact of this accounting standard update on its combined financial statements.

3. Certain risks and concentration

(a) PRC regulations

Foreign ownership of internet-based businesses is subject to significant restrictions under the current PRC laws and regulations. The PRC government regulates internet access, the distribution of online information and the conduct of online commerce through strict business licensing requirements and other government regulations. These laws and regulations also limit foreign ownership in PRC companies that provide internet information distribution services. Specifically, foreign ownership in an internet information provider or other value-added telecommunication service providers may not exceed 50%. JOYY is incorporated in the Cayman Islands and accordingly, is considered as a foreign invested enterprise under PRC law.

As mentioned in Note 1(e), in order to comply with the PRC laws restricting foreign ownership in the online business in China, the Target Business is operated in China through contractual arrangements with Guangzhou Huaduo. As of December 31, 2020, Beijing Tuda Science and Technology Co., Ltd. owned the majority equity interests of Guangzhou Huaduo.

Guangzhou Huaduo holds the licenses and permits necessary to conduct its internet value-added services in the PRC. If the Parent Company had direct ownership of the VIE, it would be able to exercise its rights as a shareholder to effect changes in the board of directors, which in turn could affect changes at the management level, subject to any applicable fiduciary obligations. However, under the current contractual arrangements, it relies on the VIE and its shareholders’ performance of their contractual obligations to exercise effective control. In addition, the Target Business’ contractual agreements have terms range from 10 to 30 years, which are subject to Beijing Huanju Shidai’s unilateral termination right. Under the respective service agreements, Beijing Huanju Shidai will provide services including technology support, technology services, business support and consulting services to Guangzhou Huaduo, respectively, in exchange for service fees. The amount of service fees payable is determined by various factors, including (a) a percentage of Guangzhou Huaduo’s revenues or earnings, and (b) the expenses that Beijing Huanju Shidai, incur for providing such services. Beijing Huanju Shidai, may charge up to 100% of the income in Guangzhou Huaduo and a multiple of the expenses incurred for providing such services, as determined by Beijing Huanju Shidai, from time to time. The service fees payable by Guangzhou Huaduo to Beijing Huanju Shidai are determined to be up to 100% of the profits of Guangzhou Huaduo, with the timing of such payment to be determined at the sole discretion of Beijing Huanju Shidai. If fees were incurred, it would be significant to the Parent Company and the operating companies’ economic performance because it will be incurred and paid at up to 100% of the earnings of the VIE. Fees incurred would be remitted, subject to further PRC restrictions. None of the VIEs or their shareholders are entitled to terminate the contracts prior to the expiration date, unless under remote circumstances such as a material breach of agreement or bankruptcy as it pertains to the service and business operation agreements and their amendment.

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

3. Certain risks and concentration—continued

(a) PRC regulations—continued

For the years ended December 31, 2018, 2019 and 2020, the wholly owned foreign enterprises determined that service fees of RMB122,596, RMB86,676 and RMB1,184,614 were charged to Guangzhou Huaduo and its subsidiaries, respectively.

Further, management believes that the contractual arrangements among Beijing Huanju Shidai and Gungzhou Huaduo, the VIE, and their shareholders are in compliance with PRC law and are legally enforceable. However, there are substantial uncertainties regarding the interpretation and application of PRC laws and regulations including those that govern the contractual arrangements, which could limit the Parent Company’ ability to enforce these contractual arrangements and if the nominee shareholders of the VIEs were to reduce their interests in the Target Business, their interest may diverge from that of the Target Business and that may potentially increase the risk that they would seek to act contrary to the contractual arrangements.

In March 2019, the National People’s Congress enacted PRC Foreign Investment Law which would be effective starting from January 1, 2020. The Foreign Investment Law does not explicitly classify contractual arrangements as a form of foreign investment, but it contains a catch-all provision under the definition of “foreign investment”, which includes investments made by foreign investors through means stipulated in laws or administrative regulations or other methods prescribed by the State Council. Existing laws or administrative regulations remain unclear whether the contractual arrangements with variable interest entities will be deemed to be in violation of the market access requirements for foreign investment under the PRC laws and regulations. However, the possibility that such entities will be deemed as foreign invested enterprise and subject to relevant restrictions in the future shall not be excluded. If VIEs fall within the definition of foreign investment entities, Parent Company’ ability to use the contractual arrangements with its VIEs and Parent Company’ ability to conduct business through the VIEs could be severely limited. Parent Company’ ability to control the VIEs also depends on the power of attorney that the wholly owned subsidiary of Parent Company has to vote on all matters requiring shareholder approval in the VIEs. As noted above, management believes these power of attorney are legally enforceable but may not be as effective as direct equity ownership. In addition, if JOYY’s corporate structure and the contractual arrangements with the VIEs through which the Target Business was conducted in the PRC were found to be in violation of any existing or future PRC laws and regulations, the relevant PRC regulatory authorities could:

- revoke or refuse to grant or renew the business and operating licenses;
- restrict or prohibit related party transactions between the wholly owned subsidiary and the VIE;
- impose fines, confiscate income or other requirements which the Target Business may find difficult or impossible to comply with;
- require the Target Business to alter, discontinue or restrict its operations;
- restrict or prohibit the Target Business’ ability to finance its operations, and;
- take other regulatory or enforcement actions against JOYY Group that could be harmful to the Target Business.

The imposition of any of these restrictions or actions could result in a material adverse effect on the JOYY Group’s ability to conduct its business. In such case, JOYY may not be able to operate or

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

3. Certain risks and concentration—continued

(a) PRC regulations—continued

control the VIEs, which may result in deconsolidation of the VIEs in the combined financial statements. In the opinion of management, the likelihood for the Target Business to lose such ability is remote based on current facts and circumstances. The Target Business’s operations depend on the VIEs to honor their contractual arrangements with JOYY’s PRC subsidiaries. These contractual arrangements are governed by PRC law and disputes arising out of these agreements are expected to be decided by arbitration in the PRC. Management believes that each of the contractual arrangements constitutes valid and legally binding obligations of each party to such contractual arrangements under PRC laws. However, the interpretation and implementation of the laws and regulations in the PRC and their application to an effect on the legality, binding effect and enforceability of contracts are subject to the discretion of competent PRC authorities, and therefore there is no assurance that relevant PRC authorities will take the same position as the Target Business herein in respect of the legality, binding effect and enforceability of each of the contractual arrangements. Meanwhile, since the PRC legal system continues to rapidly evolve, the interpretations of many laws, regulations and rules are not always uniform and enforcement of these laws, regulations and rules involve uncertainties, which may limit legal protections available to the Target Business to enforce the contractual arrangements should the VIEs or the nominee shareholders of the VIEs fail to perform their obligations under those arrangements.

APPENDIX IB

ACCOUNTANT’S REPORT OF YY LIVE

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

3. Certain risks and concentration—continued

(a) PRC regulations—continued

The following combined financial information of the Target Business’ VIEs excluding the intercompany items with the Target Business’ subsidiaries was included in the accompanying combined financial statements as of and for the years ended:

| | December 31, | | |
|---|------------------|------------------|------------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Assets | | | |
| Current assets | | | |
| Cash and cash equivalents | 48,238 | 69,722 | 196,184 |
| Short-term investments | — | 70,327 | — |
| Accounts receivable, net | 74,253 | 79,430 | 206,420 |
| Amounts due from related parties | 1,537 | 1,087 | 456 |
| Prepayments and other current assets | 24,099 | 36,921 | 42,109 |
| Total current assets | <u>148,127</u> | <u>257,487</u> | <u>445,169</u> |
| Non-current assets | | | |
| Deferred tax assets | 71 | 16,021 | 7,767 |
| Property and equipment, net | 49,065 | 80,529 | 57,229 |
| Intangible assets, net | 84 | 46,445 | 43,310 |
| Other non-current assets | 2,292 | 8,571 | 19,131 |
| Total non-current assets | <u>51,512</u> | <u>151,566</u> | <u>127,437</u> |
| Total assets | <u>199,639</u> | <u>409,053</u> | <u>572,606</u> |
| Liabilities | | | |
| Current liabilities | | | |
| Deferred revenue | 425,226 | 355,549 | 326,702 |
| Advances from customers | 80,504 | 97,928 | 80,761 |
| Income taxes payable | — | 3,459 | 21,014 |
| Accrued liabilities and other current liabilities | 935,409 | 887,338 | 753,214 |
| Total current liabilities | <u>1,441,139</u> | <u>1,344,274</u> | <u>1,181,691</u> |
| Non-current liabilities | | | |
| Deferred revenue | 6,243 | 58,210 | 28,807 |
| Total non-current liabilities | <u>6,243</u> | <u>58,210</u> | <u>28,807</u> |
| Total liabilities | <u>1,447,382</u> | <u>1,402,484</u> | <u>1,210,498</u> |
| For the year ended December 31, | | | |
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Net revenues | 10,272,696 | 10,962,538 | 9,950,286 |
| Net income | <u>3,403,357</u> | <u>3,752,690</u> | <u>3,702,266</u> |

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

3. Certain risks and concentration—continued

(a) PRC regulations—continued

| | For the year ended December 31, | | |
|---|---------------------------------|---------------|----------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Net cash provided by operating activities | 3,876,015 | 3,835,805 | 3,672,284 |
| Net cash (used in) provided by investing activities | (26,372) | (192,741) | 48,269 |
| Net cash used in financing activities | (3,809,302) | (3,621,109) | (3,418,963) |
| | <u>40,341</u> | <u>21,955</u> | <u>301,590</u> |

(b) Foreign exchange risk

The revenues and expenses of the Target Business in the PRC are generally denominated in RMB and their assets and liabilities are denominated in RMB. The RMB is not freely convertible into foreign currencies. Remittances of foreign currencies into the PRC or remittances of RMB out of the PRC as well as exchange between RMB and foreign currencies require approval by foreign exchange administrative authorities and certain supporting documentation. The State Administration for Foreign Exchange, under the authority of the People’s Bank of China, controls the conversion of RMB into other currencies.

(c) Credit risk

Assets that potentially expose the Target Business to credit risk primarily consist of cash and cash equivalents, short-term investments, accounts receivable, amounts due from related parties, prepayments and other current assets.

As of December 31, 2018, 2019 and 2020, substantially all of the Target Business’ cash and cash equivalents and short-term investments were placed with the PRC financial institutions. Management chooses these institutions because of their reputations and track records for stability, and their known large cash reserves, and management periodically reviews these institutions’ reputations, track records, and reported reserves. Management expects that any additional institutions that the Target Business uses for its cash and bank deposits will be chosen with similar criteria for soundness. Nevertheless under the PRC law, it is required that a commercial bank in the PRC that holds third party cash deposits should maintain a certain percentage of total customer deposits taken in a statutory reserve fund for protecting the depositors’ rights over their interests in deposited money. PRC banks are subject to a series of risk control regulatory standards; PRC bank regulatory authorities are empowered to take over the operation and management of any PRC bank that faces a material credit crisis. Management believes that it is not exposed to unusual risks as these financial institutions are PRC banks with high credit quality. The Target Business had not experienced any losses on its deposits of cash and cash equivalents and term deposits during the years ended December 31, 2018, 2019 and 2020 and management believes that its credit risk to be minimal.

The risk with respect to accounts receivable is mitigated by credit evaluations management performs on the payment platforms, customers and the ongoing monitoring process of outstanding balances.

Amounts due from related parties, prepayments and other current assets are typically unsecured. In evaluating the collectability of the balance, management considers many factors, including the related

APPENDIX IB

ACCOUNTANT’S REPORT OF YY LIVE

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

3. Certain risks and concentration—continued

(c) Credit risk—continued

parties and third parties’ repayment history and their credit-worthiness. An allowance for doubtful accounts is made when collection of the full amount is no longer probable.

4. Cash and cash equivalents

Cash and cash equivalents represent cash on hand, demand deposits placed with banks or other financial institutions and all highly liquid investments with original maturities of three months or less. Cash and cash equivalents balance as of December 31, 2018, 2019 and 2020 were all denominated in RMB.

5. Accounts receivable, net

| | December 31, | | |
|--|---------------|---------------|----------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Accounts receivable, gross | 74,728 | 79,430 | 207,471 |
| Less: allowance for doubtful receivables | (475) | — | (891) |
| Accounts receivable, net | <u>74,253</u> | <u>79,430</u> | <u>206,580</u> |

The following table summarizes the details of the Target Business’ allowance for doubtful accounts:

| | For the year ended December 31, | | |
|---|------------------------------------|----------|--------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Balance at the beginning of the year | — | (475) | — |
| Adoption of ASC326 | — | — | (643) |
| (Additions charged to) reversals credited to general and administrative expenses, net | (475) | 75 | (248) |
| Write-off during the year | — | 400 | — |
| Balance at the end of the year | <u>(475)</u> | <u>—</u> | <u>(891)</u> |

6. Prepayments and other current assets

| | December 31, | | |
|---|---------------|---------------|---------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Prepayments and deposits to vendors and content providers | 5,806 | 15,241 | 23,492 |
| Value added taxes to be deducted | 5,962 | 163 | 8,046 |
| Deposits | 5,186 | 2,907 | 5,936 |
| Penalty receivables from defaulted performers | — | 11,221 | 3,392 |
| Employee advances | 1,686 | 2,284 | 2,584 |
| Others | 7,145 | 7,389 | 1,551 |
| Total | <u>25,785</u> | <u>39,205</u> | <u>45,001</u> |

APPENDIX IB

ACCOUNTANT’S REPORT OF YY LIVE

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

7. Property and equipment, net

Property and equipment consists of the following:

| | December 31, | | |
|---|---------------|---------------|---------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Gross carrying amount | | | |
| Servers, computers and equipment | 340,810 | 413,472 | 435,498 |
| Less: accumulated depreciation | (291,582) | (332,882) | (375,598) |
| Property and equipment, net | <u>49,228</u> | <u>80,590</u> | <u>59,900</u> |

Depreciation expenses for the years ended December 31, 2018, 2019 and 2020 were RMB59,119, RMB41,300, and RMB42,716, respectively.

8. Intangible assets, net

The following table summarizes the Target Business’ intangible assets:

| | December 31, | | |
|---------------------------------------|----------------|----------------|-----------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Gross carrying amount | | | |
| License | — | 46,890 | 46,890 |
| Domain names | 15,110 | 15,357 | 14,372 |
| Total of gross carrying amount | <u>15,110</u> | <u>62,247</u> | <u>61,262</u> |
| Less: accumulated amortization | | | |
| License | — | (521) | (3,647) |
| Domain names | (8,051) | (9,207) | (9,573) |
| Total accumulated amortization | <u>(8,051)</u> | <u>(9,728)</u> | <u>(13,220)</u> |
| Intangible assets, net | <u>7,059</u> | <u>52,519</u> | <u>48,042</u> |

Amortization expenses for the years ended December 31, 2018, 2019 and 2020 were RMB625, RMB1,430 and RMB4,477, respectively.

The estimated amortization expenses for each of the following five years are as follows:

| | Amortization expense of intangible assets |
|------------|--|
| | RMB |
| 2021 | 4,084 |
| 2022 | 4,084 |
| 2023 | 4,084 |
| 2024 | 4,084 |
| 2025 | 3,497 |

APPENDIX IB

ACCOUNTANT’S REPORT OF YY LIVE

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

8. Intangible assets, net—continued

The weighted average amortization periods of intangible assets as of December 31, 2018, 2019 and 2020 are as below:

| | December 31, | | |
|--------------------|----------------|----------|----------|
| | 2018 | 2019 | 2020 |
| License | Not applicable | 15 years | 15 years |
| Domain names | 15 years | 15 years | 15 years |

9. Deferred revenue

| | December 31, | | |
|--|----------------|----------------|----------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Deferred revenue, current | | | |
| Live streaming | 374,750 | 264,658 | 277,823 |
| Others | 50,476 | 90,891 | 48,879 |
| Total current deferred revenue | <u>425,226</u> | <u>355,549</u> | <u>326,702</u> |
| Deferred revenue, non-current | | | |
| Live streaming | — | — | — |
| Others | 6,243 | 58,210 | 28,807 |
| Total non-current deferred revenue | <u>6,243</u> | <u>58,210</u> | <u>28,807</u> |

10. Accrued liabilities and other current liabilities

| | December 31, | | |
|---|----------------|----------------|----------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Revenue sharing fees | 709,872 | 648,436 | 555,987 |
| Salaries and welfare | 50,758 | 78,573 | 128,825 |
| Marketing and promotion expenses | 80,548 | 80,068 | 110,423 |
| Value added taxes and other taxes payable | 27,725 | 25,403 | 44,078 |
| Deposits from third parties | 27,949 | 24,535 | 22,823 |
| Other payable to content providers | 11,196 | 9,707 | 10,941 |
| Others | 28,619 | 38,196 | 34,615 |
| Total | <u>936,667</u> | <u>904,918</u> | <u>907,692</u> |

APPENDIX IB

ACCOUNTANT’S REPORT OF YY LIVE

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

11. Cost of revenues

| | For the year ended December 31, | | |
|--|---------------------------------|------------------|------------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Revenue sharing fees and content costs | 4,888,835 | 5,190,224 | 4,866,294 |
| Bandwidth costs | 178,231 | 215,694 | 192,851 |
| Salaries and welfare | 82,466 | 100,908 | 97,505 |
| Payment handling costs | 100,108 | 93,569 | 67,911 |
| Other taxes and surcharges | 31,211 | 36,203 | 39,267 |
| Depreciation and amortization | 48,447 | 37,443 | 39,169 |
| Technical service fee | 51 | 4,501 | 18,687 |
| Share-based compensation | 17,494 | 8,655 | 11,241 |
| Other costs | 10,943 | 16,058 | 9,447 |
| Total | 5,357,786 | 5,703,255 | 5,342,372 |

12. Other income

| | For the year ended December 31, | | |
|---------------------------------|---------------------------------|----------------|----------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Government grants (a) | 49,953 | 168,754 | 156,969 |
| Others | 17,065 | 34,654 | 9,303 |
| Total | 67,018 | 203,408 | 166,272 |

Note:

(a) Government grants represented various grants from different governmental authorities mainly including tax refund, subsidies related to talent retention as well as other subsidies.

13. Income tax

(i) Cayman Islands

Under the current tax laws of Cayman Islands, Runderfo is not subject to tax on income or capital gains. Besides, upon payment of dividends by Runderfo to its shareholders, no Cayman Islands withholding tax will be imposed.

(ii) BVI

Duowan BVI is exempted from income tax on its foreign-derived income in the BVI. There are no withholding taxes in the BVI.

(iii) PRC

Entities of the Target Business in China are governed by the Enterprise Income Tax Law (“EIT Law”), which became effective on January 1, 2008. Pursuant to the EIT Law and its implementation rules, enterprises in China are generally subject to tax at a statutory rate of 25%. Certified High and New Technology Enterprises (“HNTE”) are entitled to a favorable tax rate of 15%, but need to re-apply every three years. During this three-year period, an HNTE must conduct a qualification self-review each year to ensure it meets the HNTE criteria and is eligible for the 15% preferential tax rate for that

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

13. Income tax—continued

(iii) PRC—continued

year. If an HNTE fails to meet the criteria for qualification in any year, the enterprise cannot enjoy the preferential tax rate in that year, and must instead use the regular 25% EIT rate.

Enterprises qualified as software enterprises can enjoy an income tax exemption for two years beginning with their first profitable year and a 50% tax reduction to the applicable tax rate for the subsequent three years. An entity that qualifies as a “Key National Software Enterprise” (a “KNSE”) is entitled to a further reduced preferential income tax rate of 10%. Enterprises wishing to enjoy the status of a Software Enterprise or a KNSE must perform a self-assessment each year to ensure they meet the criteria for qualification and file required supporting documents with the tax authorities before adopting the preferential EIT rates. These enterprises will be subject to the tax authorities’ assessment each year as to whether they are entitled to use the relevant preferential EIT treatments. If at any time during the preferential tax treatment years an enterprise uses the preferential EIT rates but the relevant authorities determine that it fails to meet applicable criteria for qualification, the relevant authorities may revoke the enterprise’s Software Enterprise/KNSE status.

The EIT Law also provides that an enterprise established under the laws of a foreign country or region but whose “de facto management body” is located in the PRC be treated as a resident enterprise for PRC tax purposes and consequently be subject to the PRC income tax at the rate of 25% for its global income. The Implementing Rules of the EIT Law merely define the location of the “de facto management body” as “the place where the exercising, in substance, of the overall management and control of the production and business operation, personnel, accounting, properties, etc., of a non-PRC company is located.” Based on a review of surrounding facts and circumstances, management does not believe that it is likely that its entities registered outside of the PRC should be considered as resident enterprises for the PRC tax purposes.

The Target Business’ PRC entities provided for enterprise income tax are as follows:

- Guangzhou Huaduo is qualified as HNTE and entitled to enjoy the beneficial tax rate of 15% from 2018 to 2020.
- Guangzhou Huanju Shidai was qualified as a KNSE after the relevant government authorities’ assessment and was entitled to a preferential income tax rate of 10%. Guangzhou Huanju Shidai applied a reduced tax rate of 10% from 2018 to 2020.
- In June 2017, Guangzhou Juhui Information Technology Co., Ltd. was qualified as a Software Enterprise, and started to enjoy the zero preferential tax rate beginning from 2016 and 12.5% preferential tax rate from 2018 to 2020.
- Other major PRC subsidiaries and VIEs were subject to 25% EIT for the periods reported.

According to a policy promulgated by the State Tax Bureau of the PRC and effective from 2008 onwards, enterprises engaged in research and development activities are entitled to claim an additional tax deduction amounting to 50% of the qualified research and development expenses incurred in determining its tax assessable profits for that year. The additional tax deducting amount of the qualified research and development expenses have been increased from 50% to 75%, effective from 2018 to

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

13. Income tax—continued

(iii) PRC—continued

2020, according to a new tax incentives policy promulgated by the State Tax Bureau of the PRC in September 2018 (“Super Deduction”).

Qualified subsidiaries and VIEs of the Target Business claimed the Super Deduction in ascertaining the tax assessable profits for the periods reported.

Composition of income tax expense

The current and deferred portions of income tax expense included in the combined statements of comprehensive income are as follows:

| | <u>For the year ended December 31,</u> | | |
|---|--|------------------|------------------|
| | <u>2018</u> | <u>2019</u> | <u>2020</u> |
| | <u>RMB</u> | <u>RMB</u> | <u>RMB</u> |
| Income before income tax expenses | 3,869,558 | 4,366,991 | 3,680,722 |
| Current income tax expenses | <u>(522,004)</u> | <u>(682,261)</u> | <u>(531,181)</u> |
| Deferred income tax (expenses) benefit | <u>(58,931)</u> | <u>15,950</u> | <u>(8,254)</u> |
| Income tax expenses | <u>(580,935)</u> | <u>(666,311)</u> | <u>(539,435)</u> |

Reconciliation of the differences between statutory tax rate and the effective tax rate

The reconciliation of total tax expense computed by applying the respective statutory income tax rate to pre-tax income is as follows:

| | <u>For the year ended December 31,</u> | | |
|--|--|----------------|----------------|
| | <u>2018</u> | <u>2019</u> | <u>2020</u> |
| PRC Statutory income tax rate | (25.0%) | (25.0%) | (25.0%) |
| Effect of tax holiday and preferential tax benefit | 10.1% | 9.9% | 11.0% |
| Permanent differences ⁽ⁱ⁾ | (0.8%) | (0.5%) | (0.5%) |
| Change in valuation allowance | (0.1%) | (0.5%) | (1.1%) |
| Effect of Super Deduction available to the Target Business | <u>0.8%</u> | <u>0.8%</u> | <u>0.9%</u> |
| Effective income tax rate | <u>(15.0%)</u> | <u>(15.3%)</u> | <u>(14.7%)</u> |

Note:

(i) Permanent differences mainly arise from expenses not deductible for tax purposes including primarily share-based compensation costs and expenses incurred by subsidiaries and VIEs.

APPENDIX IB

ACCOUNTANT’S REPORT OF YY LIVE

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

13. Income tax—continued

Deferred tax assets and liabilities

Deferred taxes are measured using the enacted tax rates for the periods in which they are expected to be reversed. The tax effects of temporary differences that give rise to the deferred tax asset balances as of December 31, 2018, 2019 and 2020 are as follows:

| | December 31, | | |
|---|--------------|---------------|--------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Deferred tax assets: | | | |
| Tax loss carried forward | 20,858 | 26,998 | 48,233 |
| Allowance for doubtful receivable, accrued expense and others not currently deductible for tax purposes | 394 | 16,373 | 33,428 |
| Deferred revenue | — | 14,708 | 7,767 |
| Valuation allowance ⁽ⁱ⁾ | (21,181) | (42,058) | (81,661) |
| Total deferred tax assets, net | <u>71</u> | <u>16,021</u> | <u>7,767</u> |

Note:

(i) Valuation allowance is provided against deferred tax assets when management determines that it is more likely than not that the deferred tax assets will not be utilized in the future. In making such determination, management considered factors including future taxable income exclusive of reversing temporary differences and tax loss carry forwards. Valuation allowance was provided for net operating loss carry forward because it was more likely than not that such deferred tax assets would not be realized based on management estimate of its future taxable income. If events occur in the future that allow the Target Business to realize more of its deferred income tax than the presently recorded amounts, an adjustment to the valuation allowances will result in a decrease in tax expense when those events occur.

Movement of valuation allowance

| | For the year ended December 31, | | |
|--|---------------------------------|-----------------|-----------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Balance at beginning of the year | (16,257) | (21,181) | (42,058) |
| Additions | (13,210) | (30,084) | (39,631) |
| Reversals | 8,286 | 9,207 | 28 |
| Balance at end of the year | <u>(21,181)</u> | <u>(42,058)</u> | <u>(81,661)</u> |

Tax loss carry forwards

Before the completion of the reorganization, income tax is calculated based on a separate return basis as if the entities of the Target Business had filed separate tax returns. Therefore, certain entities of the Target Business was deemed to have tax losses carried forward amounting to RMB87,861, RMB120,004 and RMB234,360 as of December 31, 2018, 2019 and 2020 as if it had filed separate tax returns before. These tax losses expire from 2021 through 2030.

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

13. Income tax—continued

Tax loss carry forwards—continued

In accordance with PRC Tax Administration Law on the Levying and Collection of Taxes, the PRC tax authorities generally have up to five years to claw back underpaid tax plus penalties and interest for PRC entities’ tax filings. In the case of tax evasion, which is not clearly defined in the law, there is no limitation on the tax years open for investigation. There were no ongoing examinations by tax authorities as of December 31, 2020.

14. Earnings per share

No earnings per share information is presented as its inclusion, for the purpose of this report, is not considered meaningful due to the Reorganization and the presentation of the results for the years ended December 31, 2018, 2019 and 2020 on a combined basis as disclosed in Note 1(c).

15. Related party transactions

The table below sets forth the major related parties and their relationships with the Target Group:

| Major related parties | Relationship with the Target Group |
|-------------------------------------|---|
| The Parent Company | The Target Group is controlled by the Parent Company |
| Xiaomi Corporation (“Xiaomi Group”) | Controlled by a principal shareholder of the Parent Company |

During the years ended December 31, 2018, 2019 and 2020, significant related party transactions are as follows:

| | For the year ended December 31, | | |
|--|---------------------------------|-------------|-------------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Contribution to the Parent Company | (3,723,605) | (3,600,884) | (3,002,014) |
| Share-based compensation expenses related to JOYY’s Share-based Awards | 193,196 | 140,327 | 92,722 |
| Transactions with Xiaomi Group | 659 | 9,585 | 406 |

As of December 31, 2018, 2019 and 2020, the amounts due from/to related parties are as follows:

| | December 31, | | |
|---|--------------|-------|------|
| | 2018 | 2019 | 2020 |
| | RMB | RMB | RMB |
| Amounts due from related parties | | | |
| Due from Xiaomi Group | 1,537 | 1,087 | 456 |

All amounts due from related parties as of December 31, 2018, 2019 and 2020 are trade in nature.

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

16. Fair value measurements

Fair value reflects the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, management considers the principal or most advantageous market in which it would transact and considers assumptions that market participants would use when pricing the assets or liabilities.

Management applies a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. A financial instrument’s categorization within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. This guidance specifies a hierarchy of valuation techniques, which is based on whether the inputs into the valuation technique are observable or unobservable. The hierarchy is as follows:

Level 1—Valuation techniques in which all significant inputs are unadjusted quoted prices from active markets for assets or liabilities that are identical to the assets or liabilities being measured.

Level 2—Valuation techniques in which significant inputs include quoted prices from active markets for assets or liabilities that are similar to the assets or liabilities being measured and/or quoted prices for assets or liabilities that are identical or similar to the assets or liabilities being measured from markets that are not active. Also, model-derived valuations in which all significant inputs and significant value drivers are observable in active markets are Level 2 valuation techniques.

Level 3—Valuation techniques in which one or more significant inputs or significant value drivers are unobservable. Unobservable inputs are valuation technique inputs that reflect management’s own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The fair value guidance describes three main approaches to measure the fair value of assets and liabilities: (1) market approach; (2) income approach and (3) cost approach. The market approach uses prices and other relevant information generated from market transactions involving identical or comparable assets or liabilities. The income approach uses valuation techniques to convert future amounts to a single present value amount. The measurement is based on the value indicated by current market expectations about those future amounts. The cost approach is based on the amount that would currently be required to replace an asset.

When available, management uses quoted market prices to determine the fair value of an asset or liability. If quoted market prices are not available, management will measure fair value using valuation techniques that use, when possible, current market-based or independently sourced market parameters, such as interest rates and currency rates.

II NOTES TO THE HISTORICAL FINANCIAL INFORMATION—continued

(All amount in thousands, unless otherwise stated)

16. Fair value measurements—continued

Fair value measurement on a non-recurring basis—continued

Apart from the short-term investments, other financial instruments of the Target Business principally consist of cash and cash equivalents, accounts receivable, other receivables, amounts due from related parties and certain accrued expenses. These financial instruments are recorded at cost which approximates fair value.

17. Commitments and contingencies

The Target Business did not have significant commitments and contingent liabilities as of December 31, 2018, 2019 and 2020.

18. Subsequent events

Management evaluated subsequent events through [●], which was the date which the Underlying Financial Statements were issued.

Subsequent to December 31, 2020, the Target Business was transferred to the Target Group and the Reorganization as described in Note 1(b) was completed. As of the date of this report, the acquisition of the Target Business by Baidu in the Transaction as described in Note 1(a) has been substantially completed, with certain customary matters remaining to be completed in the near future.

III SUBSEQUENT FINANCIAL STATEMENTS

No audited financial statements have been prepared by management of the Target Business in respect of any period subsequent December 31, 2020 and up to the date of this report. No dividend or distribution has been declared or made by Runderfo or any of the companies comprising the Target Group in respect of any period subsequent to December 31, 2020.

APPENDIX IIA UNAUDITED PRO FORMA FINANCIAL INFORMATION

The following information sets out in this appendix does not form part of the Accountants’ Report from Ernst & Young, Certified Public Accountants, Hong Kong, the Company’s reporting accountants, as set out in Appendix IA to this [REDACTED], and is included for information purpose only. The unaudited pro forma financial information should be read in conjunction with the section headed “Financial Information” in this [REDACTED] and the Accountants’ Report set out in Appendix IA to this [REDACTED].

(A) UNAUDITED PRO FORMA STATEMENT OF ADJUSTED CONSOLIDATED NET TANGIBLE ASSETS

The following unaudited pro forma statement of adjusted consolidated net tangible assets prepared in accordance with Rule 4.29 of the Hong Kong Listing Rules are set out below for the purpose of illustrating the effect of the [REDACTED] on the consolidated net tangible assets attributable to ordinary shareholders of the Company as if the [REDACTED] had been completed on December 31, 2020.

The unaudited pro forma statement of adjusted consolidated net tangible assets has been prepared for illustrative purpose only and, because of its hypothetical nature, it may not reflect a true picture of the consolidated net tangible assets attributable to ordinary shareholders of the Company had the [REDACTED] been completed as of December 31, 2020 or at any future date.

The unaudited pro forma statement of adjusted consolidated net tangible assets is prepared based on the unaudited consolidated net tangible assets attributable to ordinary shareholders of the Company as of December 31, 2020, as extracted from the Company’s consolidated financial statements for the year ended December 31, 2020 included in Appendix IA to the [REDACTED], and is adjusted for the effect of the [REDACTED] described below.

| | Unaudited consolidated net tangible assets attributable to ordinary shareholders of the Company as of December 31, 2020 | Estimated [REDACTED] from the [REDACTED] | Unaudited pro forma adjusted consolidated net tangible assets attributable to ordinary shareholders of the Company as of December 31, 2020 | Unaudited pro forma adjusted net tangible assets per Share | Unaudited pro forma adjusted net tangible assets per ADS | Unaudited pro forma adjusted net tangible assets per Share | Unaudited pro forma adjusted net tangible assets per ADS |
|--|---|--|--|--|--|--|--|
| | (in millions of RMB) (Note 1) | (in millions of RMB) (Note 2) | (in millions of RMB) | (RMB) (Note 3) | (RMB) (Note 4) | (HK\$) (Note 5) | (HK\$) (Note 5) |
| Based on an indicative [REDACTED] of HK\$[REDACTED] per [REDACTED] ... | 158,426 | [REDACTED] | [REDACTED] | [REDACTED] | [REDACTED] | [REDACTED] | [REDACTED] |

Notes:

- The unaudited consolidated net tangible assets attributable to ordinary shareholders of the Company as of December 31, 2020 is arrived at after deducting Intangible assets of RMB2,022 million and Goodwill of RMB22,248 million from the Total Baidu, Inc. shareholders’ equity of RMB182,696 million as of December 31, 2020, as shown in the Accountants’ Report as set out in Appendix IA to the [REDACTED]. For the avoidance of doubt, “Licensed copyrights, net” and “Produced content, net” were not deducted for the purpose of calculating the unaudited consolidated net tangible assets attributable to ordinary shareholders of the Company.
[REDACTED]
- The unaudited pro forma adjusted net tangible assets attributable to ordinary shareholders of the Company per Share is calculated based on a total of [REDACTED] that will be in issue assuming that the [REDACTED] have been completed on December 31, 2020 and after having accounted for the Share Subdivision (as defined in the [REDACTED]), but do not take into account any allotment and issuance of Shares upon exercise of the [REDACTED], the Shares to be issued pursuant to the Share Incentive Plans, including pursuant to the exercise of options or other awards that have been or may be granted from time to time and any issuance or repurchase of Shares by the Company.

APPENDIX IIA UNAUDITED PRO FORMA FINANCIAL INFORMATION

- (4) The unaudited pro forma adjusted net tangible assets attributable to ordinary shareholders of the Company per ADS is calculated based on that eight Shares equals one ADS.
- (5) The unaudited pro forma adjusted net tangible assets per Share and the unaudited pro forma adjusted net tangible assets per ADS are converted into Hong Kong dollars at an exchange rate of RMB0.8416 to HK\$1.00.
- (6) No adjustment has been made to reflect any trading result, or other transactions of the Group entered into subsequent to December 31, 2020. Assuming the Company’s acquisition of YY Live (as defined in the [REDACTED]) had been completed on December 31, 2020, the unaudited pro forma adjusted net tangible assets per Share and the unaudited pro forma adjusted net tangible assets per ADS would have been RMB[REDACTED] or HK\$[REDACTED] and RMB[REDACTED] or HK\$[REDACTED], respectively.

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APPENDIX IIA UNAUDITED PRO FORMA FINANCIAL INFORMATION

[REDACTED]

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APPENDIX IIA UNAUDITED PRO FORMA FINANCIAL INFORMATION

[REDACTED]

**APPENDIX IIB UNAUDITED PRO FORMA FINANCIAL INFORMATION OF
THE ENLARGED GROUP**

The following information sets out in this appendix does not form part of the Accountants’ Report from Ernst & Young, Certified Public Accountants, Hong Kong, the Company’s reporting accountants, as set out in Appendix IA to this [REDACTED], and is included for information purpose only. The unaudited pro forma financial information should be read in conjunction with the section headed “Financial Information” in this [REDACTED] and the Accountants’ Report set out in Appendix IA and Appendix IB to this [REDACTED].

(A) UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

In November 2020, the Company entered into definitive agreements with JOYY Inc. (“JOYY”), subsequently amended in February 2021, to acquire JOYY’s domestic video-based entertainment live streaming business in China (“YY Live”), which were wholly-owned by JOYY, for total cash consideration of US\$3,300 million (equivalent to approximately RMB21,532 million as at December 31, 2020), subject to certain adjustments, as well as contingent cash consideration of up to US\$300 million (equivalent to approximately RMB1,958 million as at December 31, 2020) subject to certain conditions. The acquisition of YY Live (the “Transaction”) has been substantially completed, with certain customary matters remaining to be completed in the near future. The Transaction will be accounted for as a business combination.

The following is a summary of an illustrative and unaudited pro forma consolidated balance sheet of Baidu, Inc., and its subsidiaries (collectively the “Company”) and YY Live (the “Enlarged Group”) (the “Unaudited Pro Forma Financial Information of the Enlarged Group”), which have been prepared on the basis of the notes set out below for the purpose of illustrating the impact of the Transaction on the Company’s consolidated balance sheet as at December 31, 2020 as if the Transaction had been completed as at December 31, 2020.

This Unaudited Pro Forma Financial Information of the Enlarged Group has been prepared by the Directors of the Company in accordance with paragraph 4.29 of the Listing Rules and Accounting Guideline 7 Preparation of Pro Forma Financial Information for Inclusion in Investment Circulars issued by the Hong Kong Institute of Certified Public Accountants for illustrative purposes only, based on their judgments, estimations and assumptions, and because of its hypothetical nature, it may not give a true picture of the financial position of the Enlarged Group as at December 31, 2020 or at any future date following the completion of the Transaction.

The Unaudited Pro Forma Financial Information of the Enlarged Group is based on the audited consolidated balance sheet of the Company as at December 31, 2020 as set out in the accountants’ report of the Company included in Appendix IA to the [REDACTED], the audited combined balance sheet of YY Live as at December 31, 2020 as set out in the accountant’s report of YY Live included in Appendix IB to the [REDACTED], after giving effect to the pro forma adjustments relating to the Transaction as described in the accompanying notes. Narrative description of the pro forma adjustments that are [(i) directly attributable to the transactions and not relating to future events or decisions]; and (ii) factually supported, is summarised in the accompanying notes.

The Unaudited Pro Forma Financial Information of the Enlarged Group is based on a number of assumptions, estimates, and uncertainties. Accordingly, the Unaudited Pro Forma Financial Information of the Enlarged Group does not purport to describe the actual financial position of the Enlarged Group that would have been attained had the Transaction been completed as at December 31, 2020. The Unaudited Pro Forma Financial Information of the Enlarged Group does not purport to predict future financial positions or results of the Enlarged Group.

**APPENDIX IIB UNAUDITED PRO FORMA FINANCIAL INFORMATION OF
THE ENLARGED GROUP**

UNAUDITED PRO FORMA CONSOLIDATED BALANCE SHEET OF THE ENLARGED GROUP

(Amounts in millions of Renminbi (“RMB”))

| | <u>The Company</u> <i>(Note 1)</i> | <u>YY Live</u> <i>(Note 2)</i> | <u>Acquisition of YY Live</u> <i>(Note 3)</i> | <u>Pro forma Enlarged Group</u> |
|--|---------------------------------------|-----------------------------------|--|---|
| ASSETS | | | | |
| Current assets: | | | | |
| Cash and cash equivalents | 35,782 | 206 | (22,076) | 13,912 |
| Restricted cash | 758 | — | 9,918 | 10,676 |
| Short-term investments | 126,402 | — | — | 126,402 |
| Accounts receivable, net | 8,668 | 207 | — | 8,875 |
| Amounts due from related parties | 726 | — | — | 726 |
| Other assets, current | 11,006 | 45 | — | 11,051 |
| Total current assets | 183,342 | 458 | | 171,642 |
| Non-current assets: | | | | |
| Fixed assets, net | 17,508 | 60 | — | 17,568 |
| Licensed copyrights, net | 6,435 | — | — | 6,435 |
| Produced content, net | 6,556 | — | — | 6,556 |
| Intangible assets, net | 2,022 | 48 | 6,741 | 8,811 |
| Goodwill | 22,248 | — | 16,329 | 38,577 |
| Long-term investments, net | 76,233 | — | — | 76,233 |
| Amounts due from related parties | 3,438 | — | — | 3,438 |
| Deferred tax assets, net | 1,674 | 8 | — | 1,682 |
| Operating lease right-of-use assets | 9,804 | — | — | 9,804 |
| Other assets, non-current | 3,448 | 24 | — | 3,472 |
| Total non-current assets | 149,366 | 140 | | 172,576 |
| Total assets | 332,708 | 598 | | 344,218 |
| LIABILITIES AND EQUITY | | | | |
| Current liabilities: | | | | |
| Short-term loans | 3,016 | — | — | 3,016 |
| Accounts payable and accrued liabilities | 36,716 | 929 | 8,467 | 46,112 |
| Customer deposits and deferred revenue | 12,626 | 407 | — | 13,033 |
| Deferred income | 158 | — | — | 158 |
| Long-term loans, current portion | 7,427 | — | — | 7,427 |
| Convertible notes payable | 4,752 | — | — | 4,752 |
| Amounts due to related parties | 1,324 | — | — | 1,324 |
| Operating lease liabilities | 2,366 | — | — | 2,366 |
| Total current liabilities | 68,385 | 1,336 | | 78,188 |
| Non-current liabilities: | | | | |
| Deferred income | 97 | — | — | 97 |
| Deferred revenue | 686 | 29 | — | 715 |
| Amounts due to related parties | 3,543 | — | — | 3,543 |
| Notes payable | 48,408 | — | — | 48,408 |
| Convertible senior notes | 11,927 | — | — | 11,927 |
| Deferred tax liabilities | 3,067 | — | 1,011 | 4,078 |
| Operating lease liabilities | 4,693 | — | — | 4,693 |
| Other non-current liabilities | 59 | — | 667 | 726 |
| Total non-current liabilities | 72,480 | 29 | | 74,187 |
| Total liabilities | 140,865 | 1,365 | | 152,375 |
| Redeemable noncontrolling interests | 3,102 | — | | 3,102 |
| Equity | | | | |
| Total shareholders' equity/(parent company deficit) | 182,696 | (767) | 767 | 182,696 |
| Noncontrolling interests | 6,045 | — | — | 6,045 |
| Total equity | 188,741 | (767) | | 188,741 |
| Total liabilities, redeemable noncontrolling interests and equity | 332,708 | 598 | | 344,218 |

APPENDIX IIB UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

Notes:

1. The amounts are extracted from the audited consolidated balance sheet of the Company as at December 31, 2020 as set out in the accountants’ report of the Company included in Appendix IA to the [REDACTED].
2. The amounts are extracted from the audited combined balance sheet of YY Live as at December 31, 2020 as set out in the accountant’s report of YY Live included in Appendix IB to the [REDACTED].
3. These adjustments represent:
 - (i) the estimated fair value of the purchase consideration payable by the Company of US\$3,263 million (equivalent to approximately RMB21,292 million as at December 31, 2020) in relation to the Transaction; and

Pursuant to the Share Purchase Agreement, the total consideration is US\$3,600 million (equivalent to approximately RMB23,490 million as at December 31, 2020) in cash, subject to certain adjustments. Approximately US\$2,000 million of the purchase price would be payable to JOYY at the closing of the acquisition. After the closing, subject to certain conditions and adjustments, approximately US\$1,000 million would be deposited in an escrow account and should be paid no later than the later of the closing of the acquisition and April 30, 2021, approximately US\$300 million would be deposited in an escrow account and should be paid no later than the later of the closing of the acquisition and June 30, 2021, and contingent consideration with a maximum amount of US\$300 million would be deposited in an escrow account and be payable subject to the achievement of certain conditions. The Transaction has been substantially completed, with certain customary matters remaining to be completed in the near future.

The estimated fair value of the purchase consideration is US\$3,263 million (equivalent to approximately RMB21,292 million as at December 31, 2020), including: 1) US\$1,783 million (equivalent to approximately RMB11,636 million as at December 31, 2020) and US\$80 million (equivalent to approximately RMB522 million as at December 31, 2020) paid by cash and restricted cash, respectively; 2) US\$1,298 million (equivalent to approximately RMB8,467 million as at December 31, 2020) payable by cash before June 30, 2021; and 3) the fair value of the contingent consideration with a maximum amount of US\$300 million subject to the achievement of certain conditions. The directors of the Company have estimated fair value of the contingent consideration is [US\$102 million (equivalent to approximately RMB667 million as at December 31, 2020)] based on a [draft] valuation report prepared by an independent valuer. The Company is still in the process of completing the detailed projections and valuations, and the final fair value of contingent consideration could differ from the estimation.

- (ii) the provisional goodwill arising from the Transaction as if the Transaction had taken place as at December 31, 2020.

The acquisition will be accounted for as a business combination using the purchase method of accounting in accordance with *ASC Topic 805, Business Combinations*. The purchase method of accounting requires that the consideration transferred to be allocated to the assets, including separately identifiable assets and liabilities acquired, based on their estimated fair values. In applying purchase method of accounting, the identifiable assets and liabilities of YY Live acquired would be recorded on the pro forma consolidated balance sheet of the Enlarged Group at their fair values as at the date of completion of the Transaction. Any goodwill arising from the transaction represents the excess of the consideration over the fair values of the total identifiable net assets at the date of completion of the Transaction.

The directors of the Company have estimated the fair values of the identifiable assets and liabilities of YY Live as of December 31, 2020, based on a [draft] valuation report prepared by an independent valuer. For the purpose of the pro forma consolidated balance sheet of the Enlarged Group, the provisional purchase price allocation arising from the Transaction is calculated as follows:

| | Notes | RMB |
|---|--------------|----------------|
| [Total identifiable net liabilities of YY Live at book value | a | (767) |
| Fair value adjustments | b | 6,741 |
| Deferred income tax liabilities arising from fair value adjustments | b | <u>(1,011)</u> |
| Total identifiable net assets of YY Live at fair value | b | 4,963 |
| Provisional goodwill on acquisition | b | <u>16,329</u> |
| | | 21,292 |
| Satisfied by: | | |
| Cash and restricted cash | 3(i) | 12,158 |
| Cash consideration payables | 3(i) | 8,467 |
| Contingent consideration | 3(i) | <u>667</u> |
| | | <u>21,292</u> |
|] | | |

Notes:

- a. The amounts are extracted from the audited combined balance sheet of YY Live as at December 31, 2020 as set out in the accountant’s report of YY Live included in Appendix IB to the [REDACTED].
- b. Fair value adjustments related to intangible assets. Deferred income tax liabilities have been recognised for the temporary differences arising from the fair value adjustments. The directors of the Company have estimated the fair values of the

**APPENDIX IIB UNAUDITED PRO FORMA FINANCIAL INFORMATION OF
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identifiable assets and liabilities of YY Live as of December 31, 2020, based on a [draft] valuation report prepared by an independent valuer, and have applied it as the fair value of the identifiable assets and liabilities of YY Live in preparing the Unaudited Pro Forma Financial Information of the Enlarged Group. Since the fair value of identifiable net assets of YY Live at the completion date of the Transaction may substantially be different from the fair values used in the preparation of the Unaudited Pro Forma Financial Information of the Enlarged Group, the final amounts of the identified net assets of YY Live and goodwill to be recognised in connection with the Transaction may be different from the amounts presented above.

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**APPENDIX IIB UNAUDITED PRO FORMA FINANCIAL INFORMATION OF
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[REDACTED]

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**APPENDIX IIB UNAUDITED PRO FORMA FINANCIAL INFORMATION OF
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**APPENDIX IIB UNAUDITED PRO FORMA FINANCIAL INFORMATION OF
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[REDACTED]

SUMMARY OF OUR CONSTITUTION

1 Memorandum of Association

Our Memorandum of Association, as currently in effect, states, inter alia, that the liability of the members of our Company is limited, that the objects for which our Company is established are unrestricted and our Company shall have full power and authority to carry out any object not prohibited by the Companies Act or any other law of the Cayman Islands.

Our Memorandum of Association is available for inspection at the address specified in Appendix V in the section headed "Documents available for inspection".

2 Articles of Association

Our Articles of Association, as currently in effect, include provisions to the following effect:

Shares

Our ordinary shares are divided into Class A ordinary shares and Class B ordinary shares. Holders of Class A ordinary shares and Class B ordinary shares have the same rights except for voting and conversion rights. All of our outstanding ordinary shares are fully paid and non-assessable. Certificates representing the ordinary shares are issued in registered form. Our shareholders who are nonresidents of the Cayman Islands may freely hold and vote their shares.

Our board of directors will have the authority, without shareholder approval, to issue up to a total of 10,000,000 shares of preferred shares in one or more series. Our board of directors may establish the number of shares to be included in each such series and may set the designations, preferences, powers and other rights of the shares of a series of preferred shares.

Changes in Capital

We may by ordinary resolution:

- (a) consolidate and divide all or any of our share capital into Shares of larger amount than our existing Shares;
- (b) by subdivision of our existing Shares or any of them divided the whole or any part of our share capital into Shares of smaller amount than is fixed by our Memorandum of Association or into Shares without nominal or par value; and
- (c) 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.

Dividends

The holders of our ordinary shares are entitled to such dividends as may be declared by our board of directors subject to the Companies Act.

There are no provisions in our Articles governing the time limit after which entitlement to dividend lapses and an indication of the party in whose favor the lapse operates.

Conversion

Each Class B ordinary share is convertible into one Class A ordinary share at any time by the holder thereof. Class A ordinary shares are not convertible into Class B ordinary shares under any circumstances. Upon any transfer of Class B ordinary shares by a holder thereof to any person or entity which is not an affiliate of such holder (as defined in our Articles), such Class B ordinary shares shall be automatically and immediately converted into the equal number of Class A ordinary shares. In addition, if at any time our chairman and chief executive officer, Robin Yanhong Li, and his affiliates collectively own less than 5% of the total number of the issued and outstanding Class B ordinary shares, each issued and outstanding Class B ordinary share shall be automatically and immediately converted into one share of Class A ordinary share, and we shall not issue any Class B ordinary shares thereafter.

Voting Rights

All of our shareholders have the right to receive notice of shareholders' meetings and to attend, speak and vote at such meetings. In respect of matters requiring shareholders' vote, each Class A ordinary share is entitled to one vote, and each Class B ordinary share is entitled to 10 votes. A shareholder may participate at a shareholders' meeting in person, by proxy or by telephone conference or other communications equipment by means of which all the shareholders participating in the meeting can communicate with each other. At any shareholders' meeting, a resolution put to the vote of the meeting shall be decided on a poll conducted by the chairman of the meeting.

A quorum for a shareholders' meeting consists of one or more shareholders holding at least one third of the paid up voting share capital present in person or by proxy or, if a corporation or other non-natural person, by its duly authorized representative. We shall, if required by the Companies Act, hold a general meeting of shareholders as our annual general meeting and shall specify the meeting as such in the notices calling it. Our board of directors may call extraordinary general meetings, and they must on shareholders' requisition convene an extraordinary general meeting. A shareholder requisition is a requisition of shareholders holding at the date of deposit of the requisition not less than a majority of the voting power represented by the issued shares of our company which as at that date carries the right of voting at general meetings of our company. Advance notice of at least five days is required for the convening of our annual general meeting and other shareholders' meetings.

An ordinary resolution to be passed by the shareholders requires the affirmative vote of a simple majority of the votes attaching to the ordinary shares cast in a general meeting, while a special resolution requires the affirmative vote of no less than two-thirds of the votes attaching to the ordinary shares cast in a general meeting. A special resolution is required for matters such as a change of name. Holders of the ordinary shares may effect certain changes by ordinary resolution, including consolidating and dividing all or any of our share capital into shares of larger amount than our existing share capital and canceling any shares.

Transfer of Shares

Subject to the restrictions of our memorandum and articles of association, as applicable, any of our shareholders may transfer any or all of his or her ordinary shares by an instrument of transfer in the usual or common form or any other form approved by our board of directors.

Our board of directors may, in its absolute discretion (except with respect to a transfer from a shareholder to its Affiliates (as defined in our Articles)), decline to register any transfer of shares

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without assigning any reason therefor. If our directors refuse to register a transfer they shall notify the transferee within two months of such refusal. Notwithstanding the foregoing, if a transfer complies with the holder's transfer obligation and restrictions set forth under applicable law and the Articles, our directors shall promptly register such transfer. Further, any director is authorized to confirm in writing addressed to the registered office to authorize a share transfer and to instruct that the register of members be updated accordingly, provided that the transfer complies with the holder's transfer obligations and restrictions set forth under applicable law and our articles of association and such holder is not the director who authorizes the transfer or an entity affiliated with such director. Any director is authorized to execute a share certificate in respect of such shares for and on behalf of our company.

The registration of transfers may be suspended at such time and for such periods as our directors may from time to time determine, provided always that such registration shall not be suspended for more than 45 days in any year.

Liquidation

On a return of capital on winding up or otherwise (other than on conversion, redemption or purchase of shares), assets available for distribution among the holders of ordinary shares may be distributed among the holders of the ordinary shares as determined by the liquidator, subject to sanction of a special resolution of our company. If our assets available for distribution are insufficient to repay all of the paid-up capital, the assets will be distributed so that the losses are borne by our shareholders proportionately 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 such shareholders respectively.

Calls on Shares and Forfeiture of Shares

Our board may from time to time make calls upon shareholders for any amounts unpaid on their Shares in a notice served to such shareholders at least 14 days prior to the specified time or times of payment. Our Shares that have been called upon and remain unpaid are subject to forfeiture.

Redemption of Shares

Subject to the provisions of the Companies Act and our articles of association, we may issue shares on terms that are subject to redemption, at our option or at the option of the holders, on such terms and in such manner as our board of directors may determine.

Repurchase of Shares

Subject to the provisions of the Companies Act and our articles of association, our board of directors may authorize repurchase of our shares in accordance with the manner of purchase specified in our articles of association without seeking shareholder approval.

Variations of Rights of Shares

All or any of the special rights attached to any class of shares may, subject to the provisions of the Companies Act, be varied either with the written consent of the holders of a majority of the issued shares of that class or with the sanction of a special resolution passed at a general meeting of the holders of the shares of that class.

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Limitations on the Right to Own Shares

There are no limitations on the right to own our Shares.

Directors

Our board of directors shall consist of no more than nine persons provided however that our Company may from time to time by ordinary resolution increase or reduce the limits in the number of directors.

A director may vote in respect of any contract or transaction in which he is interested, provided however, that the nature of the interest of any director in any such contract or transaction shall be disclosed by him at or prior to its consideration and any vote on that matter. A general notice that a director is to be regarded as interested in any transaction shall be sufficient disclosure and after such general notice it shall not be necessary to give special notice relating to any particular transaction.

Our directors may determine remuneration to be paid to our directors. No independent quorum is required. Our directors shall be entitled to be paid their reasonable expenses properly incurred by them in going to, attending and returning from meetings of directors or any committee of our directors or general meetings, or otherwise in connection with the business of our Company, or to receive a fixed allowance in respect thereof as may be determined by our directors from time to time. Our directors may by resolution award special remuneration to any director undertaking any special work or services for, or undertaking any special mission on behalf of, our Company other than his ordinary routine work as director.

Our directors may exercise all the powers of our Company to borrow money and to mortgage or charge its undertaking, property and uncalled capital or any part thereof and to issue debentures, debenture stock and other securities whether outright or as security for any of our debts, liabilities, or obligations or those of any third party.

A shareholding qualification for directors may be fixed by our Company in general meeting, but unless and until so fixed no qualification shall be required.

There are no age limitations or retirement requirements in respect of our directors.

SUMMARY OF CAYMAN ISLANDS COMPANY LAW AND TAXATION

1 Introduction

The Companies Act is derived, to a large extent, from the older Companies Acts of England, although there are significant differences between the Companies Act and the current Companies Act of England. Set out below is a summary of certain provisions of the Companies Act, although this does not purport to contain all applicable qualifications and exceptions or to be a complete review of all matters of corporate law and taxation which may differ from equivalent provisions in jurisdictions with which interested parties may be more familiar.

2 Incorporation

Our Company was incorporated in the Cayman Islands as an exempted company with limited liability on January 18, 2000 under the Companies Act. As such, its operations must be conducted mainly outside the Cayman Islands. Our Company is required to file an annual return each year with the Registrar of Companies of the Cayman Islands and pay a fee which is based on the size of its authorized share capital.

3 Share Capital

The Companies Act permits a company to issue ordinary shares, preference shares, redeemable shares or any combination thereof.

The Companies Act provides that where a company issues shares at a premium, whether for cash or otherwise, a sum equal to the aggregate amount of the value of the premia on those shares shall be transferred to an account called the "share premium account". At the option of a company, these provisions may not apply to premia on shares of that company allotted pursuant to any arrangement in consideration of the acquisition or cancelation of shares in any other company and issued at a premium. The Companies Act provides that the share premium account may be applied by a company, subject to the provisions, if any, of its memorandum and articles of association, in such manner as the company may from time to time determine including, but without limitation:

- (a) paying distributions or dividends to members;
- (b) paying up unissued shares of the company to be issued to members as fully paid bonus shares;
- (c) in the redemption and repurchase of shares (subject to the provisions of section 37 of the Companies Act);
- (d) writing-off the preliminary expenses of the company;
- (e) writing-off the expenses of, or the commission paid or discount allowed on, any issue of shares or debentures of the company; and
- (f) providing for the premium payable on redemption or purchase of any shares or debentures of the company.

No distribution or dividend may be paid to members out of the share premium account unless immediately following the date on which the distribution or dividend is proposed to be paid the company will be able to pay its debts as they fall due in the ordinary course of business.

The Companies Act provides that, subject to confirmation by the Grand Court of the Cayman Islands, a company limited by shares or a company limited by guarantee and having a share capital may, if so authorized by its articles of association, by special resolution reduce its share capital in any way.

Subject to the detailed provisions of the Companies Act, a company limited by shares or a company limited by guarantee and having a share capital may, if so authorized by its articles of association, issue shares which are to be redeemed or are liable to be redeemed at the option of the company or a shareholder. In addition, such a company may, if authorized to do so by its articles of association, purchase its own shares, including any redeemable shares. The manner of such a purchase must be authorized either by the articles of association or by an ordinary resolution of the company. The articles of association may provide that the manner of purchase may be determined by the directors of the company. At no time may a company redeem or purchase its shares unless they are fully paid. A company may not redeem or purchase any of its shares if, as a result of the redemption or purchase, there would no longer be any member of the company holding shares. A payment out of capital by a company for the redemption or purchase of its own shares is not lawful unless immediately following the date on which the payment is proposed to be made, the company shall be able to pay its debts as they fall due in the ordinary course of business.

There is no statutory restriction in the Cayman Islands on the provision of financial assistance by a company for the purchase of, or subscription for, its own or its holding company's shares.

Accordingly, a company may provide financial assistance if the directors of the company consider, in discharging their duties of care and to act in good faith, for a proper purpose and in the interests of the company, that such assistance can properly be given. Such assistance should be on an arm's-length basis.

4 Dividends and Distributions

With the exception of section 34 of the Companies Act, there are no statutory provisions relating to the payment of dividends. Based upon English case law which is likely to be persuasive in the Cayman Islands in this area, dividends may be paid only out of profits. In addition, section 34 of the Companies Act permits, subject to a solvency test and the provisions, if any, of the company's memorandum and articles of association, the payment of dividends and distributions out of the share premium account (see paragraph 3 above for details).

5 Shareholders' Suits

The Cayman Islands courts can be expected to follow English case law precedents. The rule in *Foss v. Harbottle* (and the exceptions thereto which permit a minority shareholder to commence a class action against or derivative actions in the name of the company to challenge (a) an act which is *ultra vires* the company or illegal, (b) an act which constitutes a fraud against the minority where the wrongdoers are themselves in control of the company, and (c) an action which requires a resolution with a qualified (or special) majority which has not been obtained) has been applied and followed by the courts in the Cayman Islands.

6 Protection of Minorities

In the case of a company (not being a bank) having a share capital divided into shares, the Grand Court of the Cayman Islands may, on the application of members holding not less than one-fifth of the shares of the company in issue, appoint an inspector to examine into the affairs of the company and to report thereon in such manner as the Grand Court shall direct.

Any shareholder of a company may petition the Grand Court of the Cayman Islands which may make a winding up order if the court is of the opinion that it is just and equitable that the company should be wound up.

Claims against a company by its shareholders must, as a general rule, be based on the general laws of contract or tort applicable in the Cayman Islands or their individual rights as shareholders as established by the company's memorandum and articles of association.

The English common law rule that the majority will not be permitted to commit a fraud on the minority has been applied and followed by the courts of the Cayman Islands.

7 Disposal of Assets

The Companies Act contains no specific restrictions on the powers of directors to dispose of assets of a company. As a matter of general law, in the exercise of those powers, the directors must discharge their duties of care and to act in good faith, for a proper purpose and in the interests of the company.

8 Accounting and Auditing Requirements

The Companies Act requires that a company shall cause to be kept proper books of account with respect to:

- (a) all sums of money received and expended by the company and the matters in respect of which the receipt and expenditure takes place;
- (b) all sales and purchases of goods by the company; and
- (c) the assets and liabilities of the company.

Proper books of account shall not be deemed to be kept if there are not kept such books as are necessary to give a true and fair view of the state of the company's affairs and to explain its transactions.

9 Register of Members

An exempted company may, subject to the provisions of its articles of association, maintain its principal register of members and any branch registers at such locations, whether within or without the Cayman Islands, as its directors may from time to time think fit. There is no requirement under the Companies Act for an exempted company to make any returns of members to the Registrar of Companies of the Cayman Islands. The names and addresses of the members are, accordingly, not a matter of public record and are not available for public inspection.

10 Inspection of Books and Records

Members of a company will have no general right under the Companies Act to inspect or obtain copies of the register of members or corporate records of the company. They will, however, have such rights as may be set out in the company's articles of association.

11 Special Resolutions

The Companies Act provides that a resolution is a special resolution when it has been passed by a majority of at least two-thirds of such members as, being entitled to do so, vote in person 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, except that a company may in its articles of association specify that the required majority shall be a number greater than two-thirds, and may additionally so provide that such majority (being not less than two-thirds) may differ as between matters required to be approved by a special resolution. Written resolutions signed by all the members entitled to vote for the time being of the company may take effect as special resolutions if this is authorized by the articles of association of the company.

12 Subsidiary Owning Shares in Parent

The Companies Act does not prohibit a Cayman Islands company acquiring and holding shares in its parent company provided its objects so permit. The directors of any subsidiary making such acquisition must discharge their duties of care and to act in good faith, for a proper purpose and in the interests of the subsidiary.

13 Mergers and Consolidations

The Companies Act permits mergers and consolidations between Cayman Islands companies and between Cayman Islands companies and non-Cayman Islands companies. For these purposes, (a) "merger" means the merging of two or more constituent companies and the vesting of their undertaking, property and liabilities in one of such companies as the surviving company, and (b) "consolidation" means the combination of two or more constituent companies into a consolidated company and the vesting of the undertaking, property and liabilities of such companies to the consolidated company. In order to effect such a merger or consolidation, the directors of each constituent company must approve a written plan of merger or consolidation, which must then be authorized by (a) a special resolution of each constituent company and (b) such other authorization, if any, as may be specified in such constituent company's articles of association. The written plan of merger or consolidation must be filed with the Registrar of Companies of the Cayman Islands together with a declaration as to the solvency of the consolidated or surviving company, a list of the assets and liabilities of each constituent company and an undertaking that a copy of the certificate of merger or consolidation will be given to the members and creditors of each constituent company and that notification of the merger or consolidation will be published in the Cayman Islands Gazette. Dissenting shareholders have the right to be paid the fair value of their shares (which, if not agreed between the parties, will be determined by the Cayman Islands court) if they follow the required procedures, subject to certain exceptions. Court approval is not required for a merger or consolidation which is effected in compliance with these statutory procedures.

14 Reconstructions

There are statutory provisions which facilitate reconstructions and amalgamations approved by a majority in number representing 75% in value of shareholders or creditors, depending on the circumstances, as are present at a meeting called for such purpose and thereafter sanctioned by the Grand Court of the Cayman Islands. Whilst a dissenting shareholder would have the right to express to the Grand Court his view that the transaction for which approval is sought would not provide the shareholders with a fair value for their shares, the Grand Court is unlikely to disapprove the transaction on that ground alone in the absence of evidence of fraud or bad faith on behalf of management and if the transaction were approved and consummated the dissenting shareholder would have no rights comparable to the appraisal rights (i.e. the right to receive payment in cash for the judicially determined value of his shares) ordinarily available, for example, to dissenting shareholders of United States corporations.

15 Take-overs

Where an offer is made by a company for the shares of another company and, within four months of the offer, the holders of not less than 90% of the shares which are the subject of the offer accept, the offeror may at any time within two months after the expiration of the said four months, by notice require the dissenting shareholders to transfer their shares on the terms of the offer. A dissenting shareholder may apply to the Grand Court of the Cayman Islands within one month of the notice objecting to the transfer. The burden is on the dissenting shareholder to show that the Grand Court should exercise its discretion, which it will be unlikely to do unless there is evidence of fraud or bad faith or collusion as between the offeror and the holders of the shares who have accepted the offer as a means of unfairly forcing out minority shareholders.

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16 Indemnification

Cayman Islands law does not limit the extent to which a company's articles of association may provide for indemnification of officers and directors, except to the extent any such provision may be held by the Cayman Islands courts to be contrary to public policy (e.g. for purporting to provide indemnification against the consequences of committing a crime).

17 Liquidation

A company may be placed in liquidation compulsorily by an order of the court, or voluntarily (a) by a special resolution of its members if the company is solvent, or (b) by an ordinary resolution of its members if the company is insolvent. The liquidator's duties are to collect the assets of the company (including the amount (if any) due from the contributories (shareholders)), settle the list of creditors and discharge the company's liability to them, rateably if insufficient assets exist to discharge the liabilities in full, and to settle the list of contributories and divide the surplus assets (if any) amongst them in accordance with the rights attaching to the shares.

18 Stamp Duty on Transfers

No stamp duty is payable in the Cayman Islands on transfers of shares of Cayman Islands companies except those which hold interests in land in the Cayman Islands.

19 Taxation

Pursuant to section 6 of the Tax Concessions Act (2018 Revision) of the Cayman Islands, our Company may obtain an undertaking from the Financial Secretary of the Cayman Islands:

- (a) that no law which is enacted in the Cayman Islands imposing any tax to be levied on profits, income, gains or appreciations shall apply to our Company or its operations; and
- (b) in addition, that no tax to be levied on profits, income, gains or appreciations or which is in the nature of estate duty or inheritance tax shall be payable:
 - (i) on or in respect of the shares, debentures or other obligations of our Company; or
 - (ii) by way of the withholding in whole or in part of any relevant payment as defined in section 6(3) of the Tax Concessions Act (2018 Revision).

The Cayman Islands currently levy no taxes on individuals or corporations based upon profits, income, gains or appreciations and there is no taxation in the nature of inheritance tax or estate duty. There are no other taxes likely to be material to our Company levied by the Government of the Cayman Islands save certain stamp duties which may be applicable, from time to time, on certain instruments executed in or brought within the jurisdiction of the Cayman Islands. The Cayman Islands are not party to any double tax treaties that are applicable to any payments made by or to our Company.

20 Exchange Control

There are no exchange control regulations or currency restrictions in the Cayman Islands.

21 General

Maples and Calder (Hong Kong) LLP, our Company's legal advisers on Cayman Islands law, have sent to our Company a letter of advice summarizing aspects of Cayman Islands company law. This

letter, together with a copy of the Companies Act, is available for inspection as referred to in the section headed “Documents available for inspection” in Appendix V. Any person wishing to have a detailed summary of Cayman Islands company law or advice on the differences between it and the laws of any jurisdiction with which he/she is more familiar is recommended to seek independent legal advice.

Further Information About Us

Our Incorporation

Our Company was incorporated in the Cayman Islands under the Cayman Companies Act as an exempted company with limited liability on January 18, 2000. We have registered with the Registrar of Companies in Hong Kong as a non-Hong Kong company under Part 16 of the Companies Ordinance with an address at Suite 3101, Everbright Center, 108 Gloucester Road, Wanchai, Hong Kong. Shiu Wing Yan has been appointed as our authorized representative for the acceptance of service of process and notices in Hong Kong.

As we were incorporated in the Cayman Islands, our corporate structure and Memorandum and Articles of Association are subject to the relevant laws and regulations of the Cayman Islands. A summary of the relevant laws and regulations of the Cayman Islands and of the Memorandum and Articles of Association is set out in “Summary of our Constitution and Cayman Companies Act” in Appendix III to this document.

Changes in Our Share Capital

As at December 31, 2020, after having accounted for the Share Subdivision, we had an authorized share capital of US\$43,520 divided into 66,000,000,000 Class A ordinary shares of a nominal or par value of US\$ 0.000000625 each, 2,832,000,000 Class B ordinary shares of a nominal or par value of US\$ 0.000000625 each, and 800,000,000 preferred shares of a nominal or par value of US\$ 0.000000625 each, and our issued share capital was 2,107,228,720 Class A ordinary shares and 571,900,320 Class B ordinary shares.

APPENDIX IV

STATUTORY AND GENERAL INFORMATION

The following tables set out the changes in the share capital, after having accounted for the Share Subdivision, of our Company during the periods presented in this document:

| | Fiscal year ended December 31, 2018 | | |
|---|-------------------------------------|------------------------|----------------------|
| | Class A ordinary share | Class B ordinary share | Shareholders' Equity |
| Balances as at January 1, 2018 | 2,209,198,240 | 576,100,320 | 1,741 |
| Issuance of Shares | 26,070,320 | — | 16 |
| Repurchase and/or retirement of Shares | (16,573,200) | — | (10) |
| Balances as at December 31, 2018 | <u>2,218,695,360</u> | <u>576,100,320</u> | <u>1,747</u> |
| | Fiscal year ended December 31, 2019 | | |
| | Class A ordinary share | Class B ordinary share | Shareholders' Equity |
| Balances as at January 1, 2019 | 2,218,695,360 | 576,100,320 | 1,747 |
| Issuance of Shares | 24,997,040 | — | 16 |
| Repurchase and/or retirement of Shares | (53,162,720) | — | (33) |
| Balances as at December 31, 2019 | <u>2,190,529,680</u> | <u>576,100,320</u> | <u>1,730</u> |
| | Fiscal year ended December 31, 2020 | | |
| | Class A ordinary share | Class B ordinary share | Shareholders' Equity |
| Balances as at January 1, 2020 | 2,190,529,680 | 576,100,320 | 1,729 |
| Issuance of Shares | 38,595,040 | — | 24 |
| Class A ordinary shares converted from Class B ordinary shares in relation to share-based award | 4,200,000 | (4,200,000) | — |
| Repurchase and/or retirement of Shares | (126,096,000) | — | (79) |
| Balances as at December 31, 2020 | <u>2,107,228,720</u> | <u>571,900,320</u> | <u>1,674</u> |

On March 1, 2021, our shareholders approved by ordinary resolution a subdivision on our share capital such that our authorized share capital became US\$43,520 divided into 66,000,000,000 class A ordinary shares with a par value of US\$0.000000625 each, 2,832,000,000 class B ordinary shares with a par value of US\$0.000000625 each and 800,000,000 preferred shares with a par value of US\$0.000000625 each.

Changes in the Share Capital of Our Significant Subsidiaries

The following alterations in the share capital of our Significant Subsidiaries have taken place within the two years immediately preceding the date of this document:

Baidu Holdings Limited

On August 15, 2019, 10 ordinary shares of a par value of US\$1.00 each in Baidu Holdings Limited were issued to the Company.

Baidu (Hong Kong) Limited

On August 8, 2019, the share capital of Baidu (Hong Kong) Limited was increased from US\$1 to US\$14,164,816 by allotment of 10 ordinary shares to Baidu Holdings Limited.

Baidu Netcom

On July 11, 2019, the registered capital of Baidu Netcom was increased from RMB6,421.28 million to RMB13,421.28 million.

Further Information About Our Business

Summary of Material Contracts

The following contracts (not being contracts entered into in the ordinary course of business) were entered into by our Company or its subsidiaries within the two years preceding the date of this document and are or may be material:

- (1) the amended and restated loan agreement dated July 10, 2019, entered into between Baidu Online Network Technology (Beijing) Co., Ltd. (百度在線網絡技術(北京)有限公司, “**Baidu Online**”) and Robin Yanhong Li (李彥宏) pursuant to which Baidu Online agreed to provide a loan in an aggregate amount of RMB13,354,173,600 to Robin Yanhong Li (李彥宏) solely for the latter to fund the capitalization of Beijing Baidu Netcom Science Technology Co., Ltd. (北京百度網訊科技有限公司, “**Baidu Netcom**”);
- (2) the amended and restated exclusive equity purchase and transfer option agreement dated July 10, 2019, entered into among our Company, Baidu Netcom, Baidu Online and Robin Yanhong Li (李彥宏), pursuant to which Robin Yanhong Li (李彥宏) has irrevocably granted our Company, an option to purchase, or to cause any one or more designated persons to purchase, to the extent permitted under PRC law, all or part of the equity interests in Baidu Netcom for the cost of the initial contributions to the registered capital or the minimum amount of consideration permitted by applicable PRC law;
- (3) the amended and restated equity pledge agreement dated July 10, 2019, entered into between Baidu Online and Robin Yanhong Li (李彥宏), pursuant to which Robin Yanhong Li (李彥宏) has pledged all of his equity interests in Baidu Netcom to Baidu Online to guarantee his obligations under the amended and restated loan agreement dated July 10, 2019 and Baidu Netcom’s performance of its obligations under the exclusive technology consulting and service agreement;
- (4) the termination agreement of current control contracts dated August 20, 2019, entered into among our Company, Baidu Online, Baidu Netcom, Robin Yanhong Li (李彥宏) and Hailong Xiang (向海龍), pursuant to which Robin Yanhong Li (李彥宏) and Hailong Xiang (向海龍) acknowledged the termination of all control documents previously entered into with Baidu Online and Baidu Netcom;
- (5) the proxy agreement dated August 20, 2019, entered into between Shanshan Cui (崔珊珊) and our Company, pursuant to which Shanshan Cui (崔珊珊) agreed to entrust all the rights to exercise her voting power and any other rights as shareholders of Baidu Netcom to the person(s) designated by our Company;
- (6) the operating agreement dated August 20, 2019, entered into among Baidu Online, Baidu Netcom, Robin Yanhong Li (李彥宏) and Shanshan Cui (崔珊珊), pursuant to which Baidu Online has the rights to provide guidance and instructions on Baidu Netcom’s daily operations and financial affairs;
- (7) the loan agreement dated August 20, 2019, entered into between Baidu Online and Shanshan Cui (崔珊珊) pursuant to which Baidu Online agreed to provide a loan in an aggregate amount of RMB67,106,400 to Shanshan Cui (崔珊珊) solely for the latter to fund the capitalization of Baidu Netcom;
- (8) the exclusive equity purchase and transfer option agreement dated August 20, 2019, entered into among our Company, Baidu Online, Shanshan Cui (崔珊珊) and Baidu Netcom, pursuant to which Shanshan Cui (崔珊珊) has irrevocably granted our Company, an option to purchase, or to cause any one or more designated persons to purchase, to the extent permitted under PRC law, all or

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- part of the equity interests in Baidu Netcom for the cost of the initial contributions to the registered capital or the minimum amount of consideration permitted by applicable PRC law;
- (9) the equity pledge agreement dated August 20, 2019, entered into between Baidu Online and Shanshan Cui (崔珊珊), pursuant to which Shanshan Cui (崔珊珊) has pledged all of her equity interests in Baidu Netcom to Baidu Online to guarantee her obligations under the loan agreement dated August 20, 2019 and Baidu Netcom’s performance of its obligations under the exclusive technology consulting and service agreement;
- (10) the termination agreement dated October 30, 2019, entered into among Baidu Online, Beijing Perusal Technology Co., Ltd. (北京鼎鹿中原科技有限公司, “**Beijing Perusal**”), Zhixiang Liang (梁志祥), Lu Wang (王路) and our Company, pursuant to which Zhixiang Liang (梁志祥), Lu Wang (王路) acknowledged the termination of all control documents previously entered into with Baidu Online, Beijing Perusal and our Company;
- (11) the operating agreement dated October 30, 2019, entered into among Baidu Online, Beijing Perusal, Zhixiang Liang (梁志祥) and Shanshan Cui (崔珊珊), pursuant to which Baidu Online has the rights to provide guidance and instructions on Beijing Perusal’s daily operations and financial affairs and to appoint senior executives of Beijing Perusal, and Zhixiang Liang (梁志祥) and Shanshan Cui (崔珊珊) agreed to appoint candidates recommended by Baidu Online as their representatives on Beijing Perusal’s board of directors;
- (12) the loan agreement dated October 30, 2019, entered into between Baidu Online and Shanshan Cui (崔珊珊), pursuant to which Baidu Online agreed to provide a loan in an aggregate amount of RMB1,598,440,000 to Shanshan Cui (崔珊珊), solely for the latter to use towards the investment in Beijing Perusal;
- (13) the proxy agreement dated October 30, 2019, entered into between our Company and Shanshan Cui (崔珊珊), pursuant to which Shanshan Cui (崔珊珊) agreed to entrust all the rights to exercise her voting power and any other rights as shareholders of Beijing Perusal to the person(s) designated by our Company;
- (14) the exclusive equity purchase and transfer option agreement dated October 30, 2019, entered into among our Company, Baidu Online, Shanshan Cui (崔珊珊) and Beijing Perusal, pursuant to which Shanshan Cui (崔珊珊) has irrevocably granted our Company, an option to purchase, or to cause any one or more designated persons to purchase, to the extent permitted under PRC law, all or part of the equity interests in Beijing Perusal for the cost of the initial contributions to the registered capital or the minimum amount of consideration permitted by applicable PRC law;
- (15) the equity pledge agreement dated October 30, 2019, entered into between Baidu Online and Shanshan Cui (崔珊珊), pursuant to which Shanshan Cui (崔珊珊) has pledged all of her equity interests in Beijing Perusal to Baidu Online to guarantee her obligations under the loan agreement dated October 30, 2019 and Beijing Perusal’s performance of its obligations under the exclusive technology consulting and service agreement; and
- (16) the [REDACTED].

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Summary of the Contractual Arrangements

As described in “History and Corporate Structure—Contractual Arrangements”, our Company or its Substantial Subsidiaries entered into the following contracts in relation to the contractual arrangements that are material to our Group:

Contractual Arrangements with Baidu Netcom

- (a) the exclusive technology consulting and services agreement dated March 22, 2005 and its supplemental agreement dated April 22, 2010 entered into between Baidu Online and Beijing Baidu Netcom, pursuant to which Baidu Online has the exclusive right to provide to Baidu Netcom technology consulting and services in return for service fees;
- (b) the software license agreement dated March 22, 2005 and its supplemental agreements dated March 11, 2010, April 22, 2010, January 30, 2011 and August 15, 2013 entered between Baidu Online and Baidu Netcom, pursuant to which Baidu Online has granted to Baidu Netcom the right to use a software license only in its own business operations in return for software license fees;
- (c) the web layout copyright license agreement dated March 1, 2004 and its supplemental agreements dated August 9, 2004, March 1, 2010, January 30, 2011 and August 15, 2013, entered into between Baidu Online and Baidu Netcom, pursuant to which Baidu Online has granted to Baidu Netcom the right to use a web layout copyright license only in its own business operations in return for license fees;
- (d) the proxy agreement dated March 31, 2018, entered into between Robin Yanhong Li (李彦宏) and our Company, pursuant to which Robin Yanhong Li (李彦宏) agreed to entrust all the rights to exercise his voting power and any other rights as shareholders of Baidu Netcom to the person(s) designated by our Company;
- (e) the amended and restated loan agreement dated July 10, 2019, entered into between Baidu Online and Robin Yanhong Li (李彦宏) pursuant to which Baidu Online agreed to provide a loan in an aggregate amount of RMB13,354,173,600 to Robin Yanhong Li (李彦宏) solely for the latter to fund the capitalization of Baidu Netcom;
- (f) the amended and restated equity pledge agreement dated July 10, 2019, entered into between Baidu Online and Robin Yanhong Li (李彦宏), pursuant to which Robin Yanhong Li (李彦宏) has pledged all of his equity interests in Baidu Netcom to Baidu Online to guarantee his obligations under the amended and restated loan agreement dated July 10, 2019 and Baidu Netcom’s performance of its obligations under the exclusive technology consulting and service agreement;
- (g) the amended and restated exclusive equity purchase and transfer option agreement dated July 10, 2019, entered into among our Company, Baidu Netcom, Baidu Online and Robin Yanhong Li (李彦宏), pursuant to which Robin Yanhong Li (李彦宏) has irrevocably granted our Company, an option to purchase, or to cause any one or more designated persons to purchase, to the extent permitted under PRC law, all or part of the equity interests in Baidu Netcom for the cost of the initial contributions to the registered capital or the minimum amount of consideration permitted by applicable PRC law;
- (h) the proxy agreement dated August 20, 2019, entered into between Shanshan Cui (崔珊珊) and our Company, pursuant to which Shanshan Cui (崔珊珊) agreed to entrust all the rights to exercise her voting power and any other rights as shareholders of Baidu Netcom to the person(s) designated by our Company;
- (i) the loan agreement dated August 20, 2019, entered into between Baidu Online and Shanshan Cui (崔珊珊) pursuant to which Baidu Online agreed to provide a loan in an aggregate amount of

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RMB67,106,400 to Shanshan Cui (崔珊珊) solely for the latter to fund the capitalization of Baidu Netcom;

- (j) the equity pledge agreement dated August 20, 2019, entered into between Baidu Online and Shanshan Cui (崔珊珊), pursuant to which Shanshan Cui (崔珊珊) has pledged all of her equity interests in Baidu Netcom to Baidu Online to guarantee her obligations under the loan agreement dated August 20, 2019 and Baidu Netcom’s performance of its obligations under the exclusive technology consulting and service agreement;
- (k) the exclusive equity purchase and transfer option agreement dated August 20, 2019, entered into among our Company, Baidu Online, Shanshan Cui (崔珊珊) and Baidu Netcom, pursuant to which Shanshan Cui (崔珊珊) has irrevocably granted our Company, an option to purchase, or to cause any one or more designated persons to purchase, to the extent permitted under PRC law, all or part of the equity interests in Baidu Netcom for the cost of the initial contributions to the registered capital or the minimum amount of consideration permitted by applicable PRC law;
- (l) the operating agreement dated August 20, 2019, entered into among Baidu Online, Baidu Netcom, Robin Yanhong Li (李彦宏) and Shanshan Cui (崔珊珊), pursuant to which Baidu Online has the rights to provide guidance and instructions on Baidu Netcom’s daily operations and financial affairs;
- (m) the irrevocable power of attorney dated August 20, 2019, issued by Robin Yanhong Li (李彦宏), pursuant to which Robin Yanhong Li (李彦宏), as an individual shareholder of Baidu Netcom, has appointed Shanshan Cui (崔珊珊) as designated by our Company as his attorney-in-fact to vote on his behalf on all matters requiring shareholder approval; and
- (n) the irrevocable power of attorney dated August 20, 2019, issued by Shanshan Cui (崔珊珊), pursuant to which Shanshan Cui (崔珊珊), as an individual shareholder of Baidu Netcom, has appointed Shanshan Cui (崔珊珊) as designated by our Company as her attorney-in-fact to vote on her behalf on all matters requiring shareholder approval.

Contractual Arrangements with Beijing Perusal

- (a) the exclusive technology consulting and services agreement dated June 23, 2006 and its supplemental agreement dated April 22, 2010, entered into between Baidu Online and Beijing Perusal, pursuant to which Baidu Online has the exclusive right to provide to Beijing Perusal technology consulting and services in return for service fees;
- (b) the web layout copyright license agreement dated June 23, 2006 and its supplemental agreement dated August 15, 2013, entered into between Baidu Online and Beijing Perusal, pursuant to which Baidu Online has granted to Beijing Perusal the right to use a web layout copyright license only in its own business operations in return for license fees;
- (c) the amended and restated equity pledge agreement dated June 20, 2016, entered into between Baidu Online and Zhixiang Liang (梁志祥), pursuant to which Zhixiang Liang (梁志祥) has pledged all of his equity interests in Beijing Perusal to Baidu Online to guarantee his obligations under the amended and restated loan agreement and Beijing Perusal’s performance of its obligations under the exclusive technology consulting and service agreement;
- (d) the loan agreement dated March 31, 2018, entered into between Baidu Online and Zhixiang Liang (梁志祥), pursuant to which Baidu Online agreed to provide a loan to Zhixiang Liang (梁志祥), in an aggregate amount of RMB1,598,440,000, solely for the use towards the investment in Beijing Perusal;

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- (e) the proxy agreement dated March 31, 2018, entered into between our Company and Zhixiang Liang (梁志祥), pursuant to which Zhixiang Liang (梁志祥) agreed to entrust all the rights to exercise his voting power and any other rights as a shareholder of Beijing Perusal to the person(s) designated by our Company;
- (f) the irrevocable power of attorney dated October 30, 2019, issued by Zhixiang Liang (梁志祥), pursuant to which Zhixiang Liang (梁志祥), as an individual shareholder of Beijing Perusal, has appointed Shanshan Cui (崔珊珊) as designated by our Company as his attorney-in-fact to vote on his behalf on all matters requiring shareholder approval;
- (g) the exclusive equity purchase and transfer option agreement dated March 31, 2018, entered into among our Company, Baidu Online, Zhixiang Liang (梁志祥) and Beijing Perusal, pursuant to which Zhixiang Liang (梁志祥) has irrevocably granted our Company, an option to purchase, or to cause any one or more designated persons to purchase, to the extent permitted under PRC law, all or part of the equity interests in Beijing Perusal for the cost of the initial contributions to the registered capital or the minimum amount of consideration permitted by applicable PRC law;
- (h) the loan agreement dated October 30, 2019, entered into between Baidu Online and Shanshan Cui (崔珊珊), pursuant to which Baidu Online agreed to provide a loan in an aggregate amount of RMB1,598,440,000 to Shanshan Cui (崔珊珊), solely for the latter to use towards the investment in Beijing Perusal;
- (i) the equity pledge agreement dated October 30, 2019, entered into between Baidu Online and Shanshan Cui (崔珊珊), pursuant to which Shanshan Cui (崔珊珊) has pledged all of her equity interests in Beijing Perusal to Baidu Online to guarantee her obligations under the loan agreement dated October 30, 2019 and Beijing Perusal’s performance of its obligations under the exclusive technology consulting and service agreement.
- (j) the proxy agreement dated October 30, 2019, entered into between our Company and Shanshan Cui (崔珊珊), pursuant to which Shanshan Cui (崔珊珊) agreed to entrust all the rights to exercise her voting power and any other rights as shareholders of Beijing Perusal to the person(s) designated by our Company;
- (k) the irrevocable power of attorney dated October 30, 2019, issued by Shanshan Cui (崔珊珊), pursuant to which Shanshan Cui (崔珊珊), as an individual shareholder of Beijing Perusal, has appointed Shanshan Cui (崔珊珊) as designated by our Company as her attorney-in-fact to vote on her behalf on all matters requiring shareholder approval;
- (l) the exclusive equity purchase and transfer option agreement dated October 30, 2019, entered into among our Company, Baidu Online, Shanshan Cui (崔珊珊) and Beijing Perusal, pursuant to which Shanshan Cui (崔珊珊) has irrevocably granted our Company, an option to purchase, or to cause any one or more designated persons to purchase, to the extent permitted under PRC law, all or part of the equity interests in Beijing Perusal for the cost of the initial contributions to the registered capital or the minimum amount of consideration permitted by applicable PRC law; and
- (m) the operating agreement dated October 30, 2019, entered into among Baidu Online, Beijing Perusal, Zhixiang Liang (梁志祥) and Shanshan Cui (崔珊珊), pursuant to which Baidu Online has the rights to provide guidance and instructions on Beijing Perusal’s daily operations and financial affairs and to appoint senior executives of Beijing Perusal, and Zhixiang Liang (梁志祥) and Shanshan Cui (崔珊珊) agreed to appoint candidates recommended by Baidu Online as their representatives on Beijing Perusal’s board of directors;

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Contractual Arrangements with Beijing iQIYI

- (a) the business cooperation agreement dated December 1, 2011, entered into between Beijing QIYI Century and Beijing iQIYI, pursuant to which Beijing iQIYI agrees to provide Beijing QIYI Century with services, including internet information services, online advertising and other services reasonably necessary within the scope of Beijing QIYI Century’s business;
- (b) the exclusive technology consulting and services agreement dated December 1, 2011, entered into between Beijing QIYI Century and Beijing iQIYI, pursuant to which Beijing QIYI Century has the exclusive right to provide to Beijing iQIYI specified technology consulting and services in return for service fees;
- (c) the trademark license agreement dated December 1, 2011, entered into between Beijing QIYI Century and Beijing iQIYI, pursuant to which Beijing QIYI Century has granted to Beijing iQIYI the right to use its trademarks only in its own business operations in return for license fees;
- (d) the software usage license agreement dated December 1, 2011, entered into between Beijing QIYI Century and Beijing iQIYI, pursuant to which Beijing QIYI Century has granted to Beijing iQIYI the right to use its software only in its own business operations in return for license fees;
- (e) the amended and restated loan agreement dated January 30, 2013, entered into between Beijing QIYI Century and Xiaohua Geng (耿曉華), pursuant to which Beijing QIYI Century agreed to provide loans to Xiaohua Geng (耿曉華), in an aggregate amount of RMB27 million, solely for the latter to use towards the investment in Beijing iQIYI;
- (f) the amended and restated shareholder voting rights trust agreement dated January 30, 2013, entered into between Beijing QIYI Century and Xiaohua Geng (耿曉華), pursuant to which Xiaohua Geng (耿曉華) agreed to entrust all the rights to exercise his voting power and any other rights as shareholders of Beijing iQIYI to the person(s) designated by Beijing QIYI Century;
- (g) the amended and restated business operation agreement dated January 30, 2013, entered into among Beijing QIYI Century, Beijing iQIYI and Xiaohua Geng (耿曉華), pursuant to which Beijing QIYI Century agrees to provide Beijing iQIYI with performance guarantees with respect to any contracts, agreements and transactions Beijing iQIYI entered into in connection with its business;
- (h) the commitment letter dated January 30, 2013, issued by iQIYI and Beijing QIYI Century, pursuant to which iQIYI and Beijing QIYI Century undertook to provide financial support to Beijing iQIYI for any financial loss that might affect its business operation occurred as permitted by relevant laws;
- (i) the amended and restated equity pledge agreement dated January 30, 2013, entered into between Beijing QIYI Century and Xiaohua Geng (耿曉華), pursuant to which Xiaohua Geng (耿曉華) has pledged all of his equity interests in Beijing iQIYI to Beijing QIYI Century to guarantee his obligations under the amended and restated loan agreement and Beijing iQIYI’s performance of its obligations under the amended and restated exclusive technology consulting and services agreement;
- (j) the amended and restated exclusive purchase option agreement dated January 30, 2013, entered into among iQIYI, Beijing QIYI Century, Beijing iQIYI, and Xiaohua Geng (耿曉華), pursuant to which Xiaohua Geng (耿曉華) has irrevocably granted iQIYI or its designee, an exclusive option to purchase at its discretion, to the extent permitted under PRC law, all or part of the equity interests in Beijing iQIYI for the cost of the initial contributions to the registered capital or the minimum amount of consideration permitted by applicable PRC law;

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- (k) the irrevocable power of attorney dated January 30, 2013, issued by Beijing QIYI Century, pursuant to which iQIYI may exercise all shareholder rights during the term of the amended and restated shareholder voting rights trust agreement and may transfer such rights to a designated third party without written notice to Beijing QIYI Century; and
- (l) the spousal consent letter dated September 26, 2016, issued by the spouse of Xiaohua Geng (耿曉華), pursuant to which the spouse of Xiaohua Geng (耿曉華) committed not to impose any adverse assertions upon the validity of such contractual arrangements based on the existence or termination of the marital relationship with the relevant shareholder, or exert any impediment or adverse influence over the relevant shareholder’s performance of any contractual arrangements or claim rights on Beijing iQIYI.

For further details of the above, please see copies of the contractual arrangements, which are published on our website (<http://ir.baidu.com/>) pursuant to the Hong Kong Stock Exchange’s Guidance Letter HKEX-GL94-18 and Listing Decision HKEX-LD43-3.

Our Intellectual Property Rights

We rely on a combination of patent, trademark, copyright and trade secret protection laws in China and other jurisdictions, as well as confidentiality procedures and contractual provisions, to protect our intellectual property and our brand. As of December 31, 2020, we have over 7,800 issued patents in China covering invention, utility model and design, and intend to apply for more patents to protect our core technologies and intellectual property. We also enter into confidentiality, non-compete and invention assignment agreements with our employees and consultants, and nondisclosure agreements with selected third parties. “百度,” our company’s name “Baidu” in Chinese, has been recognized as a well-known trademark in China by the Trademark Office of National Intellectual Property Administration under the State Administration for Market Regulation.

In addition to owning “百度,” and the related logos, we have applied for registration of various other trademarks. We also have registered certain trademarks in the United States, Australia, Brazil, Canada, Hong Kong, India, Indonesia, Japan, Malaysia, Mexico, New Zealand, Russia, Singapore, South Africa, South Korea, Thailand, the European Union and several other jurisdictions. In addition, we have registered our domain name *baidu.com* and certain other domain names with authorized registrars of ICANN (Internet Corporation for Assigned Names and Numbers). We have also successfully become designated Registry Operator for *.baidu* top-level domain names by ICANN.

Further Information About Directors and Executive Officers

Disclosure of Interests

See “Major Shareholders” for disclosure of interests of directors and executive officers.

Directors’ Service Contracts

We have entered into employment agreements with each of our directors who is also an officer. See “Directors and Senior Management—Compensation—Employment Agreements and Indemnification Agreements.”

Directors’ Remuneration

See “Directors and Senior Management—Compensation” for a discussion of Directors’ remuneration.

Disclosures relating to Directors and Experts

Save as may be disclosed in “Directors and senior management” this document:

- None of our directors nor any of the persons listed in “—Other Information—Qualification of Experts” below is materially interested in the promotion of, or in any assets which have been, within the two years immediately preceding the issue of this document, acquired or disposed of by or leased to our subsidiaries and our consolidated affiliated entities, or are proposed to be acquired or disposed of by or leased to our subsidiaries and our consolidated affiliated entities.
- None of our directors nor any of the persons listed in “—Other Information—Qualification of Experts” below is materially interested in any contract or arrangement with us subsisting at the date of this document which is unusual in its nature or conditions or which is significant in relation to our business as a whole.
- None of the persons listed in “—Other Information—Qualification of Experts” below has any shareholding in us or any of our Significant Subsidiaries or has the right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in us or any of our Significant Subsidiaries.

Share Incentive Plans of the Company

See “Directors and Senior Management—Compensation” for details about our Share Incentive Plans.

Share Incentive Plans of iQIYI

One of our Significant Subsidiaries, iQIYI, adopted two employee share incentive plans, one adopted on October 18, 2010 and amended and restated on November 3, 2014, August 6, 2016 and September 15, 2020 (the “**2010 iQIYI Plan**”), and the other adopted on November 30, 2017 and amended on December 7, 2017 (the “**2017 iQIYI Plan**”).

The 2010 iQIYI Plan

The purpose of the 2010 iQIYI Plan is to grant share based compensation awards either through a proprietary interest in iQIYI’s long-term success, or compensation based on fulfilling certain performance goals to employees, officers, directors and consultants to incentivize their performance and promote the success of iQIYI’s business. The maximum aggregate number of number of shares which may be issued pursuant to all awards granted under the 2010 iQIYI Plan is 589,729,714 shares. As of February 28, 2021, options to purchase a total of 413,376,684 ordinary shares were outstanding under the 2010 iQIYI Plan.

We summarize the key terms of the 2010 iQIYI Plan below:

- Types of Awards.** The 2010 iQIYI Plan permits the awards of options, share appreciation rights, share grants and restricted share units.
- Plan Administration.** A committee consisting of at least two individuals determined by iQIYI’s board acts as the plan administrator. The plan administrator will determine the participants who are to receive awards, the number of awards to be granted, and the terms and conditions of each award grant. The plan administrator can amend outstanding awards and interpret the terms of the 2010 iQIYI Plan and any award agreement.
- Award Agreement.** Options to purchase ordinary shares granted under the 2010 iQIYI Plan are evidenced by an award agreement that sets forth the terms and conditions for each grant.

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- (d) **Exercise Price.** The exercise price of an option or a share appreciation right will be determined by the plan administrator, but shall not be less than the fair market value on the grant date of the respective option or share appreciation right. In certain circumstances, such as a recapitalization, a spin-off, reorganization, merger, separation and split-up, the plan administrator may adjust the exercise price of outstanding options and share appreciation rights.
- (e) **Eligibility.** iQIYI may grant awards to its employees, directors or consultants or employees, directors or consultants or its affiliates.
- (f) **Term of the Awards.** The term of each option or share appreciation right granted under the 2010 iQIYI Plan shall not exceed ten years from date of the grant, unless otherwise determined by the board of directors of iQIYI.
- (g) **Vesting Schedule.** In general, the plan administrator determines the vesting schedule, which is set forth in the award agreement.
- (h) **Acceleration of Awards upon Change in Control.** The plan administrator may determine, at the time of grant or thereafter, that an award shall become vested and exercisable, in full or in part, in the event that a change in control of iQIYI occurs.
- (i) **Transfer Restrictions.** Awards may not be transferred in any manner by the recipient other than by will or the laws of descent and distribution, except as otherwise provided by the plan administrator.
- (j) **Termination.** The plan shall terminate on October 17, 2030 provided that iQIYI's board may terminate the plan at any time and for any reason.

The 2017 iQIYI Plan

The purpose of the 2017 iQIYI Plan is to promote the success and enhance the value of iQIYI, by linking the personal interests of the members of iQIYI's board, employees, consultants and other individuals to those of iQIYI's shareholders and, by providing an incentive for outstanding performance, to generate superior returns for iQIYI's shareholders. The maximum aggregate number of number of shares which may be issued pursuant to all awards granted under the 2017 iQIYI Plan is 720,000 ordinary shares, all of which have been granted. As of February 28, 2021, 143,125 restricted share units were outstanding under the 2017 iQIYI Plan.

We summarize the key terms of the 2017 iQIYI Plan below:

- (a) **Types of Awards.** The 2017 iQIYI Plan permits the awards of options, restricted shares and restricted share units.
- (b) **Plan Administration.** A committee of one or more members of iQIYI's board acts as the plan administrator. The plan administrator will determine the participants who are to receive awards, the type or types of awards to be granted, the number of awards to be granted, and the terms and conditions of each award grant. The plan administrator can amend outstanding awards and interpret the terms of the 2017 iQIYI Plan and any award agreement.
- (c) **Award Agreement.** Awards granted under the 2017 iQIYI Plan are evidenced by an award agreement that sets forth the terms and conditions for each grant.
- (d) **Exercise Price.** The exercise price of an option or a share appreciation right will be determined by the plan administrator, but shall not be less than the fair market value on the grant date of the respective option or share appreciation right. In certain circumstances, such as a recapitalization, a spin-off, reorganization, merger, separation and split-up, the plan administrator may adjust the exercise price of outstanding options and share appreciation rights.

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- (e) **Eligibility.** iQIYI may grant awards to its employees, consultants, and all members of the board, and other individuals.
- (f) **Term of the Awards.** The term of each option or share appreciation right granted under the 2017 iQIYI Plan shall not exceed ten years from date of the grant.
- (g) **Vesting Schedule.** In general, the plan administrator determines the vesting schedule, which is set forth in the relevant award agreement.
- (h) **Transfer Restrictions.** Awards may not be transferred in any manner by the recipient other than by will or the laws of descent and distribution, except as otherwise provided by the plan administrator.
- (i) **Termination.** The plan shall terminate on November 29, 2027, provided that iQIYI’s board may terminate the plan at any time and for any reason.

The following table summarizes, as of February 28, 2021, the outstanding options and restricted share units that iQIYI granted to iQIYI’s directors and executive officers:

| | Class A ordinary shares underlying options and restricted share units awarded | Exercise price (US\$/Share) | Date of grant | Date of expiration |
|---------------------|--|--------------------------------|---|---|
| Yu Gong | 146,000,116 | 0.25 to 0.51 | Various dates from 2010/10/18 to 2020/10/16 | Various dates from 2024/12/15 to 2030/10/18 |
| Haifeng Wang | * (1) | N/A | N/A | N/A |
| Dou Shen | * (1) | N/A | N/A | N/A |
| Xiaodong Wang | * | 0.51 | Various dates from 2015/2/23 to 2020/10/16 | Various dates from 2025/2/23 to 2030/10/16 |
| Xiaohui Wang | * | 0.51 | Various dates from 2016/8/5 to 2020/10/16 | Various dates from 2026/8/5 to 2030/10/16 |
| Xiangjun Wang | * | 0.25 to 0.51 | Various dates from 2010/10/18 to 2020/10/16 | Various dates from 2020/10/18 to 2030/10/16 |
| Xianghua Yang | * | 0.25 to 0.51 | Various dates from 2010/10/18 to 2020/10/16 | Various dates from 2020/10/18 to 2030/10/16 |
| Youqiao Duan | * | 0.25 to 0.51 | Various dates from 2012/5/8 to 2020/4/1 | Various dates from 2022/5/8 to 2030/4/1 |
| Wenfeng Liu | * | 0.30 to 0.51 | Various dates from 2014/12/5 to 2020/10/16 | Various dates from 2024/12/5 to 2030/10/16 |
| Total | 218,639,807 | | | |

Notes:

* The aggregate number of ordinary shares exercisable from all options granted is less than 1% of iQIYI’s total issued and outstanding ordinary shares.

(1) In the form of restricted share units

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Other Information

Estate duty

Our directors have been advised that no material liability for estate duty is likely to fall on our Company or any of our subsidiaries.

Litigation

See “Business—Legal Proceedings” for further information.

Joint Sponsors

The Joint Sponsors made an application on behalf of our Company to the Listing Committee for the listing of, and permission to deal in, the Shares in issue, the Shares to be issued pursuant to the [REDACTED] (including the additional Shares which may be issued pursuant to the exercise of the [REDACTED]), and the Shares to be issued pursuant to the Share Incentive Plans, including pursuant to the exercise of options or other awards that have been or may be granted from time to time. All necessary arrangements have been made to enable such Shares to be admitted into [REDACTED].

Each of the Joint Sponsors satisfies the independence criteria applicable to sponsors set out in Rule 3A.07 of the Hong Kong Listing Rules.

The fee payable to each of the Joint Sponsors is US\$[REDACTED] and is payable by our Company.

No Material Adverse Change

Our directors confirm that except as disclosed in “—Impact of COVID-19 On Our Operations” and elsewhere in this document, up to the date of this document, there has been no material adverse change in our financial or trading position or prospects since December 31, 2020, and there has been no event since December 31, 2020 which would materially affect the information shown in our consolidated financial statements included in the Accountants’ Report in Appendix IA to this document.

Qualification of Experts

The following are the qualifications of the experts (as defined under the Hong Kong Listing Rules and the Companies (Winding Up and Miscellaneous Provisions) Ordinance) who have given opinions or advice which are contained in this document:

| <u>Name</u> | <u>Qualification</u> |
|--------------------------------------|---|
| Merrill Lynch (Asia Pacific) Limited | A licensed corporation under the SFO for type 1 (dealing in securities), type 4 (advising on securities), type 5 (advising on futures contracts) and type 6 (advising on corporate finance) of the regulated activities as defined under the SFO |
| CLSA Capital Markets Limited | A licensed corporation under the SFO for type 4 (advising on securities) and type 6 (advising on corporate finance) of the regulated activities as defined under the SFO |
| Goldman Sachs (Asia) L.L.C. | A licensed corporation to conduct type 1 (dealing in securities), type 4 (advising on securities), type 5 (advising on futures contracts), type 6 (advising on corporation finance) and type 9 (asset management) regulated activities as defined under the SFO |

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| <u>Name</u> | <u>Qualification</u> |
|------------------------------------|--|
| Ernst & Young | Certified public accountants and Registered Public Interest Entity Auditor registered in accordance with the Financial Reporting Council Ordinance |
| PricewaterhouseCoopers | Certified Public Accountants under Professional Accountant Ordinance (Cap. 50) Registered Public Interest Entity Auditor under Financial Reporting Council Ordinance (Cap. 588) |
| China Insights Consultancy Limited | Industry consultant |
| King & Wood Mallesons | Legal adviser to Company as to PRC law |
| Maples and Calder (Hong Kong) LLP | Legal adviser to Company as to Cayman Islands law |

Consents of Experts

Each of the experts above has given and has not withdrawn its consent to the issue of this document with the inclusion of its report and/or letter and/or legal opinion (as the case may be) and references to its name included in the form and context in which it respectively appears.

None of the experts named above has any shareholding interests in our Company or any of our subsidiaries or the right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in our Company or any of our subsidiaries.

Preliminary Expenses

Our Company did not incur any material preliminary expenses.

Promoter

Our Company has no promoter for the purpose of the Hong Kong Listing Rules. Within the two years immediately preceding the date of this document, no cash, securities or other benefit has been paid, allotted or given nor are any proposed to be paid, allotted or given to any promoters in connection with the [REDACTED] and the related transactions described in this document.

Binding Effect

This document shall have the effect, if an application is made in pursuance of this document, of rendering all persons concerned bound by all of the provisions (other than the penal provisions) of Sections 44A and 44B of the Companies (Winding Up and Miscellaneous Provisions) Ordinance insofar as applicable.

Bilingual Document

[REDACTED]

Miscellaneous

- Save as disclosed in “Financial information”, “Directors and senior management” or this appendix in this document or otherwise waived or exempted from disclosure pursuant to the waivers and

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exemptions disclosed in “Waivers and Exemptions”, within the two years immediately preceding the date of this document:

- to the best of our knowledge, neither we nor any of our Significant Subsidiaries has issued or agreed to issue any share or loan capital fully or partly paid up either for cash or for a consideration other than cash;
- no share or loan capital of our Company is under option or is agreed conditionally or unconditionally to be put under option;
- no commissions, discounts, brokerage or other special terms have been granted in connection with the issue or sale of any share capital or debentures of our Company or any of our Significant Subsidiaries;
- no founder, management or deferred shares of our Company or any of our subsidiaries have been issued or agreed to be issued; and
- there is no arrangement under which future dividends are waived or agreed to be waived.
- Our branch register of members will be maintained in Hong Kong by our [REDACTED]. Unless the directors otherwise agree, all transfers and other documents of title of Shares must be lodged for registration with and registered by our share register in Hong Kong and may not be lodged in the Cayman Islands. All necessary arrangements have been made to enable the Shares to be admitted to [REDACTED].
- Our directors confirm that:
 - there has not been any interruption in our business which may have or have had a material adverse effect on our financial position in the 12 months immediately preceding the date of this document; and
 - save as otherwise disclosed in “Financial Information—Liquidity and Capital Resources”, we and our Significant Subsidiaries have no outstanding debentures or convertible debt securities.
- The English version of this document shall prevail over the Chinese version.

Documents Delivered to the Registrar of Companies

The documents attached to a copy of this document and delivered to the Registrar of Companies in Hong Kong for registration were, among other documents:

- a copy of the [REDACTED];
- a copy of each of the material contracts referred to in “Statutory and General Information—Further Information About Our Business—Summary of Material Contracts” in Appendix IV to this document; and
- the written consents referred to in “Statutory and General Information—Other Information—Consents of Experts” in Appendix IV to this document.

Documents Available for Inspection

Copies of the following documents will be available for inspection at the office of Skadden, Arps, Slate, Meagher & Flom at 42/F Edinburgh Tower, The Landmark, 15 Queen’s Road Central, Hong Kong during normal business hours up to and including the date which is 14 days from the date of this document:

- the Memorandum and Articles of Association of our Company;
- our audited consolidated financial statements for the years ended December 31, 2018, 2019 and 2020;
- the Accountants’ Report from Ernst & Young, the text of which is set out in Appendix IA to this document;
- the audited combined financial statements of YY Live for the years ended December 31, 2018, 2019 and 2020;
- the Accountant’s Report of YY Live from PricewaterhouseCoopers, the text of which is set out in Appendix IB to this document;
- the reports on the unaudited pro forma financial information from Ernst & Young, the text of which is set out in Appendix IIA and Appendix IIB to this document;
- the report issued by China Insights Consultancy Limited, a summary of which is set forth in “Industry Overview”;
- the legal opinion issued by King & Wood Mallesons, our PRC legal adviser, in respect of certain aspects of us;
- the letter of advice prepared by Maples and Calder (Hong Kong) LLP, our Cayman Islands legal adviser, summarizing certain aspects of the Cayman Companies Act referred to in Appendix III to this document;
- the material contracts referred to in “Statutory and General Information—Further Information About Our Business—Summary of Material Contracts” in Appendix IV to this document;
- the written consents referred to in “Statutory and General Information—Other Information—Consents of Experts” in Appendix IV to this document; and
- the Cayman Companies Act.