

OUR MARKET OPPORTUNITIES

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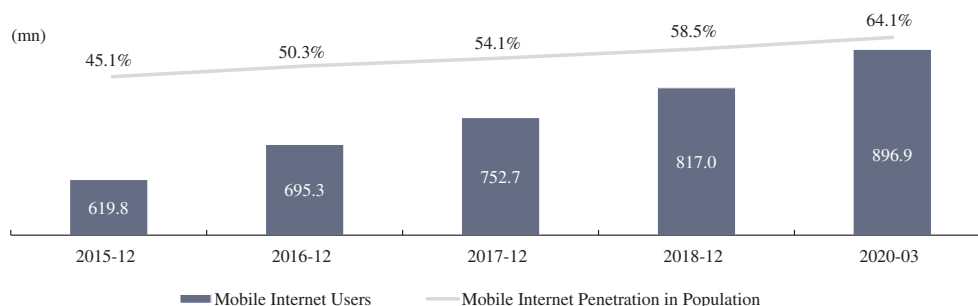
FAVORABLE MACRO TRENDS FOR DIGITAL CONTENT AND SERVICE CONSUMPTION IN CHINA

The high penetration of the mobile internet in China, combined with the sustained growth in its GDP and disposable income per capita, has changed consumption habits and driven the demand for digital content and services in recent years. In particular, China's digital content and service consumption is driven by the following favorable macro trends.

Rising spending power and demand for content and services. With China's robust economic growth and rising income, Chinese consumers are expanding their consumption from goods to content and services. Per capita consumption expenditure on education, cultural and recreation increased at a CAGR of 9.9% from 2015 to 2019, outpacing the overall GDP and consumption growth, according to the NBS.

China represents the largest internet and mobile internet population in the world. According to the CNNIC, the number of internet users in China reached 903.6 million in March 2020. The number of mobile internet users reached 896.9 million in March 2020, representing 64.1% of the total population in China as of December 31, 2019, according to NBS, and approximately 2.7 times of the total population of the United States as of December 31, 2018, according to the World Bank.

Significant Penetration of Mobile Internet in China, 2015-2020

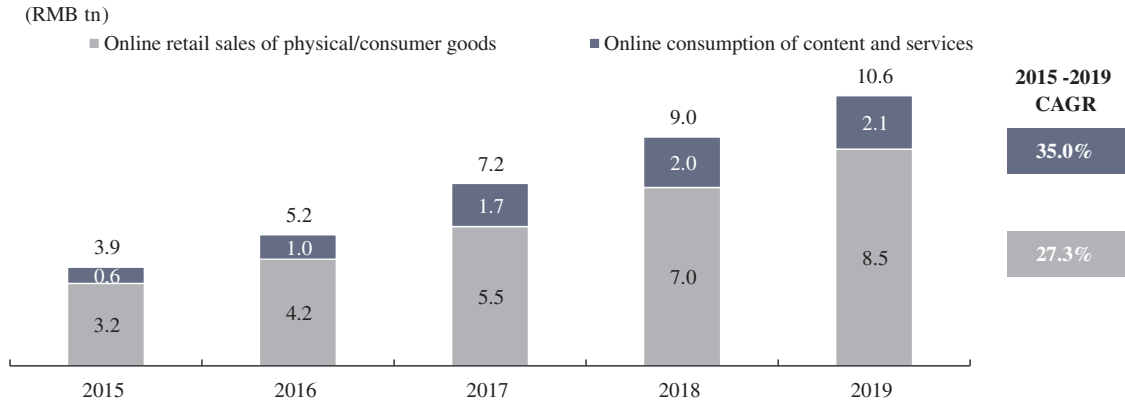


Source: CNNIC (for mobile internet users) and NBS (for total population as of 2015-2019 year-end)

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Well-established infrastructure to boost digital content and service consumption. Enabled by the high penetration and wide coverage of mobile network, total mobile data usage in China amounted to 122 billion GB in 2019, or nearly 60 times of that in 2014, according to the MIIT. In addition, 85.0% of Chinese netizens were using digital payment in March 2020. As a result, consumers in China can easily access, enjoy and pay for premium digital content and data-intensive services. Total digital consumption of content and services in China reached RMB2.1 trillion in 2019, representing a CAGR of 35.0% since 2015 and outgrowing that of online retail sales of physical/consumer goods, according to the NBS.

Rising Digital Consumption in China, 2015-2019



Source: NBS

Note: Total digital consumption figures include online retail sales of physical goods and non-physical goods (including content and services).

Evolving demand for quality content and services. We believe that the massive internet population and the general trends of consumption upgrade in China will further drive the demand and willingness to pay for more diverse and quality digital content and services. At the same time, empowered by various new technologies, content and service providers have more capabilities to explore innovative formats, enrich user interaction, offer quality experience and fulfill evolving consumer needs. We see tremendous opportunities in delivering and innovating in major digital content and service segments, including games, intelligent learning and music streaming.

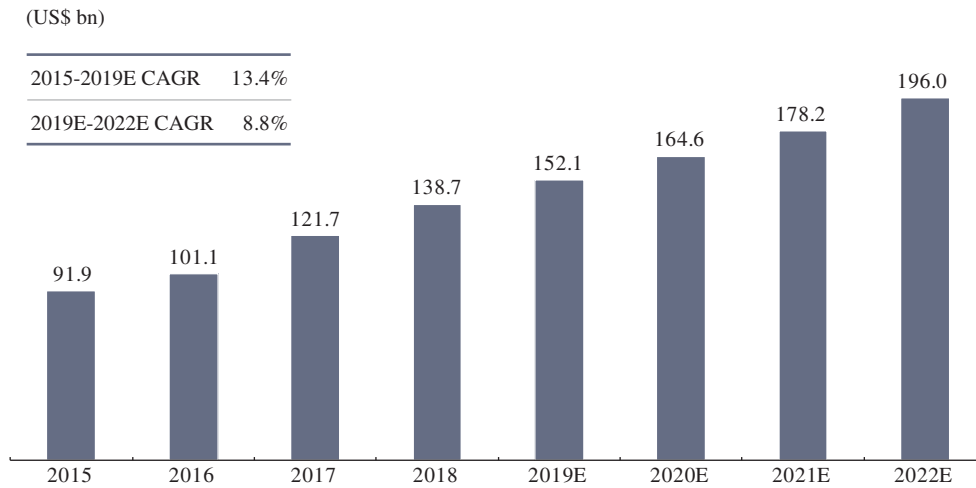
GLOBAL GAMES MARKET

Overview of the global games market

The estimated market size of global games market in 2019 was US\$152.1 billion, representing a CAGR of 13.4% from 2015, and is forecasted to further grow to US\$196.0 billion in 2022, according to Newzoo.

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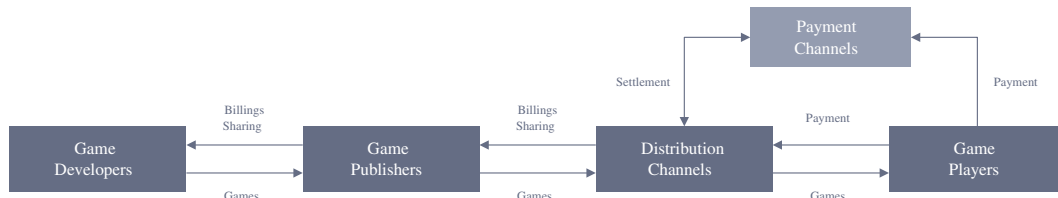
Global Games Market Size in Terms of Revenue, 2015-2022E



Source: Newzoo

Participants in the games market primarily comprise game developers and other IP holders, game publishers, game distribution channels and game players. Certain market participants take multiple roles along the industry value chain and develop, publish and distribute games from time to time.

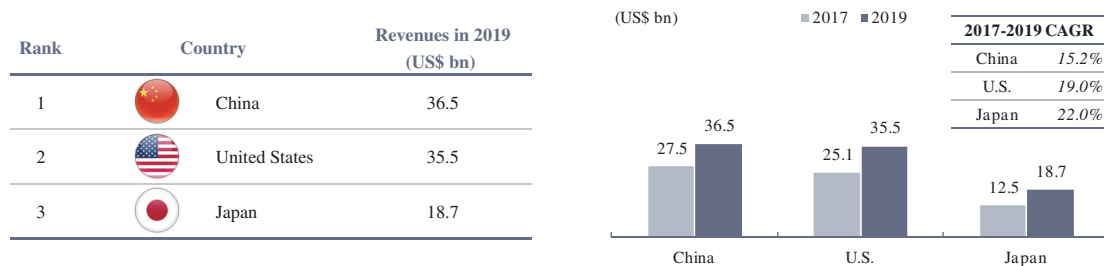
Typical Games Market Value Chain Illustration



Top Three Games Markets: China, the United States and Japan

China, the United States and Japan ranked as the three largest games markets globally in 2019 in terms of revenue estimates, according to Newzoo. The combined market size of these top three games markets was estimated to be US\$90.7 billion in 2019, taking up approximately 60% of the global games market, according to Newzoo.

Top Three Global Games Markets and Their Growth



Source: Newzoo

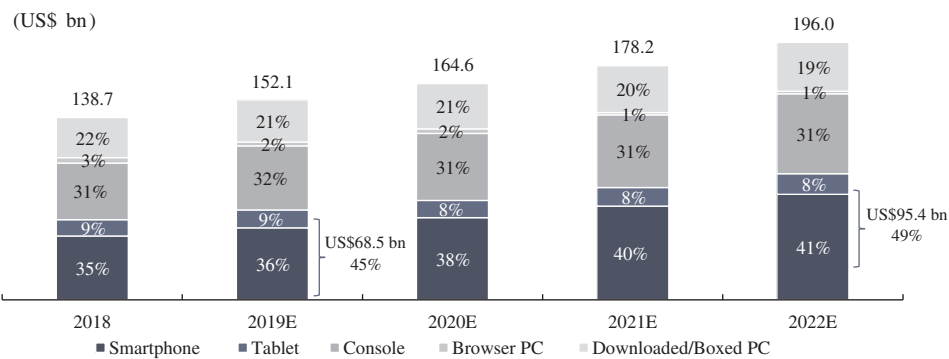
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Shift towards mobile games

Size and fast growth of the global mobile games market

Benefitting from the proliferation of mobile internet, penetration of smart devices and shifting user habits, mobile games has become the largest and fastest-growing segment in the overall games market. In 2019, mobile gaming was estimated to generate revenues of US\$68.5 billion, accounting for approximately 45% of the total global games market, according to Newzoo. Mobile gaming is expected to generate revenues of US\$95.4 billion in 2022 at a CAGR of 11.7% from 2019 to 2022, and account for almost half of the entire global games market in 2022, outpacing growth of other segments and the overall games market, according to Newzoo.

Breakdown of Global Games Markets by Segment in Terms of Revenue, 2018-2022E



Source: Newzoo

Competitive landscape of global mobile games market

In 2019, NetEase ranked as the second largest mobile app publisher globally in terms of combined iOS and Google Play revenue estimates, according to App Annie.

Top 10 Global Mobile App Publishers in Terms of Combined iOS and Google Play Revenue, 2019

Rank	Company	Nationality
1	Tencent	China
2	NetEase	China
3	Activision Blizzard	United States
4	Supercell	Finland
5	BANDAI NAMCO	Japan
6	Netmarble	South Korea
7	Playrix	Ireland
8	Sony	Japan
9	Playtika	Israel
10	InterActiveCorp (IAC)	United States

Source: App Annie

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Market opportunities for Chinese game companies

China ranked as the largest games market in the world in terms of revenue estimates in 2019, according to Newzoo. The number of game players in China reached approximately 531.8 million in March 2020, compared to approximately 417.0 million in December 2016, according to CNNIC. The domestic market therefore provides massive opportunities for Chinese game developers and publishers. At the same time, overseas markets also represent further opportunities for Chinese game developers to expand their footprint.

In light of the geographical concentration and rising share of mobile gaming in the global games market, we believe participants with an established presence in top markets such as China, the United States and Japan and in-depth expertise in developing and operating mobile games are well-positioned to capture future opportunities.

Key market trends affecting competition in China's online and mobile games markets

We have observed the following key market and competitive trends of China's online and mobile games markets:

- *Focus on game quality and innovation.* As game players become increasingly sophisticated, we believe that the quality and innovative features of games, such as new and engaging gameplay elements, attractive visuals and intriguing narratives, are key in ensuring a superior user experience and attracting and retaining users.
- *Overseas markets expansion.* Market participants in China's online and mobile games industries continue to launch games in global markets as well as partner with or invest in international game studios to enhance development capabilities and operational experience.
- *IP ownership.* As the online and mobile games industries continue to attract new entrants, strong capabilities in developing and maintaining in-house IPs are key for building solid game pipelines, attracting large and engaged player bases and competing effectively.

The online and mobile games markets are fast-evolving. The emergence of new technologies, such as migration from 4G to 5G and the widespread adoption of AR/VR games, might enable new formats of gameplay, further boost online content consumption, and create space for new entrants. Online game companies also constantly compete with providers of other pan-entertainment services such as online video, online music live streaming, news feed and social media for user traffic, time and spending. Established companies, including us, face challenges in keeping up with the shifting trend, consistently producing popular new content and effectively engaging users.

The ability to continually creating original content and differentiated user experience is crucial for success in the online and mobile game markets. Such capabilities rely on multiple factors, including established brand and IPs, deep user insights, technology, R&D and operational expertise. It typically takes significant investment and years of time for new entrants to build strong brands and IPs, gain market expertise and insights and build a pipeline that can produce popular content in a systematic manner.

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OTHER DIGITAL CONTENT AND SERVICE MARKETS IN CHINA

Online learning market

Benefiting from the development of internet and other technologies, as well as the increasing demand and recognition for remote and flexible learning, the user base of the broader online education sector in China increased almost threefold from 110.1 million in December 2015 to 423.0 million in March 2020, according to CNNIC.

Market trends that are expected to drive the development of online learning market in China mainly include further integration of technology with learning, increasing coverage of more learning scenarios, use of smart devices and AI tutoring, competition over high-quality teaching resources, rising user acquisition costs, the shift from exam-oriented to quality-oriented learning and favorable government policies. Market players that can adapt well to these trends are expected to compete more effectively in the industry.

Other digital content and service markets

The rapid development and penetration of the internet has further propelled the growth of various other digital content and services, such as media, e-commerce and online music. Users continue to seek high-quality and reliable content and services, and the availability of vast user data enables the creation of a more user-centric experience based on customized recommendation, real-time content delivery and vibrant online communities. Digital services including media, e-commerce and music streaming have accumulated sizable internet and mobile user bases in China and represent diverse market opportunities.