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SINA - Q3 2018 SINA Corp Earnings Call

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OVERVIEW:

Co. reported 3Q18 non-GAAP net revenues of \$554.6m, non-GAAP net income attributable to SINA of \$67.7m, and non-GAAP diluted EPS of \$0.93. Expects FY18 revenues (assuming US dollar and RMB exchange rate of 6.7) to be CNY14.0-14.2b or \$2.09-2.12b.



CORPORATE PARTICIPANTS

Guowei Chao *SINA Corporation - Chairman & CEO*

Sandra Zhang

Yi Zhang *SINA Corporation - CFO*

CONFERENCE CALL PARTICIPANTS

Alicia Yap *Citigroup Inc, Research Division - MD and Head of Pan-Asia Internet Research*

Eddie Leung *BofA Merrill Lynch, Research Division - MD in Equity Research and Analyst*

Karen Chan *Jefferies LLC, Research Division - Equity Analyst*

PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the SINA's Earnings Company Call for the Third Quarter of 2018 Conference Call. (Operator Instructions) I must advise you that this conference is being recorded today, Wednesday, 28th of November 2018.

I would now like to hand the conference over to your first speaker today, Ms. Sandra Zhang. Thank you. Please go ahead.

Sandra Zhang

Thanks, operator, and hello, everyone. Welcome to SINA's Earnings Conference Call for the Third Quarter 2018.

Joining us today are Chairman and CEO, Charles Chao; and our CFO, Bonnie Zhang. This call is also being broadcast on the Internet and is available through our IR website at ir.sina.com.

Now let me read you the safe harbor statement in connection with today's conference call. Our discussion today will contain forward-looking statements, which involve inherent risks and uncertainties that may cause actual results to differ materially from our current expectations. SINA assumes no obligation to update the forward-looking statement in this call and elsewhere. For detailed discussion for these risks and uncertainties, please refer to our latest Annual Report on Form 20-F and other filings with the SEC.

In addition, I would like to remind you that our discussion today include non-GAAP measures, which mainly exclude stock-based compensation and certain other items. We use non-GAAP measure to gain better understanding of SINA's comparative operating results and future prospects. Please refer to our earnings release for more detailed information on reconciliation of GAAP to non-GAAP measures.

During the call, we may discuss non-GAAP measures for Weibo, which applied the same methodology we use to calculate non-GAAP measure at the SINA group level. After management remark, we will open the lines for brief Q&A session.

With that, I would like to turn the call over to our CFO, Bonnie.

Yi Zhang - SINA Corporation - CFO

Thank you, Sandra, and thank you all for joining our conference call today. Let me walk you through the operational and the financial highlights for the third quarter 2018.



Before the detailed financial review, I would like to remind you that unless otherwise noted, my prepared remarks would focus on non-GAAP results, and all the comparisons are on a year-over-year basis. In addition, for ease of comparison, I may also indicate our revenue or expenses figures under the old accounting standard, which excludes barter transactions and adds back value-added tax to the related current period financials.

Let's start with an overview of third quarter results. SINA's net revenue for the third quarter of 2018 were \$554.6 million, up 26% or 29% on a constant currency basis. SINA's operating income grew 16% to \$168.1 million. Net income attributable to SINA was \$67.7 million, and the diluted EPS was \$0.93. SINA's online advertising revenue for the third quarter of 2018 grew 33% to \$483.8 million, primarily driven by an increase of \$132.5 million or 48% of growth in Weibo advertising and marketing revenue.

Let me provide some color on Weibo's platform growth. As a platform with mobile MAU over half of the mobile Internet population in China, we will continue to deliver strong user growth and engagement, further solidifying the platform position as the leading social media in China. We attributed the robust growth of the platform to team's efforts in product revamp, channel investment and content ecosystem cultivation, which further strengthened the social network effect and broadened our strategic moat to serve public and social interactions among Chinese and the global Chinese communities.

On top of user growth, Weibo demonstrated and reinforced the unique value proposition for advertisers through a full spectrum of social products for -- commercial products serving advertisers' comprehensive social marketing demand. In the third quarter, the increase in customer number and ARPA continued to be the driver of ad revenue growth. From an industry perspective, we'll continue to see vitality in Weibo's top key account industry, with FMCG and the 3C growing at a triple-digit rate on an annual basis.

The SME sector also delivered soft growth in Q3 amid the recent regulatory changes in few vertical industry, such as gaming and fintech. We expect these challenges will continue to weigh on the gross perspective of marketing dollar in the above-named industry segment in the foreseeable future.

Portal ad revenue were \$74.5 million, down 15% or 10% under the old accounting method or down 12% on a constant currency basis. Excluding the accounting and unfavorable currency changes, portal revenue was pressured from ad budget cutback by SME customers operating in sectors under tightened regulations such as fintech. Despite the regulatory and macro uncertainties, we're pleased to see the resilient advertising performance of few brand industry of portal such as auto. This was partially attributable to the healthy traffic growth across SINA's mobile media properties, particularly the SINA Finance app with the average DAU growing 214% on an annual basis.

On the monetization front, mobile ad revenue continued to grow at a healthy rate, contributing approximately 79% of total portal ads, up from 63% last year.

Turning to non-advertising business. Non-ad revenue was \$70.8 million, down 8% or down 2% under the old accounting method. Excluding the accounting change and the negative currency translation impact, the decline was resulted from the lackluster fintech business due to the regulatory headwinds, which was partially offset by the increase in Weibo value-added service.

Portal non-ad revenue was \$24.1 million, 35% decrease on a year-over-year basis, mainly resulted from the downturn of payment business because of the sweeping default wave of P2P companies, as we alerted in the prior conference call. On the other hand, the micro loan facilitation business has returned to the growth trajectory even under the tough comps in Q3 2017 as we launched new fintech products and upgraded our compliance standards according to the latest government regulation outlines.

Turning to gross margin. Gross margin for the third quarter of 2018 was 80%, up from 76% last year. Advertising gross margin was 82%, up from 77%. The increase in advertising gross margin was mainly result from our revenue reporting changes from gross basis to net basis under the new accounting standard adopted. Non-advertising gross margin for the third quarter of 2018 was 70%, flat year-over-year.

Now moving on to operating expenses. In the third quarter, operating expenses totaled \$276.4 million, up 46% or 30% under the old accounting standard year-over-year. Under the old method, sales and marketing expenses took approximately 26% of SINA's net revenue, up 1% from last year but dropped 2% sequentially. The slight rise of sales and marketing expenses as a percentage of revenue was driven by the increase in -- of

investment in channel marketing on user acquisition of Weibo app, SINA News app and SINA Finance new -- Finance app. In addition to the sales and marketing expenses, the increase in personnel-related costs was another factor that led to the increase in OpEx.

Operating income grew 16% to \$168.1 million, representing an operating margin of 30%, down from 33% last year. Nonoperating income under GAAP measure was \$77.3 million compared to \$11.1 million last year. Nonoperating income in Q3 included a \$50.1 million net gain on sale of investment, fair value changes and the impairment on investments, which is excluded under non-GAAP measures; a \$17.1 million net interest and other income; and a \$10.2 million net earnings from equity method investment mainly resulted from earning pickup related to company's investment in Tian Ge. Please refer to our earning release for more detailed information about nonoperating item for the same period last year.

Turning to tax. Under the GAAP measure, income tax expenses were \$68.1 million compared to \$24.6 million last year, largely attributable to the deferred tax liability recognized from the fair value changes of certain investment.

Net income attributable to SINA was [\$67.7] million or \$0.93 diluted net income per share (corrected by company after the call).

Now let me turn to the balance sheet and cash flow items. As of September 30, 2018, SINA's cash, cash equivalents and short-term investments totaled \$2.5 billion compared to \$3.4 billion as of December 31, 2017. The decrease of SINA's cash and short-term investments were primarily due to continued investment activities made in the first 3 quarters, including the payment of land use rights for our headquarter building in Beijing and the execution of share repurchase program in an amount of \$228.9 million. For the third quarter 2018, net cash provided by operating activities was \$100.8 million, capital expenditures totaled \$46.8 million, and the depreciation and amortization expenses amounted to \$9.9 million.

Before wrapping up my prepared remarks, I would like to make a note on the company's fiscal year 2018 revenue guidance. In view of the macroeconomic condition and the regulatory impact, we're revising our fiscal year 2018 revenue guidance to a range of RMB 14 billion to RMB 14.2 billion or USD 2.09 billion to USD 2.12 billion, assuming U.S. dollar and RMB exchange rate of 6.70. The revised revenue guidance represents a year-over-year growth rate of 32% to 34%, reflects a 5% to 7% adjustment to the midpoint of original revenue guidance we provided at the beginning of 2018.

With that, operator, please open up for the calls.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from the line of Eddie Leung from Merrill Lynch.

Eddie Leung - BofA Merrill Lynch, Research Division - MD in Equity Research and Analyst

Charles and Bonnie, a couple of questions. I guess the first one is a more high level. SINA has been in the Internet industry for quite a while, so just wondering if you could share your thoughts and observations with us on the macro environment we are facing this time versus a couple of macro headwinds in the past like 2009 as well as, for example, 2012, those times, any differences and similarities. And then secondly, could you also give us an update on the SINA News app? Any -- for example, any update on the operating metrics as far as contributions to the portal advertising dollars, that would be great.

Guowei Chao - SINA Corporation - Chairman & CEO

Okay, Eddie, I'll try to answer your first question. That's a tough one. Okay, I think it's -- actually, it's a very good question. I mean, over the last 20 years, we have been through several cycles, up and downs, I mean, and the Internet bubbles and then the Internet bubble bursts and then the new opportunities coming from gaming, from SPE and from eCommerce, and then we have mobile Internet. And so there are a few round of cycles

we have been going through, and some of these are impacted by the macroeconomic conditions, some of these are not. And -- but in terms of impact of macroeconomics, I mean, I think in the past, our experience has -- if the macroeconomic conditions impact the entire economy, and the Internet industry may not be affected too much primarily because the entire Internet market is growing despite of the bad economic conditions on macro basis. And in terms of user growth, in terms of more adoption of different applications and in terms of more time spending on Internet. So when you have this kind of situation, I mean, the Internet industry is not so much affected by the macroeconomic. I mean, maybe certain industry like auto, like real estate, this type of vertical areas might be more affected in terms of advertising dollars for particular vertical industry. But overall, I think there's not that much impact. And especially, I mean, in the economic downturn and when the macroeconomic condition not very good -- was not very good, people actually tend to Internet for more -- for the improvement of efficiency of their old businesses and more effective marketing channels for their products. So overall, I think that in the past, I think that the macroeconomic conditions, I mean, in the down cycle do not have too much impact on the Internet industry. But this time, maybe a little bit different partly because the entire Internet market in terms of the user growth is kind of stabilized or stagnant a little bit. And in terms of time-consuming consumption, our Internet is also slowing down in terms of the time spent, I mean, on Internet grows, and so these factors, and not to mention that Internet is already in everybody's life, affecting every industry already. So in that sense, I think the macroeconomics condition, I mean, will have more impact this time versus previous round. And that's probably what we have seen in some of the areas -- I mean, we have been experiencing right now in both SINA portal and Weibo and especially in some of the areas like travel, for example, like some of the auto service industries and big-ticket items like wedding-related expenditures, we have seen some slowing down. That has to do with macroeconomic conditions. And indirectly, we believe that it can also impact the investment in the entire Internet industry as a whole. And you have seen sort of weakened decline in terms of investments in that particular sector. That actually also indirectly impact the demand for advertising for a lot of the data companies or companies trying to driving traffic for their new applications, new Internet services. And this kind of demand also coming down, and so that will have impact indirectly on our industry. And so this is kind of -- sort of our take in terms of the impact of macroeconomic conditions on our industry as a whole, I mean, for this particular cycle, I guess.

And regarding the second question, the News app, I think the News app is an area that, on overall market basis, is likely to be mature in terms of overall market growth and also in terms of time spent. So the people actually are more competing on the time spent on this particular app versus another one. And so the overall growth rate for every app in this sector is quite -- is slowing down quite a bit. And for us, we're still growing but on a much smaller paces in the second half of this year versus -- and comparing to the previous first half and in -- or comparing to previous year. But in terms of efficiency, monetization is still growing. And -- but on an overall basis, I mean, given that the chart is not growing that much and given that the demand for advertising as much for SME, I mean, is kind of challenging not only for Weibo but also for the -- our SINA Mobile business, and so we're still going to have some challenges in the near future in terms of growing our revenues for SINA Mobile, especially for SMEs. Hopefully, I answered your question.

Operator

Your next question comes from the line of Alicia Yap from Citigroup.

Alicia Yap - Citigroup Inc, Research Division - MD and Head of Pan-Asia Internet Research

I have follow-up questions on the Weibo comment earlier. I think Gaofei Wang mentioned about the internal investment into the MCN for some of the subsidy given its -- the slowing macro, and the subsidies is also affecting the slower guidance growth. So just wanted to know roughly how much of this initiative in terms of reinvestment into the MCN is affecting our fourth Q guidance slowdown. And is this actually in line or related to Alibaba's strategy, which is also pushing off the monetizations of the recommended feeds? Or is it kind of separately? And then quickly, on the housekeeping questions is that, does the revisions of SINA and also Weibo guidance include any of the Yi Zhibo contribution in the fourth quarter?

Guowei Chao - SINA Corporation - Chairman & CEO

Okay, Alicia, let me try to answer your first question. I think these are 2 separate issues in terms of investment in our KOL and the MCNs. I think this is really try to build a stronger content ecosystem for our Weibo platform basically with more KOLs, with more MCNs, we're going to see more content being contributed by the big KOLs and also more interactions between our KOLs and our user base. And this has always been our strategies, I mean, for the last whatever years and try to build a strong good ecosystem for our KOLs. And our subsidiary really try to encourage people to



actually create more content and help them to building -- to build a bigger social asset on our Weibo platform so that they can benefit from their strong social assets going forward. And also indirectly, I mean, when these people are building a stronger social asset and they have more incentive actually to spend marketing dollar on us, actually, I mean, to -- this will be organic drivers for our advertising revenues for our ecosystem. And -- but this has nothing to do really -- yes, I mean, it's more from our perspective to create a stronger content ecosystem not really directly to our revenue guidance for the fourth quarter. And for the fourth quarter, I think Gaofei has already kind of elaborate some of the market conditions and as well as some of the challenges we are facing in the market. Some of these are regulatory related. Some of these are macroeconomics related. And some of these are competition related, and some of these could be our internal related. And there are multiple factors. I mean, when some of this from demand side, some are from supply side, and there's a mixed picture. Overall, I think with KA, we should be still doing very well and have very meaningful strong growth. And SME is a little bit challenging. And we can elaborate some of the factors affecting SME, and some of this could be near term, I mean, like regulatory issues, whether it's in gaming and this type of things. And some of these could be a little bit longer in terms of the demand side and -- like a travel business, like wedding businesses. And -- but some of supply side issue could be more complicated because we have been a much competitive market in terms of supplying this kind of inventories for the mobile advertising, and so this coped with the demand side problems we are facing some of the challenges in the SME areas, I mean, in near future. But overall, I think there's probably an overall picture, and I think I've got -- already elaborated these very well in the previous conference call. And in terms of revision of the guidance, maybe Bonnie can give you some color on that.

Yi Zhang - SINA Corporation - CFO

For the fourth quarter guidance, we have included our best estimates of Yi Zhibo live broadcasting revenue contribution into the number. So -- but again, it's a very preliminary estimate. We just acquired the team, and we're still in the midst of the product conversion period.

Operator

Your next question comes from the line of Karen Chan from Jefferies.

Karen Chan - Jefferies LLC, Research Division - Equity Analyst

Two questions here. First, within our top 5 KA verticals, including auto, FMCG or finance, which have seen the most macro impact? And in particularly for auto OEMs, are we seeing any indication to pull back in ad spending as these advertisers plan for their 2019 ad budget? Secondly, maybe more a question for Charles. Given the many changes we have seen in the regulatory environment recently, be it mobile games, eCommerce, video, et cetera, just want to get your thoughts on how is this level of participation from regulatory bodies different from the last, if in any way? And will any of these Internet segments or what kind of platforms do you think will show a higher resilience when the dust settles?

Guowei Chao - SINA Corporation - Chairman & CEO

Okay. In terms of the verticals, and historically, our top verticals, like automobiles, like the financials, like FMCG, these are our 3 top ones. And the smaller ones, like eCommerce and maybe the...

Sandra Zhang

IT product.

Guowei Chao - SINA Corporation - Chairman & CEO

IT product, yes -- IT product, yes, that's -- like IT product, actually including the mobile phones. And I think that -- currently, I think we are seeing, as Gaofei mentioned in the previous call, some are big-ticket items, I mean, affecting some of the spendings, especially for performance-related

advertisement. But in terms of the brand advertising, we are not seeing that much impact so far. And everybody -- for example, for automobile industry, we know that the auto sales is going down in the second half of the year on a yearly basis for China market, but then we're not seeing that much impact on advertising yet. Obviously, it's not great, but maybe it explains the serious act. When the market is not doing very well, the automobile manufacturers actually have more incentive to spend money to push themselves. And in some way, that offset some of the impact of the declining sales for automobile industry. And that's the -- some of the market where they have been. In terms of the FMCG, I think it's not that much related to the macro yet, and we're not seeing too much impact from the spending from customers for these kind of industries, and same for IT. And so overall, the KA, I think we are not seeing that impact at the current stage. But the real impact is really for the SME. And also for the -- I will say the big customers, I mean, some of the big customers for performance-based advertising, they actually scaled back quite a bit in certain industries, as we mentioned, like travel, like wedding related, like fintech, these kind of areas. And in terms of the other question you have, on the overall basis in the regulatory environment, in terms of macro environment, which industry is less affected, that is a tough question, and I think it's a complicated one because it's difficult to pin down a particular industry or particular application that were more resilient. On overall basis, if you look at the Internet industry as a whole, although you have a very different product format for different companies, at the end of the day, most of the companies generate their revenues from advertising, I mean, right? And some of these are more related to performance-based advertising for Internet service, like gaming advertising, like eCommerce advertising, like download our apps, this type of things. And some of these are related to the -- I will say, the brand advertising. And then you have another category now generate revenue from advertising, mainly the content fee-based service like gaming, like long video, this type of things. And these are the major advertise -- sorry, the business models or revenue models for majority of Internet companies. And so if you look at these models, and you can easily identify some of these areas, if they're relying on certain revenues and certain regulatory change, and the macroeconomic change will have a great impact on these particular companies who rely on particular model. But on overall basis, I think each company will be affected by slowing down in advertising business and which including the KA business, brand advertising business and the performance-based SME business. And in terms of KA, I mean, as I said, at the current stage, we're not seeing that much impact right now, but maybe it's due to the strength of our platform in terms of delivering service better for our KA customers than other platforms. And as you know, we have a pretty robust platform for both Weibo social media and for the News app and to provide overall service for advertising customers, for KA customers. And -- but over longer term, if macroeconomic continues -- that the condition lasts, then I think overall, it will eventually KA customer base and have impact on the KA advertising. But I think at the current stage, I mean, we are seeing actually more challenging environment is in the performance-based advertising for SMEs, as I elaborated in the previous question, that a lot of these has demand issues, and then also we are facing some supply issues. That actually is common for every player in this market. And in the demand side, we have regular impact on the gaming and fintech. We have the macroeconomic impact on investment-related travel and this type of industries. And so these was the inventory, I mean, I think hit the market. And if you look at the companies will allow much on the performance-based advertising, I think these companies will be more affected on an overall basis. That will be my assessment. I hope that answer your question.

Operator

There are no further questions at this time. I would now like to hand the conference back to today's presenter, Ms. Sandra Zhang. Please continue.

Sandra Zhang

This concludes our conference call today. Thank you all for joining us. We'll see you next quarter.

Operator

Ladies and gentlemen, that does conclude our conference for today. Thank you for participating. You may all disconnect.

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