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MOMO - Q4 2018 Momo Inc Earnings Call

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## PRESENTATION

### Operator

Ladies and gentlemen, thank you for standing by, and welcome to Fourth Quarter and Full Year 2018 Momo Inc. Earnings Conference Call. (Operator Instructions)

Please note this conference is being recorded today.

I would now like to hand the conference over to your first speaker today, Ms. Cathy Peng. Thank you. Please go ahead, ma'am.

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**Cathy Peng** - *Momo Inc. - Head of IR*

Thank you, operator.

Hello, everyone, and thank you for joining us today for Momo's fourth quarter and fiscal 2018 earnings conference call. The company's results were released earlier today and are available on the company's IR website.

On the call today from Momo are: Mr. Tang Yan, Co-Founder, Chairman and Chief Executive Officer; Mr. Wang Li, President and Chief Operating Officer; Mr. Wang Yu, Founder and Chief Executive Officer of Tantan; and Mr. Jonathan Zhang, Chief Financial Officer. They will discuss the company's business operations and highlights as well as the financials and guidance. They will all be available to answer your questions during the Q&A session that follows.

Before we begin, I would like to remind you that this call may contain forward-looking statements made under the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Such statements are based on management's current expectations and current market and operating conditions and relate to the events that involve known or unknown risks, uncertainties and other factors, all of which are difficult to predict and many of which are beyond the company's control, which may cause the company's actual results, performance or achievements to differ materially from those in the forward-looking statements.

Further information regarding these and other risks, uncertainties and factors is included in the company's filings with the U.S. Securities and Exchange Commission. The company does not undertake any obligation to update any forward-looking statements as a result of new information, future events or otherwise, except as required under law.



I will now pass the call over to Mr. Tang. I will translate for him. Mr. Tang, please.

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**Yan Tang** - Momo Inc. - Chairman & CEO

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

Good morning, and good evening, everyone. Thank you for joining our conference call today.

Q4 was a solid quarter, closing out a fruitful year in 2018. Now my team and I will take you through the details.

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**Yan Tang** - Momo Inc. - Chairman & CEO

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

Firstly, a brief overview of the financial performance.

For the fourth quarter 2018, total revenue reached CNY 3.84 billion, up 50% year-on-year. Adjusted operating income for the quarter was CNY 1.03 billion, up 30% from the same period last year.

For fiscal 2018, total revenue came in CNY 13.4 billion, up 51% year-over-year. Adjusted operating income reached CNY 3.9 billion, up 42% year-on-year.

Excluding Tantan's financial impact, our adjusted operating income for the year would have been CNY 4.2 billion, or a 32% adjusted operating margin, compared to 31% last year.

During the year 2018, we have made significant investment in strengthening the content ecosystem and expanding the talent pool to better support our research and development effort. These investments have made a solid foundation for us to drive further product innovation as well as revenue growth in the year 2019.

Even with the significant investments that we've made, I'm pleased to see that, on an ex-Tantan basis, we were still able to deliver an improvement in bottom line margins as compared to the prior year.

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**Yan Tang** - Momo Inc. - Chairman & CEO

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

Now a deeper dive into the quarter. Firstly, our community continued to grow. The core Momo app had 113.3 million monthly actives for the fourth quarter, up 14% year-on-year and representing a 2.8 million net addition from the previous quarter. Last quarter, we mentioned that we had a major cleanup of the spamming activity starting from September. The campaign had a peak of its impact well into September and October. Since then, we've seen a gradual rebound in different engagement metrics. Per user time spent reached an all-time high since the beginning of 2017,

largely driven by the rapid growth of the audio- and video-based live interactive experiences that have flourished on the platform during the past 2 years.

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**Yan Tang** - Momo Inc. - Chairman & CEO

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**Cathy Peng** - Momo Inc. - Head of IR

Total paying users for the core Momo platform reached 9.1 million in Q4 2018, representing a 16% year-over-year growth or a 200k net addition from last quarter. Paying user for Tantan continues to increase rapidly, reaching 3.9 million in the fourth quarter, a quarterly net addition of 300,000.

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**Yan Tang** - Momo Inc. - Chairman & CEO

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

As we close out the year 2018 and start going into '19, I'd like to share some of my thoughts on how to better serve our users and pursue growth opportunities in the coming year.

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**Yan Tang** - Momo Inc. - Chairman & CEO

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**Cathy Peng** - Momo Inc. - Head of IR

Although China's mobile Internet user growth has been substantially slowing down, we still see plenty of growth opportunities in the open social space. More importantly, unlike some of the trends that come into fashion quickly and out of it just as fast, discovering new relationships is a basic human demand that is always going to be there. Although Momo and Tantan, collectively, we are already the dominant player in this space, our rough estimation is that the combined MAU of Momo and Tantan is less than 1/2 of the total addressable market that we're aiming at. How fast we can grow and penetrate deeper into that addressable market depends on how fast we can innovate in order to help more users effectively discover new friends and build meaningful interactions.

If we think about the key challenges that have been holding us back from growing faster, here are the major ones: a, the limited ways that we connect people; and b, the limited forms of interactions that we offer. For example, for many of our users, especially those in lower-tier cities, text-based communication can be a high-barrier form of interaction, and we found that audio- and video-based interaction and entertaining content can effectively lower that communication barrier. In addition, physical proximity has long been the major connecting dimension that we offer. In some cases, it can be a very natural bonding element. But in many other cases, it is not. We believe, by considering other factors, for example user's behavioral data and measurements indicating the likelihood of interaction, we can help the users make much more relevant discoveries and improve their quality of interaction on the platform.

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**Yan Tang** - Momo Inc. - Chairman & CEO

(foreign language)

**Cathy Peng** - Momo Inc. - Head of IR

During the past 2 years, we have made tremendous progresses in enriching the social features to broaden the form of interactions as well as diversifying the ways of connecting people. Three years ago, when people came to Momo, what they could do were pretty much limited to checking out Nearby People and IM-based chatting. Nowadays, people are connecting and interacting over a variety of different use cases, including Nearby functions, live shows, short video, social games, karaoke and other form of audio and video experiences. More specifically, in the year 2018, one of our biggest achievements on the product side is that after several quarters of trial and error, we finally figured out the right formula for building live audio and video interactive experiences beyond the live broadcasting showrooms. That's essentially pushing the application of live streaming technology beyond the talent show business to better serve Momo users' unique social demands. In Q1 2018, we introduced audio chat rooms. Later in the year, we added karaoke and other sort of interactive tools into the chat rooms. Throughout the year, we've seen the retention ratio of the chat room gradually improving, and now it is already one of the major social use cases on the platform. In terms of DAU penetration, it's now at the same level as the interest group. Because users on average spend much longer time in audio chatting than in text-based chatting, in terms of total time spent, audio chat room is actually more than twice as big as the interest group and half as big as the live streaming service. In addition, Quick Chat and Parties, which were 2 earlier social experiences we launched in late 2017 after several rounds of group iteration, also reached a stable growth in Q3, both in terms of usage and in terms of revenues.

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**Yan Tang** - Momo Inc. - Chairman & CEO

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

In 2018, we also took the first step towards diversifying the connecting dimensions. We started to test other recommendation strategies in the algorithm to supplement physical proximity. Our experiments in Nearby People and Nearby Posts showed positive results in driving interactions and response rate to greetings. What we are doing here are still pretty early days, and we have a long way to go. In the year 2019, it remains an important task of ours to tweak the algorithm with the goal of helping people make more relevant discoveries and build more meaningful interactions.

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**Yan Tang** - Momo Inc. - Chairman & CEO

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**Cathy Peng** - Momo Inc. - Head of IR

Overall, the team has made impressive progress this year in expanding the form of interaction based on audio/video technology and in pushing the ways we connect people beyond physical proximity. With these changes happening, we have a chance to serve the users that we were not able to serve well in the past. In the coming 2 quarters, one of our key strategies is to leverage new use cases and go after the huge amount of dormant users, pull them back through effective channels and see if we can better retain them. In addition, the booming growth of audio and video interactions also leave bigger room for us to build richer monetization features and drive business growth beyond live streaming shows. Throughout the year 2018, we've seen an acceleration in the growth of the VAS line. We are seeing a great deal of potential here, and we'll continue to pursue these opportunities in 2019.

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**Yan Tang** - Momo Inc. - Chairman & CEO

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

Other than the changes that we drove to the core Momo application, in 2018, we also completed the acquisition of Tantan. The acquisition has strengthened our leadership and dominance in China's open social space.

Tantan's growth in 2018 was undoubtedly impressive. However, we believe that it has bigger potential to be unleashed, both in terms of user growth and in terms of revenues. Our goal is to make Tantan a new engine for the company in the coming 2 to 3 years.

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**Yan Tang** - Momo Inc. - Chairman & CEO

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**Cathy Peng** - Momo Inc. - Head of IR

Lastly, I would like to finish my speech today by announcing that our board has declared a cash dividend in the amount of USD 0.62 per ADS, which will amount to a total cash payment of approximately USD 128.3 million or 25% of our adjusted net income, in 2018. The dividend payment demonstrates our commitment to delivering shareholder value. Such commitment is backed by our consistent record of earnings growth and strong operating cash flow.

One thing worth pointing out here is that Momo is still a fast-growing company, and we do see many opportunities to further grow our platform and business. However, we have and will continue to be disciplined and selective in pursuing investment opportunities. If there are opportunities that can strengthen our position in the way that Tantan has, we will strive to capture them. But -- and if we continue to generate excess cash flow compared to our need for operation and investment and is seen by our Board of Directors to be in the best interest of our company, we may continue to share our prosperity with the shareholders in the form of future dividends.

Thank you for trusting the Momo team. We look forward to creating and sharing more value to the investors in 2019.

With that, I'm handing over to Wang Li for our business review. Wang Li, please.

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**Li Wang** - Momo Inc. - COO, President & Director

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

Thanks.

Now let me take you through the key things that we've done as well as the future direction for our major business lines.

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**Li Wang** - Momo Inc. - COO, President & Director

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

Firstly, on live streaming, total revenue from live broadcasting business for the quarter was CNY 2.96 billion, an increase of 36% from the same period last year. As pointed out on the November earnings call, the macro headwind and overall consumption weakness have caused us to have a soft October and November. In December, we held a year-end competition event. In the face of the macro uncertainty, we have refrained from utilizing the extreme stimulating measures as we did in 2017. Instead, we focused on the efforts on designing the competition structure as well as innovating the key features to enhance the overall tournament experience. The enthusiasm we saw from the users in December tournament exceeded our expectations, giving us a 7% quarter-over-quarter growth in live broadcasting revenue for Q4 despite a high revenue base in Q3 and the softness in October and November.

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**Li Wang** - Momo Inc. - COO, President & Director

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

As we put the year-end tournament behind, we can now shift the focus towards driving much longer-term structural changes to our system. Last quarter, Tang Yan mentioned that we would like to better cultivate the paying potential of the middle cohort of paying users by introducing more interactive tools into the showroom. In January, we rolled out an interactive gift called Penguin Hitting. When a user sends a traditional gift, it is simply a virtual gift with certain special screen effects. An interactive gift, such as the Penguin Hitting, comes with a game that allows the users to have fun and compete with other users in the same live channel. That way, the users can enjoy themselves even with a limited amount of spending. Data shows that the game very effectively drove the paying activities of the middle cohort of paying users by enhancing their paying experience. For example, during the 7-day Chinese New Year holiday, the tipping revenue from the top 100 paying users only showed a slight uptick. However, the total revenue during the CNY holiday showed a healthy double-digit year-on-year growth. Nearly all of the growth came from the middle- and bottom-layer paying users. That is just one of the examples of how we can innovate to offer better, entertaining experience to our users. As a matter of fact, the team is now working on a series of products and operational adjustments to drive new demand and better paying conversion in view of the new macro environment. As we speak now, some of these plans are already taking to the execution stage. We believe that with these measures gradually taking effect, we will be able to drive steady and healthy growth for live broadcasting business in the year 2019.

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**Li Wang** - Momo Inc. - COO, President & Director

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

Now on our non-live broadcasting line items. Revenue from value-added service, or VAS, continued to ramp up fast and reached CNY 722.4 million in the fourth quarter, a 272% growth on a year-over-year basis. Wang Yu will talk about Tantan's business later, so I'll be focusing on the VAS business for the core Momo part.

Excluding Tantan, Momo's VAS revenue was CNY 499.4 million, a 157% year-over-year increase. For the past 4 quarters in a row, VAS has been accelerating its y-o-y growth rate, driven by the virtual gifting service outside of the live broadcasting channel. When we first launched the virtual gifting service in early 2017, we started with the largest and also the most established use case - the Nearby People. Many users sent virtual gifts to increase their response rate to their greetings. Later on, we expanded the paying use case into interest groups. Since the beginning of 2018, we began to push harder on the virtual gifting business by introducing new gift features and organizing more operational events around the service. At the same time, we also started to test virtual gifting service in some of the new live interactive experiences based on audio and video streaming technology. Now both Werewolf, Quick Chat and Parties are all pretty sizable revenue contributors. All of this led to the outperformance of the virtual gifting business in year 2018.



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**Li Wang** - Momo Inc. - COO, President & Director

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

Going to the year 2019, we do expect the growth of VAS business to continue to outpace other business lines. As compared with live broadcasting business, VAS bears a much lower ARPPU and, therefore, should be more defensive against the macro headwinds. At the same time, the flourishing live interactive experiences based on audio and video technology provide ample room for us to build paid services that add value to the users. One thing worth pointing out here is that although live broadcasting currently represents the big majority of our total revenues, less than 30% of our total DAU actually consume live streaming content. The rest, 70-plus percent, are engaging with other social experiences that have nothing to do with the live talent shows. We believe these users also have strong inclination to pay for value-added services as long as we give them a good reason to do so. In 2019, we would like to see ourselves move a bit faster in experimenting on paying use cases for virtual gifting across the different non-talent-show experiences that we offer on the platform.

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**Li Wang** - Momo Inc. - COO, President & Director

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

Now briefly on mobile marketing business. Mobile marketing revenue was CNY 122.1 million, a 15% year-over-year decrease. The decline was caused by the challenging macro environment as well as the regulatory changes in some of our big ad sectors. Our current expectation is that the macro environment will continue to be tough for mobile marketing business in the year 2019. Therefore, instead of aggressively pursuing growth opportunities here, our strategy is to increase the operating efficiency of the mobile marketing team. We plan to apply the same strategy to the downsized game business in the year 2019.

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**Li Wang** - Momo Inc. - COO, President & Director

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

That's the review of the key business lines. Now let me hand over to Mr. Wang Yu to review Tantan's product and business development. Mr. Wang, please?

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**Wang Yu** - Tantan Limited - Co-Founder & CEO

Thanks. So let me briefly review Tantan's operational and business development in the year 2018 and our plans for 2019. First, an overview of the key metrics for the quarter.

In Q4, the Tantan community continued to grow rapidly. Total paying users reached 3.9 million in the fourth quarter or a quarterly net addition of 300,000, largely driven by the overall user base growth.

Total revenue was CNY 223 million for the quarter, up 36% sequentially, driven by both paying user growth and the rapid increase in ARPPU, which was, in turn, due to the greater adoption of the See Who Likes Me feature.





Now let me briefly review the achievements we made in the year.

First of all, user growth was the number one priority for Tantan in 2018. I'm glad that we delivered very well on that front. The users grew significantly faster in 2018 compared to 2017. The accelerated growth was driven by both an increase in retention and an acceleration in growth in new users. The increase in retention came from the launch in paid users, growth optimizations and algorithm improvements, while the acceleration in growth in new users came from proactive channel strategies and an increase in organic growth as we've become more widespread.

I'm especially happy that we were able to make the value-added services the big driving factor in the growth formula and align the improvements of user experience with increase in the commercial value of our platform.

Next, on monetization. 2018 was the first year of Tantan's monetization. I'm glad that we delivered beyond targets on this front. In January 2018, we launched the VIP subscription service. Because of the high quality of Tantan's user base as well as the right pricing strategy adopted, we were able to quickly grow the paying subscribers to 3.1 million by end of June. Off the success of the VIP service, we launched 2 additional paid features in July 2018 - the See Who Likes Me and the Super Exposure. The See Who Likes me feature significantly improved the paying conversion as well as the ARPPU, giving a boost to revenue growth in the second half of the year. In 2018, we established our AI team, working to improve the algorithm so we can better distribute value in the network.

On the operational front, in Q4, we also started to build the data tracking system to make our user acquisition efforts more effective and ROI driven. We believe there's further room for improvement in the area of marketing efficiency. That will continue to be an area of focus for us in the coming few quarters.

As we look out to the year 2019, user growth remains on top of our priority list. With that said, monetization and revenue growth will be taking an increasing bigger role as we continue to grow.

In order to achieve the goals we set for ourselves in the year, 2 things are crucially important for the team. Firstly, we need to continue to improve the user experiences we offer. We believe that Tantan already offers the best dating experience among dating open services in China. But we believe that there's still a big room for improvement, and our products, engineering and AI teams will relentlessly keep pursuing to optimize our product offerings. We believe that providing a killer product is the best way to take over and dominate not only the Chinese market but other markets as well.

The other thing that we need to get right is the continuous optimization of existing premium features and the launch of new monetization features. In the area of optimizing existing features, our experience is that sometimes, small ideas can make big differences. Throughout last year, our monetization team were able to continuously output optimizations that seem insignificant but were able to significantly boost conversion rates and revenue. Our ability to massively A/B test for best solutions plays a very important part of this success, and we will continue to build on our data and testing platforms this year.

Regarding new monetization features, we'll be testing a number of different models, both subscription based and non-subscription based. The latter is important for us to significantly increase ARPPU and fully unleash the monetization potential of Tantan.

Overall, the year 2018 was a milestone year for -- both for our team and for our users. We look forward to creating more value for our users and the investors in the new year.

With that, I'm passing over to Mr. Jonathan Zhang for financial review. Jon Zhang, please.

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**Xiaosong Zhang** - Momo Inc. - CFO

Thank you.

Hello, everyone. Thank you for joining our conference call today.



Before getting to the financials, starting from this quarter, we changed our reporting currency from U.S. dollar to renminbi to reduce the impact of foreign exchange changes on the company's reported results. Our operation is mainly conducted in China, and all of our revenue is generated locally. Based on the significant fluctuations in currency exchange rates during the past recent periods, we believe financial results presented in RMB better reflect the fundamental performance of our businesses.

The press release issued earlier today contains U.S. dollar translated from RMB amounts using spot rate on December 31, [2018], (corrected by company after the call) just for reference purposes.

In the interest of time, let me go direct into costs and expenses as revenue line items have been covered pretty comprehensively by Mr. Tang Yan and Wang Li.

Our non-GAAP cost of revenue was CNY 2.08 billion, compared to CNY 1.32 billion for the same period last year. Non-GAAP cost of revenue as a percentage of total revenue was 54%, an increase of 2% from Q4 2017. The higher cost base for Q4 2018 was mainly caused by costs incurred in connection with PhantaCity TV variety show and higher payouts from our live streaming business and fast-ramping virtual gifting business under VAS.

On a sequential basis, non-GAAP costs as a percent of revenue decreased around 1 percentage point from 55% to 54% in Q4. The improvement was mainly due to less drag from PhantaCity show and positive contribution from Tantan revenue, partially offset by higher payout ratios from our live streaming business and the fast-ramping virtual gifting business under VAS.

Non-GAAP R&D expenses for the fourth quarter was RMB 193.9 million compared to RMB 107 million for the same quarter last year, representing 5% and 4% of total revenue, respectively. The year-over-year increase reflected our step-up efforts in expanding the engineering talent pool to support our various product initiatives and the consolidation of Tantan as well.

On a sequential basis, non-GAAP R&D expenses as a percentage revenue remained relatively stable. We ended the quarter with 2,147 total employees, of which 432 are from Tantan. The R&D personnel as a percentage of our total employees for the group was 55%. Overall, we feel that in terms of the size of our engineering talent pool, we are in much better position now as compared to the year ago. Looking deeper into 2019, our efforts will be shifted to mainly focusing on optimizing the structure of it and to improve the talent pool quality. Therefore, we do expect the pace of our overall headcount growth to meaningfully reduce in 2019 comparing to 2018.

Non-GAAP sales and marketing expenses for the fourth quarter was CNY 557.3 million or 14.5% of total revenue compared to CNY 353.8 million and CNY 502.8 million or 13.8% of total revenue for the same period last year and third quarter 2018, respectively.

On a year-over-year and sequential basis, the increase in the sales and marketing expenses as a percent of revenue was mainly due to the consolidation of Tantan, while the core Momo business continued to gain operating leverage on the sales and marketing side.

Our non-GAAP G&A expenses was RMB 133 million in the fourth quarter 2018, RMB 39.3 million higher than the RMB 93.8 million in the third quarter 2018. The sequential increase was mainly because that we recorded RMB 30.3 million one-off write-down of a prepayment related to PhantaCity project, which we currently expect we would not be able to benefit in the future period.

Non-GAAP operating income was RMB 1.03 billion, up 30% year-on-year from RMB 790.6 million, representing approximately 27% non-GAAP operating margin for the quarter.

Now turning to the balance sheet and cash flow items.

As of December 31, 2018, Momo's cash, cash equivalents and term deposits totaled RMB 11.3 billion compared to RMB 6.9 billion as of December 31, 2017. Net cash provided from operating activities during the first quarter 2018 was RMB 1.16 billion, compared to RMB 790.8 million for the same quarter last year.

Lastly, turning to the first quarter 2019 revenue guidance.

We estimated our first quarter revenue to come in a range from RMB 3.55 billion to RMB 3.65 billion, representing an increase of 28% to 32% year-on-year or a decrease of 8% to 5% quarter-over-quarter. Such estimates is based on assumptions that VAS business will increase on a sequential basis and live broadcasting and advertising business are going to decrease quarter-over-quarter due to the seasonality around Chinese New Year. Please be mindful that this forecast represents the company's current and preliminary view based on the market condition and operational status which are subject to changes.

That concluded our prepared portion of our -- today's discussion. With that, let me turn the call back to Cathy for Q&A. Cathy, please.

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**Cathy Peng** - Momo Inc. - Head of IR

Yes. (Operator Instructions) .

Operator, we are ready. Please take the first person in.

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## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) Your first question comes from the line of Thomas Chong from Crédit Suisse.

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**Thomas Chong** - Crédit Suisse AG, Research Division - Regional Head of Internet

(foreign language) I have 2 questions. My first question is about any update on the macro impact to the live broadcasting business. How should we think about the 2019 revenue outlook as well as the monetization strategies? And my second question is about our thoughts on overseas expansion.

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**Yan Tang** - Momo Inc. - Chairman & CEO

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

Firstly, I'm going to talk about our view on the macro impact. Our current view is that macro is probably still going to stand out as a risk factor to the pace of revenue growth this year. However, right now, we are seeing some favorable policy getting rolled out at a macro level. So we'll see how it goes as we move deeper into the year. As the company, we tend to focus on the things that we have control on, and these are the product and operational levers that we have in hand. By pulling these levers in the right way, we still see a lot of growth opportunities here. For example, the operational effort that we put into the year-end gala event had a clear impact in driving the tipping consumption from the top users. Immediately -- and also immediately after that competition event, we also quickly rolled out the interactive gifts to stimulate the middle cohort, and we were able to see almost immediate positive impact in that cohort in January and also during the Chinese New Year period. If you look at the Q4 revenues on an ex-Phanta basis, the revenue in Q4 grew 10% on a sequential basis. And if you look at our Q1 guidance, although we are making relative prudent assumptions on the performance from the top users, our guidance is still indicating a year-on-year growth -- a pretty satisfactory year-over-year growth rate.



**Yan Tang** - Momo Inc. - Chairman & CEO

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

For the whole year 2019, there are several directional stuff that I can -- I like to share with you guys here. Number one, for our live broadcasting business, the team needs to focus on cultivating new demand through product and operational efforts. At the same time, we are also looking to do a better job in converting the problem traffic into live streaming paying activities. For example, we now see a clear mismatch on the platform, where, on the one hand, we have a lot of users having difficulty in finding effective interactions. On the other hand, we also have tons of small long-term broadcasters or entry-level broadcasters who cannot find enough traffic support, so when they go live, they essentially have no audience in their channel. That is a problem that can be better addressed by making our traffic dispatching system better. And then the other opportunity that we see is that in some local areas in China, we feel that there are still a lot of wealthy people who have the potential to become our high-paying users that have actually never touched Momo's live broadcasting service before. So these are examples of the opportunities that we have this year and will continue to pursue. Our other planned initiatives will include several things that I can talk about here. Number one is the continuing introduction of new product features into the live showroom. And number two is the revamp of the broadcasters' ranking system to provide better motivation. And number three is the adjustment to the platform algorithm to support better live streaming conversion. And lastly, we do have some off-line commercial events to drive new paying users into live broadcasting. These strategies will get rolled into the system step by step in the coming 2 quarters.

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**Yan Tang** - Momo Inc. - Chairman & CEO

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

And the second focus of ours on monetization side is that VAS and Tantan, as mentioned before, these 2 business lines tend to be more resilient in a macro headwind. And as compared with live broadcasting business, these 2 currently do not monetize as deep. So we actually see a lot of growth potential in driving the paying activities from the middle towards longer-tail paying users. But to unlock the values in these cohorts of users, we need richer monetization features and more diversified paying use cases for our VAS service. For example, recently, we took the ideas from some of the Japanese and Korean TV dating reality shows, and we applied these ideas into building new gamifications in the VAS service and created a new party experience, moderated the party experience to replace the old one. Right now we are seeing very positive data in terms of user engagement and also paying activities. So far into Q1, despite of the negative impact from Chinese New Year, our own VAS business and Tantan are all showing very strong growth momentum on a sequential basis. So throughout the year 2019, that's going to be an area that we will be pushing very hard on, which is to experiment on more of these new VAS experiences. Right now we are seeing plenty of monetization potential for our Quick Chat and Parties experience, the chat room experience and also Tantan. We believe that the revenue contribution from VAS and Tantan as a percentage of total is going to see pretty significant increase in the coming couple of years.

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**Yan Tang** - Momo Inc. - Chairman & CEO

(foreign language)

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**Cathy Peng** - Momo Inc. - Head of IR

For Momo, we have been looking at the overseas expansion -- we have been keeping an eye on overseas expansion opportunities and making regular assessment from time to time. And in doing so, we generally have 2 guiding principles. One is that there has to be a proven business model.

And the second one is that it has to be something that fits into the forte of our team. Right now on Momo side, we do not have any definitive plan, but Tantan may have a more specific opportunity that it would like to pursue. I'll pass on to Wang Yu to elaborate a little bit.

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**Wang Yu** - *Tantan Limited - Co-Founder & CEO*

Okay. So regarding Tantan's overseas strategy, so while China is still our focus, we do, in fact, already have a pretty sizable overseas user base. We do see the overseas market, especially Eastern markets, as a big growth opportunity for Tantan down the road. We believe Tantan has a significant competitive advantage in our operational fit for the Eastern cultures.

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**Operator**

Your next question comes from the line of Jialong Shi from Nomura.

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**Jialong Shi** - *Nomura Securities Co. Ltd., Research Division - Head of China Internet & Media Research and VP*

And I have 2 questions here I -- first, I will first ask my question in Chinese then translate it into English. (foreign language)

I have 2 questions here. My first question is a follow-up question on live broadcasting. Management mentioned on the -- during the prepared remark Momo actually has a few new features to be added into the live broadcasting service which are similar to the Penguin Hitting feature added last quarter. So I just wondered if management can provide more details on those upcoming new features. And my second question is about Tantan. We understand Tantan's revenue in 2018 was mainly driven by premium membership. So I just wonder how we should assess the monetization level for this premium membership model. And management mentioned during the prepared remark Tantan is currently testing a few new monetization models, and I just wonder if management can provide more colors on those upcoming monetization models and also when those model are likely to be rolled out.

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**Li Wang** - *Momo Inc. - COO, President & Director*

(foreign language)

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**Cathy Peng** - *Momo Inc. - Head of IR*

The growth of the VAS business has largely been driven by the virtual gifting service in the past 2 years, which mainly involved users sending each other virtual gifts in the non-live broadcasting use cases to enhance the overall social experience. In terms of DAU penetration, the order of ranking among different stand-alone use cases on the platform goes like this. The biggest one is Nearby People and then it's live broadcasting and Diandian the chat room experience and interest group. Quick Chat and Parties, Werewolf, these are relatively smaller use cases in terms of DAU penetration. Quantitatively, live broadcasting represents a bit less than 30% of total DAU, and the rest of the social experiences represents 70% collectively. That's why we actually think that the non-live broadcasting use cases provide a long runway to ramp up the virtual gifting service. Virtual gifting is a model that has been proven by multiple consumer experiences like Nearby People, interest group, Werewolf, Quick Chat and Parties. Right now, based on the existing use cases, our VAS is still ramping up -- the VAS revenue is still ramping up very fast. And this year, we do have the plan to start testing monetization features in the chat room experience. And chat room experience, as said before, is a relatively bigger use case. In terms of total time spent, it's already half as big as the live broadcasting service, and the -- which, like the live audio interactions and the karaoke feature within the chat room experience, also provides pretty rich channel to build diversified paying use cases. So we do believe that it has the potential to become a pretty meaningful driver for VAS down the road. However, because we really haven't monetized the chat room experience in any big way in the past, this year we may need to allow the team some time for trial and error. And Tantan?



**Wang Yu** - *Tantan Limited - Co-Founder & CEO*

Okay. Okay. So generally, we believe that the -- our potential for dating in China is as high if not higher than the West. But we probably need to use some -- besides subscription-based models, use some non-subscription-based models to fully unleash the -- our potential. With that said, so far into Q1, we have been outperforming our own expectations on user growth by quite a lot. As an indication, we expect that the quarterly add-on and paying users to increase very significantly from the 300,000 net add that we saw in Q4 and even surpass that of the net add in Q3. We are testing a number of different new premium features. Some of them are subscription based and others are not. When we feel that we're ready, we'll do an official launch. But we will take our time in testing features to make sure we do things right.

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**Operator**

Your next question comes from the line of Daniel Chen from J.P. Morgan.

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**Qi Chen** - *JP Morgan Chase & Co, Research Division - Research Analyst*

(foreign language) I will translate myself. So my question is for Jonathan. So how should we look at Momo's margin profile in 2019? So -- and any place that we can -- we are going to see the operating leverage for the whole company?

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**Xiaosong Zhang** - *Momo Inc. - CFO*

Thank you. Actually, as a public company, we don't provide specific margin guidance for the coming year. But however, based on the -- what Tang Zong just discussed, we feel confident that our revenue will continue to grow from live streaming, faster pace of revenue ramp from our VAS business and also Tantan's business. So definitely, we're going to be very carefully to manage our cost structure. As we communicated in the past, we feel that the current level of revenue sharing is adequate to the agencies and the broadcasters. We do not have a plan to significantly increase the payout ratio. That's probably we're going to continue in 2019. And then there are other factors in the cost components. Since the virtual gifting business under VAS ramps up quickly, it could provide additional drag on the gross margin side. And also, Tantan's business will -- as the revenue ramps, it's going to positively impact to the gross margin. So we're going to carefully manage that. In 2019, with no Phanta impact, which is a positive factor, so we do see there's a potential. We hope that our gross margin will improve based on the 2018 level. And based on the current macro condition, as I said during the earnings call -- during the prepared remarks, we're going to be very disciplined in terms of headcount control, mainly focusing on optimizing the talent pool quality. And the only incremental area would be the selling, marketing expense to support Tantan's user growth. On the core Momo side, we're going to continue on the discipline side to generate operating leverage. So overall for 2019 on the operating margin side, we definitely hope that we can achieve similar level of profitability comparing to [2018] (corrected by company after the call) on a consolidated basis.

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**Operator**

Your next question comes from the line of Tian Hou from T.H. Capital.

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**Tianxiao Hou** - *T.H. Capital, LLC - Founder, CEO & Senior Analyst*

(foreign language) Okay. So Momo has been proven -- has a deep understanding of China's social connection market and proven by the successful acquisition, integration, monetization of Tantan and its own Momo app. So if we can -- if we use Match Group in the U.S. as a comp company and we see Match growth has many apps, each app targeting one particularly social connection desire and particular group, so I wonder, what's the future strategy for Momo? You want to do the APP (sic) [app] internally or externally? You want to have just existing 2 apps or develop more apps? So what's the future strategy? That's my question.



**Yan Tang** - Momo Inc. - Chairman & CEO

(foreign language)

**Cathy Peng** - Momo Inc. - Head of IR

Well, first of all, thank you for your compliment on Momo's management team in the specific open social space. My view toward your strategic question in that specific space is that in the open social territory, it's hard to find a one-size-fits-all kind of solution to satisfy all the specific vertical demands in some specific demographic or form of interaction or in some specific market. So we probably need multiple solution to keep penetrating deeper into the market. As a matter of fact, since last year, we've actually already stepped up our efforts in self-developing new products to satisfy new demands and new demographic, and we've actually launched a few projects and new applications last year. But -- and we will continue to try to go in deeper on that front this year. We also have some plans for stand-alone application developments down the road. However, because that is a new area for the company, so we probably also need to allow some trial-and-error time for the team. And lastly, other than self-development of new products, we also do not want to rule out the possibility of getting into new areas through M&A or partnering with other people in some new projects. That was also an area that we've already got into in the year 2018. That's still one of the -- one of our strategies in the coming year as well. So that's the answer to your question.

**Operator**

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

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