

Cheetah Mobile Inc.
Q4 and Full Year 2020 Earnings Conference Call
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Officers and Speakers

Helen Zhu, Director, Investor Relations
Fu Sheng, Chairman and Chief Executive Officer
Thomas Ren, Chief Financial Officer

Analysts

Vicky Wei, Citi
Melody Chan, Jefferies

Presentation

Operator: Good day, and welcome to the Cheetah Mobile Fourth Quarter and Full Year 2020 Conference Call. (Operator Instructions). After today's presentation, there will be an opportunity to ask questions. Please note this event is being recorded.

I'd now like to turn the conference over to Helen Zhu, Investor Relations Director of Cheetah Mobile. Please go ahead, ma'am.

Helen Zhu: Thank you, operator. Welcome to Cheetah Mobile's fourth quarter and full year 2020 earnings conference call.

With us today are our company's Chairman and CEO, Mr. Fu Sheng, and our company's CFO, Mr. Thomas Ren. Following management's prepared remarks, we will conduct a Q&A section.

Before we begin, I refer you to the safe harbor statement in our earnings release, which also applies to our conference call today, as we will make forward-looking statements.

At this time, I would now like to turn the conference call over to our CEO and Chairman, Mr. Fu Sheng. Please go ahead, Fu Sheng.

Fu Sheng: Thank you, Helen. Hello, everyone. While the macro environment remains challenging, with focus and determination, Cheetah Mobile improved operational efficiency, diversified our revenue streams beyond advertising, and stayed focused on the domestic market. In 2020, we earned RMB1.6 billion in revenues and RMB417 million in net income attributable to our shareholders, as our business began to take hold. Meanwhile, we remained committed to our AI-related robotic business to build sustainable growth for Cheetah Mobile in the long run.

Here are the operating highlights. First, we cut our costs and expenses. As a result, non-GAAP operating loss continued to narrow since Q4 2019. In the fourth quarter of 2020, non-GAAP

operating loss was RMB57 million, reduced from RMB204 million in the same period last year and RMB119 million in the previous quarter.

Specifically, our Internet business earned about RMB76 million in non-GAAP operating profit in the fourth quarter of 2020, compared to an operating loss of RMB92 million in the same period last year and an operating profit of RMB71 million in the previous quarter.

Thanks to our continued operational optimization, Cheetah Mobile still held US\$255 million at hand, despite that we paid US\$200 million cash dividends to our shareholders in 2020. Looking ahead, we will continue to cut our costs and expenses and improve operational efficiency.

Second, through offering membership services within our utility products, we diversified our revenue streams beyond advertising in 2020. We put user experience, user satisfaction, and our user privacy protection as our top priorities in our home market. Our goal is to improve the user retention rate and attract more users through word-of-mouth.

In the domestic market, we continued to encourage users to subscribe for an ad-free experience. Such initiative helped us reduce reliance on advertising and allowed our utility products to deliver a superior experience. As a result, both paying user count and subscription revenue continued to grow in 2020, and we expect these metrics to continue the growth trend in the future. Supported by the membership services and our efforts on enhancing user experience, we expect revenues from our key Internet business to gradually stabilize, and resume quarter-over-quarter growth in the coming quarters.

Third, we optimized our operation for our AI business by focusing on a selected number of use cases. One of them is deploying our AI-robots in shopping malls. Covid-19 in China has been well controlled, and the Chinese economy has recovered. Our AI-related robotics can help shopping mall operators better serve their customers, and help brands and shops promote their products and services. While our AI business is still in its early stage, we believe we are on the right direction of our business.

Before I turn the call to Thomas for financial highlights, I would like to emphasize our strong cash reserves and our consistent shareholder returns. In 2021, we will continue to cut our cost and expense, and experiment more monetization models for our AI business to rebuild a sustainable growth model for the long term.

With that, I will now turn the call to our CFO, Thomas Ren, to go through the details of our fourth quarter financial results.

Thomas Ren: Thank you, Fu Sheng, and good day, everyone. Thank you all for joining us today. Now, I will walk you through our financial results. Please note that unless stated otherwise, all money amounts are in RMB terms.

In the fourth quarter of 2020, our total revenues were RMB271 million, within our revenue guidance. It represented a year-over-year decrease of 56%. The year-over-year decline was primarily due to the suspension of our collaborations with Google since February 2020, as well as the disposal of certain gaming-related business and assets.

On February 21, 2020, Cheetah Mobile announced that the Company's Google Play Store, Google AdMob, and Google AdManager accounts had been disabled, which negatively affected its ability to attract new users and generate revenue from Google. Given the unfavorable environment in the overseas markets, we have chosen to shift our focus from overseas markets to the domestic market. In the second half of 2020, the Company disposed certain gaming-related business and assets in the overseas markets. As a result, we expect that revenue contribution from the mobile game business to decrease in the foreseeable future.

Post such disposals, Cheetah Mobile's business primarily comprises of 2 pieces. One is the Internet business, which includes our utility products on both the PC and mobile platforms in the domestic market and a remaining and diminishing portion of the mobile game business. The other is the AI and other businesses. Therefore, we started reporting our revenues and operating profits by the above 2 business lines from this quarter. We have retrospectively revised segment information from the previous periods to be comparable with the current period.

Revenues from the Company's Internet business decreased by 56% year-over-year to RMB257 million in the fourth quarter of 2020 due to the above-mentioned factors. In the fourth quarter of 2020, nearly 74% of the Company's revenues from its Internet business were generated from utility products, while the remaining came from the diminishing mobile game business. In the future, we expect revenues from our utility products to account for a vast majority of this reporting segment.

Revenues from AI and others were RMB14 million in the quarter, representing a year-over-year decrease of 50%, mainly due to a decline in consumer-facing AI-related products.

Turning to our fourth quarter of 2020 costs and expenses, the following discussion of results will be on a non-GAAP basis, which excludes stock-based compensation expenses and goodwill impairment. The use of non-GAAP measures in this context will help us to better present the results of our operating performance without the effect of non-cash items. For financial information presented in accordance with U.S. GAAP, please refer to our earnings release.

In the past several quarters, we continued to streamline our operations and cut our costs and expenses. In the fourth quarter of 2020, total costs and expenses decreased by 61% year-over-year and 33% quarter-over-quarter. As a result, our operating loss significantly narrowed to RMB57 million in the quarter, from RMB203 million in the same period last year and RMB119 million in the previous quarter.

Notably, the operating profit for the Internet business was RMB76 million in the fourth quarter of 2020, increased from an operating loss of RMB92 million in the same period last year, and an operating profit of RMB71 million in the previous quarter due to our cost and expenses cutting.

As of December 31, 2020, Cheetah had about 1,050 full-time employees, decreasing by about 50% from the end of 2019.

In 2020, our total operating expenses decreased by 44%. In 2021, we will continue to cut our costs and expenses, particularly sales and marketing and personnel-related expenses.

Turning to non-operating items, during the quarter, the fair value of some of our investees

increased. As a result, we reported a net income attributable to Cheetah Mobile's shareholders of RMB85 million in the fourth quarter.

Importantly, our balance sheet remains strong. As of December 31, 2020, we had cash and cash equivalents, restricted cash, and short-term investments of US\$255 million and long-term equity investments of US\$369 million. Our strong balance sheet gives us the confidence to continue to invest in the AI-related business to rejuvenate long-term growth for the Company.

And for our first quarter revenue guidance, we currently expect total revenues to be between RMB165 million and RMB215 million.

Please note, this forecast reflects our current and preliminary views and is subject to change.

This concludes our prepared remarks. Operator, we are now ready to take questions.

Questions and Answers

Operator: Thank you. We will now begin the question-and-answer session. [Operator instructions]. Vicky Wei with Citi.

Vicky Wei: My question is about the advertising market and the AI robot. So what does management think of the current advertising market sentiment going into the first quarter 2021? And what was the top 3 key advertising verticals for fourth quarter?

And my second question is post the pandemic, does management witness any behavioral changes in habits in terms of adoption of AI robots? Any color about the progress of Cheetah Mobile's AI robot adoptions will be great. (Speaking foreign language).

Thomas Ren: Thank you, Vicky. So I will answer your first question about the general advertising market, and Fu Sheng will answer your second question.

So for the advertising market, it seems that COVID-19 pandemic is now already under control in China. We can see a strong recovery trend of the macro-economy in China, which in turn lead to a recovery to advertising market as well. So specifically, for a few sectors like FMCG, auto gaming and education, I think those few sectors will maintain a strong growth momentum. And also we can see the recovery from the travel and entertainment sectors from last year.

But I also want to call your attention that, well for us, as we mentioned in the prepared remarks, we are now defocusing our reliance on advertising, while we are developing the user subscription model. So we expect we can see more contribution from user-contributed revenue for our domestic utility products. I hope this answers your question.

So I will turn to Fu Sheng to answer your question about AI.

Fu Sheng: (Speaking foreign language).

Thomas Ren: Okay. I will translate this part. So after the COVID-19 pandemic, we indeed noticed that there are a lot of business customers. Their acceptance level for the AI robotics are accelerating and also it benefits us from the past few years. We continue to invest on AI technologies including our investee OrionStar to reduce the cost of the robotics, so we can feel that the [whole] market acceptance to the AI robotics is becoming much more than before.

Fu Sheng: (Speaking foreign language).

Thomas Ren: Okay. So I will translate this part. So for an example, our robotics in the shopping mall, along with the traffic in the shopping mall, is recovering. We can see in more and more shopping mall, the interaction with our shopping mall robotics is increasing. So some customers already are used to asking our robotics about where to find certain brands of coffee, or certain brands of restaurants and where is the toilets, etc. So we are seeing that more and more customers in the shopping mall used to such kind of inquiry to our robotics.

Another example is robotics in restaurants promoted by our investee OrionStar again. So toward the end of 2020, OrionStar promoted restaurant service robotics. The monthly rental OrionStar is collecting from [one] restaurant is less than RMB2,000. And actually, this cost is already lower than a common waiter's cost. And the efficiency on the delivery is already enough to substitute a waiter. And just in a couple of months, OrionStar already entered into a few hundred restaurants, which they rent the restaurant robotics.

So especially after the COVID-19 pandemic, and also our continuing investment into the AI technology, I think we already reduced our cost to a level that could be accepted by the market. And also we can see the untouched service and also the service with fewer face-to-face communication is also gradually accepted by the market. So we think it's a right timing; we can benefit from the market acceptance.

So that's all Fu Sheng's response. Hope it answers your question, Vicky.

Vicky Wei: Thank you very much.

Operator: [Operator instructions]. Melody Chan with Jefferies.

Melody Chan: So I have two questions. The first is can management share some views on 2021 outlook across different sectors?

And my second question is so Apple recently increased its privacy control and all the app developers are required to have the approval from users to use data. So will this impact advertising business? (Speaking foreign language).

Fu Sheng: (Speaking foreign language).

Thomas Ren: Okay. So I will translate this part. So Fu Sheng was talking about the outlook for our own business. So first, as we mentioned just now, I think we met great challenge in the overseas market last year. So the strategy for us in the prior year was to return to our home

market, which is domestic market. And now it seems that our domestic mobile Internet business, not only we stabilize our revenue level and also we expect we can regain some growth in this year. And the growth is not only coming from the advertising and also coming from our user subscription model. And we believe for the Internet segment, we can see a recovery trend in this year.

Fu Sheng: (Speaking foreign language).

Thomas Ren: So Fu Sheng was talking about in the coming year, we can see more severe competition for the whole Internet industry. And for us, our utility products can not only to do some functional features, and also we need to connect, to be connected, with content and community or the cloud functions. And then we can regain some energy for our utility software.

Fu Sheng: (Speaking foreign language).

(Translated). Okay. So as I just said, for the AI and the robotics industry, I think it is now the turning point. Although you can see some not -- some AI company, they are not doing great, or is not smooth for them to either to new round financing or the IPO. But I think, generally, it's not a bad thing for the whole industry. And for the AI and the robotics business, it's not only about some certain technology indicator, or you published some essays or win some prize on some competitions as a just standard.

So I think now, it has been turning to stage that the product should be the core feature. And as long as your product can meet your customers' needs, and also to reduce customers' actual cost and to leverage or improve the users' experience, I think that's the core energy for the AI products.

Yes, I think the obvious phenomena we can see is for the robotic products, previously, it depends highly on some governance purchase but -- or to use the robotics in some exhibition. But now, it has been converted to a wider use at either the restaurants or hotels as an efficient, more efficient, tool. So I think I'm quite confident that this industry will grow very fast.

Yes, for your second question about the new policy by Apple, I think basically, it has a very minimum effect on our utility products because our utility apps or products mainly are on either Android or PC platforms. And also for our overseas gaming products, we already, as we mentioned, we already disposed certain overseas gaming products. So for the Apple policy itself, there is a very minimum impact on us.

I also want to emphasize that another outlook is about no matter the overseas market or domestic market, now it's becoming more and more important for the users' privacy information. It requires more and more focus for the old apps developers. We can see from the recent March 15 [Gala] by CCTV, either the fraud advertisement or disruptive advertisement is also becoming a focus by government.

For the whole industry, I think in the future, the advertisement with low quality or violating some user price information, it will be controlled more and more strict by either the government or mobile phone manufacturers. So when we were facing some challenges from either Facebook or Google in the last year, or the year before, so we already realized that the user experience and

also the low-quality advertisement issue. So we are already in 2020, we already start to reduce our advertisement and also to reduce our reliance to advertising. So we developed the user subscription model.

I think it improves our user experience and so in the -- we just mentioned now the CCTV Gala. So there is no Cheetah Mobile product was involved. I think it has a big relation, or a great relation, with our change on our business model for our utility products. Thank you.

And also I want to supplement a little bit about our outlook for 2021 because I want to emphasize that because first, we were terminated by Google last year. And also secondly, we already disposed certain gaming-related products or business in the second half of 2020. So I think generally, for our full year outlook, I think we will still see a decrease trend for the full year revenue. But we are confident that since Q2 -- because Q1 is always a slack season for advertising. So I think we can expect some recovery from our revenue price in Q2. So that's my supplement information. Okay. Thank you.

Operator: Thank you. And there are no further questions. So at this time, I'd like to turn it back over to our management team for final remarks.

Helen Zhu: Thank you all for joining us today. If you have any further questions, please do not hesitate to contact us. Thank you. Bye.

Operator: Thank you. This concludes today's conference call. Thank you all for attending today's presentation. You may now disconnect your lines.