

**CooTek Inc. [CTK]
Fourth Quarter and Fiscal Year 2018 Earnings Conference Call
March 7, 2018**

Company Representatives:

Christian Arnell; Christensen & Associates; IR
Karl Zhang; CooTek Inc.; Chairman and Chief Architect
Jean Liqin Zhang; CooTek Inc.; Chief Financial Officer

Analysts:

Alicia Yap, Citigroup
Gregory Gu, Credit Suisse
Emerson Chan, Bank of America Merrill Lynch
Hans Chung, KeyBanc Capital Markets

Presentation:

Operator: Good day, and welcome to the Cootek Fourth Quarter and Fiscal Year 2018 Earnings Conference Call. All participants will be in listen-only mode. (Operator Instructions). After today's presentation, there will be an opportunity to ask questions. (Operator Instructions). Please note this event is being recorded.

I would now like to turn the conference over to Christian Arnell. Please go ahead.

Christian Arnell: Thank you. Hello, everyone, and thank you for joining us today. Our earnings release was distributed earlier today and is available on our IR website at ir.cootek.com and on PRNewswire.

On the call today from Cootek are Mr. Karl Zhang, Chairman and Chief Architect, and Ms. Jean Liqin Zhang, Chief Financial Officer. Mr. Zhang will review business operations and Company highlights, followed by Ms. Zhang, who will discuss financials and guidance. They will both be available to answer your questions during the Q&A session that follows.

Before we begin, I'd like to kindly remind you that this conference contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements are made under the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995.

These forward-looking statements can be identified by terminology such as "will," "expects," "anticipates," "future," "intends," "plans," "believes," "estimates," "confident" and similar statements.

CooTek may also make written or oral forward-looking statements in its reports filed with, or furnished to, the U.S. Securities and Exchange Commission, and in its annual report to shareholders, in press releases and other written materials and oral statements made by its officers, directors or employees to third parties.

Any statements that are not historical facts, including statements about CooTek's beliefs and expectations, are forward-looking statements that involve factors, risks and uncertainties that could cause actual results to differ materially from those in the forward-looking statements.

Such factors and risks include, but are not limited to the following: CooTek's mission and strategies; future business development, financial conditions and results of operations; the expected growth of the mobile internet industry and mobile advertising industry; the expected growth of mobile advertising; expectations regarding demand for, and market acceptance of, the Company's products and services; competition in the mobile application and advertising industry; and relevant government policies and regulations relating to the industry.

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.

All information provided on this call is current as of the date of this call, and CooTek does not undertake any obligation to update such information, except as required under law.

It is now my pleasure to introduce Mr. Karl Zhang. Mr. Zhang, please go ahead.

Karl Zhang: Thank you. Thank you, everyone, for joining our fourth quarter and fiscal year 2018 earnings call. We are excited about the progress we made during the fourth quarter of last year.

Q4 revenue reached US\$47 million and, remarkably, the DAU of our content-rich portfolio products exceeded our expectations by reaching nearly 17 million in December 2018, up 54% quarter-over-quarter, and contributing nearly 70% of total revenue.

It only took us 5 quarters to grow our portfolio products' DAUs from less than 1 million to nearly 17 million while maintaining profitability. Considering the relatively short 2-year history of our portfolio products, we are very proud of this result and are confident that we can continue to gain growth momentum.

Our revenue for the full year reached US\$134 million, up 259% from 2017.

We hit a critical milestone in 2018. We believe that the global content app market is promising, and we are on the fast-track to take advantage of these great opportunities to become a market leader. As a market leader, we will be able to realize greater financial benefit in the future. That's why, as I emphasized on the last quarter's earnings call, we set growing our user base rapidly, especially the DAUs of our content-rich portfolio products, as our first priority at this stage.

We are very happy to see such strong DAU growth in the fourth quarter, which exceeded our expectations, and will allow us to maintain our leading market position.

The fast-growing DAUs also demonstrates the effectiveness of our strategy to be an AI-driven

global content delivery platform.

By leveraging our in-depth user insights and established systematic user growth approach, we acquired new users for our content-rich portfolio products more aggressively than we did in the third quarter, and still kept the average user acquisition unit cost relatively stable. We believe that this demonstrates the sustainability of our user growth capabilities.

Aside from acquiring new users, and in order to accumulate DAU even faster, we have been focusing our efforts on improving our products. We made very good progress on the product side since Q4 2018.

Our portfolio app Cherry, which provides female-oriented content in its news feed including posts, articles and short videos, was released on iPhone and demonstrated an impressive user retention rate. It now ranks as one of the most popular lifestyle apps on the AppStore in the U.S. Cherry's success on iPhones demonstrates our product development capabilities and the potential our systematic user growth approach has.

Breeze, our meditation content app, was also released on iPhone. We are also incubating a number of new content-rich apps to capture mobile internet users' ever-evolving content needs.

At the same time, we have also devoted significant resources towards optimizing the user experience, content recommendation quality and ad load of our existing products to continuously improve user engagement and user retention. The user engagement, which is DAU over MAU, of our portfolio products improved significantly from 33% to 37%. The 2nd month user retention rate improved as well.

In summary, with all these efforts on user acquisition, product improvement and optimization, DAUs of our portfolio products grew from 11 million to 16.9 million, up about 54% sequentially, beyond our original expectation of about 14 million with strong financial outcomes.

Our super app, TouchPal Keyboard, continued to gain growth momentum. The average DAUs of TouchPal Keyboard were 140.8 million in December 2018, an increase of 38% year-over-year.

In the fourth quarter of last year, we signed a pre-load contract with LG under which LG is going to pre-load TouchPal on some of their smartphone devices. We consider TouchPal Keyboard as a strategic asset, as it contributes very unique value to our fast-growing portfolio products.

With that, I will hand over the call to CFO Jean to walk you through the financial results for the quarter.

Jean Zhang: Thank you, Karl, and thanks, everyone, for joining us on the call today. I'm going to walk you through our fourth quarter financial results and a few key 2018 financial results.

All comparisons are on a year-over-year basis unless otherwise noted.

Now, let's start with users. We ended December with approximately 237 million people using our global products, up 50% from a year ago. Approximately 158 million people accessed our global products each day on average in December, up 50% from the prior year.

Monthly active users on portfolio products reached 46.1 million in December, up 3.9 times from a year ago. Average Daily active users on our portfolio products in December reached 16.9 million, up 4.8 times compared to last year.

Average daily active users on TouchPal Smart Input in December were approximately 141 million, up 38% from last year. This number represented about [54]% of 191 million monthly active users. The MAU was up 29% compared to last year.

Total revenue in the fourth quarter was up 147%, while ads revenue was up about 164%. We continued to see a positive impact from our investments in user growth and ad monetization.

We estimate that, of the total advertising revenue for the fourth quarter of 2018, portfolio products contributed approximately 70%; TouchPal Smart Input contributed approximately 20%; and TouchPal Phonebook contributed approximately 10%.

With a fast-growing portfolio products user base, and the sizeable percentage of total revenue they contributed, we have realigned resources internally to focus more on growing our content-rich portfolio products. So we expect that the contribution from portfolio products will increase in the future, and with this shift in our focus, we expect revenue from TouchPal Phonebook will decrease as a percentage of total revenue.

Now, turning to expenses, our Q4 GAAP cost and expenses were US\$43 million, an increase of [100]% from last year.

Cost and expenses accounted for 91% of revenue, an improvement from 113% last year and flat sequentially.

We achieved portfolio products DAU growth of 4.8 times year-over-year, and of 53.6% sequentially with sales and marketing expenses up 2.2 times year-over-year and 40% sequentially. DAU also grew at a faster pace than sales and marketing expenses. The sequential and year-over-year increases in sales and marketing expenses, as a percentage of total revenue, were primarily due to an increased investment in our user acquisition.

We ended the quarter with 498 full-time employees, up 30% from last year and 10% from last quarter.

R&D employees represented 62% of total employees, compared to 60% last year.

During the fourth quarter, we received about US\$1.5 million in government subsidies as one-time reward for our successful IPO, which we used these funds as a one-time bonus for our employees to thank them for excellent achievement and a successful IPO in 2018.

Our gross margin was 93%, up from 91% last quarter and 73% during the same period last year.

We had GAAP net income of US\$4.1 million, representing an 8.7% net profit margin.

Excluding the impact of stock compensation, adjusted net income was approximately US\$4.9 million, representing a 10.4% non-GAAP net profit margin.

We generated US\$13.3 million from operating activities, an increase of 153% compared to US\$5.3 million during the last quarter, and compared to outflow from operations of US\$1.2 million for the corresponding period in 2017.

I will now quickly run through a few key full year 2018 financial results. Further details can be found in the earnings release.

Net revenue for the full year 2018 was US\$134 million, an increase of 259% from US\$37 million in 2017.

Mobile advertising revenue for the full year 2018 was \$131 million, an increase of 275% from \$35 million in 2017.

Portfolio products contributed approximately 63%; TouchPal Smart Input contributed approximately 22%; and TouchPal Phonebook contributed approximately 15% of total mobile advertising revenue.

Cost and operating expenses for the full year 2018 was \$124 million, an increase of [100]% from \$61 million in 2017.

Sales and marketing expenses for the full year 2018 were \$80 million, up 3 times year-on-year. As a percentage of total revenue, sales and marketing expenses accounted for 60%, an increase from 54% in 2017, primarily resulting from increased investment in user acquisition.

R&D expenses for the full year 2018 were \$19 million, an increase of 50% from \$13 million in 2017, mainly due to increased costs associated with technology R&D staff. As a percentage of total revenue, R&D expenses accounted for 14%, down from 35% in 2017.

G&A expenses for the full year were \$11 million, an increase of 28% from \$8.4 million in 2017, primarily due to an increase in management staff and administrative teams. As a percentage of total revenue, G&A expenses accounted for 8%, a decrease from 22% in 2017.

Gross margin for the full year 2018 was 89%, compared to 46% in 2017.

Net income for the full year 2018 was US\$10 million, compared to a net loss of US\$24 million in 2017. Adjusted net income was \$12.7 million, compared to an adjusted net loss of \$21.2 million in 2017.

As of December 31, 2018, cash and cash equivalents were \$84.9 million compared to \$29.4 million as of September 30, 2018, and \$26.7 million as of December 31, 2017.

The Company used US\$2.5 million to repurchase 311,000 ADSs in the fourth quarter.

There are no loans outstanding as we repaid all bank borrowings in the third quarter of 2018, and our convertible redeemable preferred shares were converted into ordinary shares in the fourth quarter.

Turning now to the revenue outlook, we expect total revenue in the first quarter of 2019 to be

between US\$40 million and US\$42 million, representing an 82% to 92% increase year-over-year. These estimates reflect the Company's current and preliminary view, which is subject to change. Operator, we are now ready to take questions.

Questions and Answers

Operator: We will now begin the question-and-answer session. (Operator Instructions). Alicia Yap of Citigroup.

Alicia Yap: I have two questions. Number one is related to your first quarter guidance. So I understand there could be some first quarter seasonality, but could you elaborate a little bit the reasons for this kind of lower-than-expected revenue guidance? And how should we be thinking about the overall revenue growth rate for the full year?

The second question is related to the sales and marketing spend. It does look like our fourth quarter sales and marketing spend came in a bit higher than our estimate. Wonder what are the reasons? Is that mainly because of higher channel marketing spend for the new user acquisition? And then if you could also share with us if the sales and marketing budget for 2019, that would be great. Thank you.

Karl Zhang: Thank you, Alicia. I'm going to answer you the first question and then I will hand it over to Jean to answer the second question.

So the first question is about the -- so let me just elaborate a little bit more on our Q1 guidance. So our Q1 guidance reflected our strategic priority, seasonality and (inaudible) shift in focus. Potentially, all of our revenue is generated from mobile apps, but this industry has obvious seasonality. Our guidance is absolutely aligned with most of the mobile internet companies in the same industry.

Secondly, as we mentioned before, with the fast-growing portfolio products user base, and the sizeable percentage of total revenue that contributed, we have realigned the resources internally to be more focused on growing content-rich portfolio products. With this shift in focus, we expect that the revenue from TouchPal Phonebook will shrink.

Our guidance reflects the decrease of the revenue from TouchPal Phonebook, and we believe this is a short-term impact, as our portfolio apps are growing very fast.

Certainly, as I mentioned at the beginning, and in the last quarter's earnings call, we set our first priority at this stage to grow our user base rapidly. We have been taking efforts to improve the user experience, including optimizing ad levels of our product to improve user engagement and the retention rate.

Actually, from late Q3, we started to pass different ad load. In Q4, based on the [tax] results, we decided to reserve some at inventory for future use on our own initiative; although this will impact ARPU, but we believe it is aligned with our strategy. As a result, the unit engagement rate, which is DAU over MAU, of our portfolio products improve significantly from 33% to 37% this quarter. And the second month's retention rate improved as well.

So this helped us to reach outperforming DAU growth, and we are expecting stronger DAU growth this year. We are very satisfied with the balance of current ARPU and the DAU growth rate.

So here, I want to emphasize one point, that the history of our portfolio products is relatively short. We believe that the global content app market is promising, and we are on the fast track to take advantage of this great opportunity to become a market leader. As a market leader, we will be able to realize greater financial benefit in the future.

As for 2019, we are confident that we can achieve high year-over-year growth rate with strong DAU growth and ARPU increase. Thank you.

Jean Zhang: Yes, this is Jean. Regarding your second question, in the fourth quarter, we spend 31.6 on sales and marketing expenses, representing 67% of our total revenue, slightly above our original plan. Most of the cost was spend on acquiring new user.

As Karl mentioned, our first priority at this stage is to grow our user base rapidly, considering the great economics and our systematic growth approach demonstrated. We spent a bit more money to acquire new users with stable unit cost compared to last period. As a result, the DAU grew from 11 million to 16.9 million, which is beyond our estimation of 14 million, [as we noted]. We are actually very happy with this result.

Alicia Yap: Thank you, Jean. Any color for the spend for 2019? And then Karl, to follow up on your DAU and the user, the engagement ratio, will 2019 be similar with the fourth quarter at like 36%, 37%? Thank you.

Karl Zhang: At this moment, we are confident that we can keep that keep relatively stable user engagement level for this year.

Jean Zhang: Yes, in the fourth quarter, you can see that our engagement level improved to be around 37%, and we have the confidence to remain set and stable. And for the percentage of sales and marketing compared to the total revenue, generally, we will keep the similar unit economics compared to 2018. And of course, under the condition that we will grow our user base as the first priority. At the same time, we can show the financial results in a balanced sum.

Alicia Yap: Okay. Thank you.

Operator: Gregory Gu of Credit Suisse.

Gregory Gu: I have two questions. My first question is regarding the competition landscape of the portfolio products. So what is the current competition landscape in overseas market when promoting our portfolio products? And who are the major competitors that we are facing? Are

they from China or are they local companies?

And also, is that because of the competition, so we are changing our strategic focus to user growth, rather than ramp-up the monetization that we have for the portfolio products? This is my first question.

And my second question is about the geographic distribution for our portfolio products. Can we get some color about how much DAU or MAU are from developed areas like Europe and North America? Thank you.

Karl Zhang: Thank you. So I'm going to answer these two questions. So the first question is about the competition. So from my point of view, global content app market is promising. Based on our data, the amount of time that global users spend on mobile devices every day, compared to Chinese mobile phone users, are relatively short, but increasing. We believe that most of the increased time was spent to consume content for different verticals.

So our strategy is to release multiple companies' apps to capture mobile internet users' ever-evolving content needs. So this strategy is ensured will release profit ads to target a more specific group and the growth after. We began to (inaudible) and the competition situation change in this quarter.

And the only reason that we often like the ad load and the reserve to some inventory for future use now [technical difficulty] to improve user engagement and retention. And such optimization, the related part actually started from Q3 last year, so a [very specific] time with the (inaudible) current user acquisition and engagement. So this is for the first question.

And the second question is about just the vertical distribution. There is no specifics from the change in terms of the MAU phase vertical distribution of our portfolio products. So we have approximately a 32% MAU from tier-one countries, mostly from the U.S.

And the percentage of these in Asia has -- which has relatively high monetization potential -- increased from 2.4% to approximately 4.3%; and the percentage of Southeast Asia increased from 7% to 10%; and South Asia decreased from 18% to 15% approximately. Thank you.

Gregory Gu: Thank you, management.

Operator: Emerson Chan of Bank of America Merrill Lynch.

Emerson Chan: I just have one question regarding the big jump on the other operating income in Q4. I think it is related to the government subsidy, but can we elaborate more about it? And how do we see the subsidy amount in this year? Thank you.

Jean Liqin Zhang: Yes, this is Jean. In the fourth quarter, we received about US\$1.4 million equivalent from government as one-time reward for our successful IPO. And actually, we [resolved] this. We were in one time (inaudible) happened in this year and actually, the Company used this money to fund the bonus to our employee for one-time reward for their achievement in last year and the success of our IPO. So this is the general situation about the government subsidy.

Emerson Chan: Thank you. That's helpful.

Operator: Hans Chung of KeyBanc Capital Markets.

Hans Chung: So I have a couple of questions. First, for the fourth quarter, we have a better-than-expected result for portfolio DAU. And so is that upside across-the-board, or it's on certain apps?

And then following that, for 2019 regarding the portfolio app, so what's our -- the going strategy? How many new apps are you expecting to launch for this year? And then, do you have any focus on any potential app? I think it could be a big app and so you want to put more on that. And then also, any color around the geography? Like where you maybe have more focus and then against the others? So that's my question.

Karl Zhang: Thank you, Hans. So this is Karl; I'm going to answer your question. So I'm going to merge your questions and answer as one. So first, I want to simplify; I want to simply introduce the product development, the model of our Company. So based on our invest in user insight capability, we have developed a growth foundation for user prediction, unified recommendation and monetization so -- and also, we encourage product team to incubate new content-rich apps to catch the mobile internet users' ever-evolving content needs.

So if the new app meets certain criteria, and with some critical product matches, such as business engagement, retention and certain ROI level. So it is graduated from incubation stage and we are going to put more results to grow if user basing large scale. So that's how we work. And we're happy focusing on improving our existing product line, which covers 5 content verticals when we (inaudible).

So it's like healthcare, lifestyle, fitness, entertainment and the short video and make good progress. So I have to say that all of the 5 verticals are growing well, and the user engagement rates of our portfolio products improved significantly from 33% to 37% approximately.

And here, I want to highlight one app, which is sharing our portfolio action, which provides female-oriented content in the news feed including posts, articles and short videos was released on iPhone, and demonstrated impressive user retention rates. So it's now known as one of the most popular lifestyle apps on the App Store for U.S.

The Cherry success on iPhone demonstrates our product development capabilities and the potential of our systematic user growth approach. So this year, we will be -- we're going to take more effort to grow IOS platform. And for example, a 3-hour meditation content apps was also released on iPhone.

And we are also incubating a number of new content-rich apps, and some of them are showing good momentum. So we are expecting to release 2 or more new content apps in the first half of this year. Thank you.

Operator: (Operator Instructions). This concludes our question-and-answer session. I would like to turn the conference back over to Christian Arnell for any closing remarks.

Christian Arnell: Thank you, everyone, for joining the call tonight. That concludes the call. If

you have any questions or comments, please don't hesitate to reach out to any of us. Thank you, and good night.

Operator: The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.