

[YALA] Yalla Group Ltd.
Q1 2021 Earnings Conference Call
May 10, 2021 08:00 PM E.T.

Executives

Kerry Gao, IR Director
Tao Yang, Chairman and Chief Executive Officer
Saifi Ismail, President
Karen Hu, Chief Financial Officer

Analysts

Feiya Zhao, Haitong International
Bo Pei, Oppenheimer
Kai Fang, CITIC
Chuting Ji, CICC
Fiona San, Jefferies

Presentation

Operator: Good morning and good evening, ladies and gentlemen. Thank you for attending -- standing by for Yalla Group Limited's First Quarter 2021 Earnings Conference Call. (Operator Instructions). After management's prepared remarks, there will be a question-and-answer session. Today's conference call is being recorded.

Now I would like to turn the call over to your speaker host today, Ms. Kerry Gao, IR Director of the company. Please go ahead, ma'am.

Kerry Gao: Hello, everyone, and welcome to Yalla's First Quarter 2021 Earnings Conference Call. We released our earnings earlier today, and it is now available on our IR website as well as on Newswire services.

Before we continue, please note that the discussion today will contain forward-looking statements made under the safe harbor provision of the U.S. Private Securities Litigation Reform Act of 1995. Forward-looking statements involve inherent risks and uncertainties. As such, our future results may be materially different from the views expressed today.

Further information regarding this and other risks and uncertainties is included in our earnings release and our registration statements filed with the SEC. Yalla does not assume any obligation to update any forward-looking statements, except as required by law.

Please also note that Yalla's earnings press release and this conference call include discussion of unaudited GAAP financial information as well as unaudited non-GAAP financial measures. Yalla's press release contains a reconciliation of the unaudited non-GAAP measures to the unaudited most directly comparable GAAP measures.

Today, you'll hear from Mr. Tao Yang, our Chairman and Chief Executive Officer, who will provide an overview of our recent achievements and growth strategies. He will be followed by Mr. Saifi Ismail, the company's President, who will give a brief review of our recent developments. Ms. Karen Hu, our Chief Financial Officer, will then provide additional details on the company's financial results and discuss financial outlook.

Following management's prepared remarks, we'll open up the call to questions. Our Chief Operating Officer Mr. Jeff Xu will join the call for our Q&A session.

With that said, I would now like to turn the call over to our Chairman and Chief Executive Officer, Mr. Tao Yang. Please go ahead, sir.

Tao Yang: Thank you, Kerry, and thank you, everyone, for joining our 2021 first quarter earnings conference call. 2021 is off to a remarkable start. Yalla Group's total revenue increased almost by 40% Q-on-Q and reached US\$67.6 million, exceeding the upper end of our guidance range by 7.4%. This stellar performance was driven by our continued efforts to grow our user community, the effective conversion of active users into paying users, and the further advancement of our monetization capabilities and initiatives.

In the first quarter of 2021, we also maintained robust profitability, as demonstrated by our non-GAAP net margin of 49.7%.

With the strong execution of our efforts to raise brand awareness across the Middle East and North Africa region, and our effective marketing campaigns tailored to the local culture, monthly active users for our group increased by 14.6% Q-on-Q and reached \$18.8 million.

In addition, increasing user engagement on our platform drove Yalla Group's paying users up by 11.5% quarter-over-quarter to 5.8 million, leading to outstanding paying ratio of 31%. Our ability to monetize also continued to improve as our group's ARPPU grew rapidly by 25.5% quarter-over-quarter, reaching \$11.6 in Q1.

During previous earnings calls, we announced 4 new products in our pipeline; 3 of them are casual game platforms, including Baloot for users in Gulf countries, 101 Okey for Turkish users and Yalla Parchis for South American users. The beta versions of all 3 casual game products have been made available online. And we have also made great progress in refining the technological and user interface details of these new products over the past quarter. Our President Saifi will share more details with you in his part later.

Our 4th new product is YallaChat, an instant message or IM product designed specifically for Arabic users. We are pleased to share that we launched the beta version of YallaChat in March. With this strategically significant product, Yalla Group aims to build and strengthen connections among our individual apps and create an integrated and synergistic ecosystem. To this end, we have adopted measures to attract the right talent to join our R&D and product teams. This beta version supports basic instant messaging functions, such as messaging, voice chatting and video chatting.

Since its launch, our development team has continued to refine and enhance the product based on user feedback, and will gradually roll out new design features and functions on the platform

based on the local users' feedback and desires. The improvement and iteration of an IM product is always an ongoing process, and the initial beta stage can take more than several months. We are dedicated to perfecting the details of the product before the team decides to officially launch the product and start full promotion.

As we mentioned in our last earnings call, Yalla's top priority this year is to expand our user base. With new products lined up for official launch, we plan to increase our sales and marketing activities to build out an initial user base for these products.

For our existing 2 products, Yalla and Yalla Ludo, we will maintain our strategy for steady user growth and don't expect to see much change in expense base related to these 2 products. Furthermore, as we continuously enrich our portfolio, we aim to amplify synergies among our various products, and gradually build and develop a comprehensive Yalla ecosystem. Our President Saifi will elaborate more on this idea in a few minutes.

We had an outstanding first quarter marked by strong growth across our primary operational and financial metrics. In just a few days, Yalla is going to have its 5th anniversary. 5 years ago, we identified voice chats to be uniquely suitable for online social networking and entertainment in MENA and pioneered the development of Yalla, as the first voice-centric mobile social networking and entertainment platform in the region. Over the past 5 years, our leadership in this field went from strength to strength as we gradually enriched and enhanced the products we offer to better serve local users while affirming our mission to build the most popular destination for online social networking and entertainment activities in MENA.

Looking ahead, we continue to closely watch trends in MENA's local culture, expand our friendly community, and build Yalla's ecosystem with various products and services tailored to local users' needs.

Now I will turn this call over to our President Mr. Saifi Ismail, for a closer look at our recent developments.

Saifi Ismail: Thanks, Tao. Hello, everyone. Thanks for joining us today. As we continue to enrich our product portfolio, including Yalla, Yalla Ludo, and the 4 new products in the pipeline, we are looking to boost synergies among individual apps to develop a more integrated ecosystem, which will help us improve efficiency in acquiring new users going forward. With this move, we expect to see an increase in the flow of users from application to application, especially between the chatrooms available on each of our products.

We also anticipate seeing an increase in users' awareness of the multiple products and services provided by the Yalla Group, which will as a whole, lead to a larger user base, longer time spent in Yalla's ecosystem and deeper brand loyalty in the long run.

We recently tested the effectiveness of advertising Yalla on Yalla Ludo in a few regions, and the resulting traffic gain for Yalla was solid. While we have observed good potential for cross-selling on Yalla Ludo, before we decide to launch this project officially, we plan to run more trials. Essentially, we will test the concept in a few countries first, progressively apply it to all other countries that we operate in, and potentially replicate the same process to help promote our upcoming new products, or even collaborate with other apps in the future.

Another exciting update we would love to share with you, our investors here, is about our new product, Yalla Parchis. As UAE's first technology unicorn listed on the NYSE, besides focusing on serving our MENA users' needs in the internet era, Yalla is also exploring overseas opportunities in the South American market.

Our first product customized for South America, Parchis, has received very good user feedback in its beta trial. And we are very encouraged by its user metrics that we are constantly evaluating. We will keep monitoring the trend, and we will share more updates for Parchis' development with you next time.

Yalla will continue to leverage the teams' deep local insights to provide MENA local users with various products tailored to their needs and preferences, as it remains dedicated to building and developing the Yalla ecosystem. Our mission is to become the number one provider for online social networking and entertainment in the MENA region, and we are well on our way to achieve it.

With that, I will now turn the call over to our CFO Karen, who will discuss our key financial and operational results.

Karen Hu: Thank you, Saifi. Hello, everyone. Thank you for joining us. Our strong performance sustained into the first quarter, as we steadfastly executed our growth strategy that prioritizes user experience and community development.

Our first quarter revenues grew by 221% year-over-year to US\$67.6 million, while our non-GAAP net income reached US\$33.6 million with a growth rate of 263.7% year-over-year.

Our non-GAAP net margin remained elevated at 49.7%, reflecting our unique monetization strategy, marketing positioning and strong operating efficiency.

Now I would like to walk through our financial details for the first quarter of 2021. Our revenues were US\$67.6 million in the first quarter of 2021, a 221% increase from US\$21.1 million in the same period last year. The increase was primarily driven by the widening of both Yalla's and Yalla Ludo's user base and the enhancement in Yalla Group's monetization capability.

Our average MAUs increased by 206.9% from 6.1 million in the first quarter of 2020 to 18.8 million in the first quarter of 2021. Yalla's MAUs increased by 81.6% to 7.3 million in the first quarter of 2021 from 4 million in the same period of last year. And Yalla Ludo's MAUs increased by 445.4% to 11.5 million in the first quarter of 2021 from 2.1 million in the same period of last year.

In addition, another primary contributor to our solid revenue growth was the significant increase in the number of paying users, which grew from 1.6 million in the first quarter of 2020 to 5.8 million in the first quarter of 2021.

Now let's look at our costs and expenses. Our cost of revenues was US\$24 million in the first quarter of 2021. Excluding share-based compensation expenses, cost of revenues in the first quarter of 2021 were US\$22.3 million, a 227.2% increase from US\$6.8 million for the same

quarter last year. The increase was primarily due to an increase in commission fees for third-party payment platforms resulting from our expanding business scale.

Excluding share-based compensation expenses, other components of cost of revenues as a percentage of our total revenues remained relatively stable at 33% in the first quarter of 2021, compared with 32.3% in the same period in 2020.

Our selling and marketing expenses were US\$8.4 million in the first quarter of 2021. Excluding share-based compensation expenses, other components of selling and marketing expenses for the first quarter of 2021 were US\$5.1 million, an 81.7% increase from US\$2.8 million for the same quarter last year. The increase was primarily due to higher advertising and marketing promotional expenses as a result of our continued user acquisition efforts.

Excluding share-based compensation expenses, other components of selling and marketing expenses as a percentage of our total revenues decreased from 13.4% in the first quarter of 2020 to 7.6% in the same period in 2021, primarily due to strong growth in organic user acquisition through word-of-mouth referrals as well as brand effect, and enhanced marketing efficiency.

Our general and administrative expenses were US\$11.7 million in the first quarter of 2021. Excluding share-based compensation expenses, other components of general and administrative expenses for the first quarter of 2021 were US\$3 million, a 124.4% increase from US\$1.3 million for the same quarter last year, which was primarily due to an increase in salaries and other benefits for our general and administrative staff, which was in turn driven by an expansion of our general and administrative staff.

Excluding share-based compensation expenses, other components of general and administrative expenses as a percentage of our total revenues dropped from 6.4% in the first quarter of 2020 to 4.4% in the first quarter of 2021 due to economies of scale.

Our technology and product development expenses were US\$3.3 million in the first quarter of 2021. Excluding share-based compensation expenses, other components of technology and product development expenses for the first quarter of 2021 were US\$3.2 million, a 277% increase from US\$0.9 million for the same quarter last year. The increase was primarily due to an enhancement in salaries and benefits for our technology and product development staff, which was in turn driven by an expansion of our technology and product development arising from higher investment in new products and services.

As a result of these reasons, other components of technology and product development expenses as a percentage of our total revenues rose from 4.0% to 4.7% year-over-year.

As such, our operating income was US\$20.2 million in the first quarter of 2021, compared with operating income of US\$9.2 million in the same period last year. Excluding share-based compensation, non-GAAP operating income for the first quarter of 2021 was US\$34 million, a 267.8% improvement from the same quarter last year.

Our income tax expense was US\$0.43 million in the first quarter of 2021, in comparison to US\$0.19 million in the first quarter of 2020.

Moving to the bottom line, our net income was US\$19.8 million in the first quarter of 2021, a 114.6% increase from US\$9.2 million in the same period last year. Excluding share-based compensation expenses, non-GAAP net income for the first quarter of 2021 was US\$33.6 million, a 263.7% improvement year-over-year.

Next, I would like to briefly go through our liquidity and capital resources. As of March 31, 2021, we had cash and cash equivalents of US\$261.7 million, as compared to cash and cash equivalents of US\$236.9 million as of December 31, 2020. This improvement demonstrates our resolve and capability to improve Yalla Group's operations on a consistent basis.

As we entered the second quarter, with the Ramadan fasting period taking place across MENA between 13 April through 12 May in 2021, we expect to have a relatively moderate revenue growth due to potentially reduced social and entertainment activities, which is an annual seasonal impact. We expect our revenues to be between US\$65 million and US\$71 million in the second quarter of 2021, taking the seasonality into consideration.

Looking ahead, we will leverage our team's deep local insights, continue to develop the Yalla ecosystem and enhance our brand building to further pave the runway for long-term growth, as we are committed to delivering a superb experience to our users and meaningful returns for shareholders.

The above outlook is based on the current market conditions and reflects the Company management's current and preliminary estimates of marketing and operation conditions and customer demand, which are all subject to change.

This concludes our prepared remarks for today. 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). For the benefit of all participants on today's call, if you wish to ask your question to management in Chinese, please immediately repeat your question in English.

The first question today comes from Feiya Zhao with Haitong International. Please go ahead.

Feiya Zhao: (Speaking foreign language). I will translate for myself. Now thank you, management, for taking my questions and congrats on your strong quarter. So my question is mainly related to the Yalla Parchis. Could you please provide some color to the current stage of Yalla Parchis such as MAU revenue, user profile content and user paying behavior? And what is the most active country for Yalla Parchis now and when are you going to officially launch the product?

Tao Yang: Hi, Feiya. I will answer your question. But based on the feedback we received, which clearly showed love for Yalla Parchis from users in South American market, we believe Parchis

has the potential to become a popular product in this region. We have already started the promotion of Yalla Parchis in Q1. And according to App Annie's data, it's, it has already among the top 5 in 6 countries under the Board game category in Android. And we will continue to monitor the engagement trend, and look forward to sharing more feedback and data with you next quarter.

Again, we are starting to strengthen our campaigns in Q2. The numbers like the MAUs, the other operation data that we prefer to provide later next earnings call.

Feiya Zhao: Thank you, Mr. Yang.

Operator: Bo Pei with Oppenheimer.

Bo Pei: So I do have two quick questions here. So first is I guess our non-GAAP margin actually improved sequentially in 1Q. I guess that's because we haven't started spending ourselves and marketing, yes. So my question is when do we tend to spend more on sales and marketing for especially for our new products, right? And then if we -- but when we do that, what was going to be the impact on our net income margin?

And then the second question is about our MAU growth outlook. So last time, we talked about 10% to 15% sequential growth for each quarter of this year. So can management comment on that, any update on that? And then how should we think about the MAU outlook for the new products? For example by the end of in this year, like what's going to be the user size with new products?

Karen Hu: Thank you, Bo. Thank you for your question. So for Q1, Yalla achieved very good net margin again. And for Q2, since we have going Q4 on promotions of our new products, we may see some influence from that to our margin. In terms of how much we are going to spend in sales and marketing, it really depends on user feedback and marketing dynamics. We will adjust our promotion strategy accordingly and in time to maximize the efficiency of spending.

For the Yalla and Ludo's MAUs outlook, as we mentioned last quarter, we think that both products' MAUs will change to 15% quarter-over-to-quarter in 2021. And for the new products' MAUs outlook, we think that it will depends on the user feedback and for the sales and marketing progress. Thank you for your question.

Bo Pei: Got it. Thank you.

Operator: Kai Fang with CITIC.

Kai Fang: Congratulations for the quarter. So my question is Yalla Chat, so in terms of the instant message product, how do you see the competition from other products like WhatsApp? And what is your user growth strategy and timeline for Yalla Chat?

Tao Yang: Good morning, Kai Fang. I'd like to answer your question. As a company with local teams based in UAE, we are dedicated to offering an IM product, that's tailored to Arabic users' life scenarios, using habits and preferences, which is the main difference between Yalla Chat and

WhatsApp. We will build many localized features for this product and continue to refine it based on local user feedback.

And in terms of user growth strategy, when we think the product is ready, we'll introduce Yalla Chat to users in our Yalla community and from Yalla and Yalla Ludo and other products, and encourage them to give it a try. In this way, we will be able to leverage the community we have built and the social connections we have fostered over the past years. Thank you, Kai Fang.

Kai Fang: Okay. Thank you.

Operator: Chuting Ji with CICC.

Chuting Ji: First, I would like to congratulate for another strong quarter. I have a question regarding your product pipeline. Currently, both of Yalla's products are voice-centric, since video entertainment applications have gained a lot of attention these days. Do you have any plans to launch video-centric products in the future? Can you please share more color about that?

Tao Yang: Thank you, Chuting. At this point, we don't have video-centric product in our pipeline, but it doesn't mean that we will only focus on voice-centric products. We will keep monitoring MENA users' need and trends in social networking and entertainment. And we will continue to adjust our strategy accordingly. Thank you.

Chuting Ji: Thank you.

Operator: Fiona San with Jefferies.

Fiona San: Congratulations on the great results. I have two questions. So the first question is about the strategies of user acquisition. I would like to ask are there any differences of user acquisition strategies for a different product in different regions? So like for example, we launch new product in South America. So what will be the marketing strategies there?

And my second question is about major long-term outlook. So could management share some colors about outlooks for 2 to 3 years from now, like geographic expansion and business line expansion that products offers?

Jeff Xu: Thanks, Fiona. Good question. This is Jeff, I'll be answering the question. Through running marketing campaigns on Yalla and Yalla Ludo over the past 5 years, our team has gained valuable experiences and gradually built strong capability in marketing. Our high user acquisition and efficiency can be demonstrated by our expense controls in sales and marketing and the consistent increase in our MAUs, besides the traditional user acquisition through advertising on media, both of Yalla and Yalla Ludo have also shown strong organic growth.

And at the same time, because of the high quality of the product and deep localization, our products have also been recommended for free by top-tier platforms like Apple and Google. These all contributed to our successful user acquisition. For every new product, we will design marketing plan based on our understanding of the product's special characteristic, and we will always follow our own pace in execution and adjust our strategy according to the feedback and metrics that we keep monitoring, as it's always a very dynamic process.

We also have different plans tailored for different regions to maximize the efficiency of spending. So for the upcoming promotion of our new product, we are very confident in our teams' capability to achieve strong results. Thank you for the question again.

Tao Yang: And I'll be answering the second question. For the next 2 to 3 years, MENA will certainly be our main focus. And with Yalla Parchis' launch, we will keep our eye on the South American market and see if there are any other potential opportunities. In addition to Yalla, Yalla Ludo and 4 new products we've introduced earlier, we will continue to monitor local users' needs and preferences and identify further opportunities to serve MENA users.

At the same time, as we introduced earlier, we will gradually start to drive traffic from one product to another, with the dedication to build and develop our Yalla ecosystem, which will, as a whole, lead to a more integrated user community, longer time spent in Yalla's ecosystem and deeper brand loyalty in the long run. Thank you, Fiona.

Fiona San: Thanks.

Operator: As there are no further questions now, I'd like to turn the call back over to management for any closing remarks.

Kerry Gao: Thank you once again for joining us today. We look forward to speaking with you in the next quarter. If you have further questions, please feel free to contact Yalla's Investor Relations through the contact information provided on our website or the Piacente Group Investor Relations.

Operator: This concludes the conference call. You may now disconnect your line. Thank you for attending.