

[YALA] Yalla Group Ltd.
Q3 2022 Earnings Conference Call
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Executives

Kerry Gao, IR Director
Tao Yang, Chairman and Chief Executive Officer
Jeff Xu, Chief Operating Officer
Karen Hu, Chief Financial Officer

Analysts

Kaifang Jia, CITIC
Thomas Shen, Nomura
Edward Wang, Credit Suisse
Xueqing Zhang, CICC
Chenghao Li, CICC
Yulin Zhong, Haitong International
Zemin Chen, Huafu Securities

Presentation

Operator: Good morning and good evening, ladies and gentlemen. Thank you for standing by for Yalla Group Limited Third Quarter 2022 Earnings Conference Call. (Operator Instructions). After management's prepared remarks, there will be a question-and-answer session. Today's conference is being recorded.

Now I will hand the conference 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 third quarter 2022 earnings conference call. We released our earnings earlier today, and the release 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 annual report 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 a discussion of unaudited GAAP financial measures, 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 will hear from Mr. Tao Yang, our Chairman and Chief Executive Officer, who will provide an overview of our latest achievements and growth strategies. He will be followed by Mr. Jeff Xu, our Chief Operating Officer, who will briefly review our recent business developments. Ms. Karen Hu, our Chief Financial Officer, will then provide additional details on the company's financial results and discuss our financial outlook.

Following management's prepared remarks, we will open up the call to questions. Mr. Saifi Ismail, the company's President, is unavailable for today's call due to a personal emergency.

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 third quarter 2022 earnings conference call. We are pleased to have delivered another strong quarter, with record revenue of USD80.1 million, exceeding the higher end of our guidance by 6.8%. This also represents a third consecutive quarter of record-breaking revenue for the company, and underscores our unique capabilities in driving business growth at a solid pace while continuing to develop our integrated product ecosystem.

Such robust quarterly results are underpinned by our continuous efforts to refine our operational processes, optimize user acquisition and further drive our product monetization. Together, these actions have effectively improved our user experience, thereby further boosting Yalla's and Yalla Ludo's user engagement and users' willingness to pay on our platforms.

Also, our impressive quarterly results are a testament to our core strategy as well as our operational improvements. As we further deepen our expertise and broaden our product portfolio in MENA, we are confident in our future growth potential.

Now let's take a closer look at our new product updates. Leveraging our extensive, industry-leading experience in social and online entertainment in MENA, we established Yalla Game to explore the mid-core and hard-core game distribution business as a complement to our casual games portfolio. This quarter, Yalla Game has taken a crucial step. We are excited to share with you that after several months of collaboration with the gaming studio we invested in, we have launched the beta version of our first hard-core mobile game, Merge Kingdom, in a number of MENA countries.

We will soon begin to gather user feedback and actively fine-tune the product through the beta stage, paving the way for a full-on promotion. We will share more details and metrics with you on our next call.

The second hard-core game that we plan to distribute in the region, the RPG game, is on track to be launched by the end of this year. Moreover, as MENA is becoming the next popular emerging market, and continues to attract attention from more and more gaming studios, we remain open to discovering good gaming content and potential collaborators with whom we can jointly further

explore the MENA market. We look forward to sharing more updates with our investors in the near future.

We are also very excited to report that we recently launched YallaChat version 1.3, which we had already developed into an instant messaging product with a broad array of localized and customized functions. This quarter, we added more engaging functions into the product. And as we shared previously, we are enhancing YallaChat by leveraging a unified login system. Over the past 2 quarters, we have upgraded our platform and hosted campaigns to encourage users to log into Yalla and Yalla Ludo using their YallaChat accounts, and to motivate more Yalla Group users to register for YallaChat accounts.

In addition, this quarter we launched a Yalla Ludo mini program within the YallaChat app. Yalla Ludo is the No.1 tabletop game across MENA. Yalla Ludo users now have full access to their game assets and get data in the game app when using the Yalla Ludo mini program in YallaChat. We believe this is a crucial step to boost product synergies and at the same time, increase users' stickiness to our apps.

Next, let's take a look at our WAHA product, the first-ever social metaverse designed for the MENA region. In Q3, we rolled out a number of new functions to enhance WAHA's gamification and entertainment features. First, we continue to launch new social scenes in WAHA, including a Disco scene this quarter, in which users can dance and play the role of DJ on stage. Second, beyond voice chatting with friends in WAHA's rooms, users can now also play music and videos, creating a virtual theater space for sharing their favorite entertainment while hanging out with their friends.

In addition, to further build out the product's gamification, our team began to roll out mini games in WAHA rooms, encouraging user engagement and boosting user interactions. We will continue to monitor the latest trends and upgrade WAHA accordingly to keep providing our users with fun and cool functions that are tailored to local culture and trends.

Before I wrap up, I am thrilled to share with you that our President, Mr. Saifi Ismail, has been named one of the region's 50 most inspiring business leaders of 2022 by the prestigious magazine Arabian Business, which is the Middle East region's top resource for informed news, features, and commentary. Its output includes interviews with some of the world's leading business people and long-form features from around the Middle East. Congratulations, Saifi!

In conclusion, I am happy with our ongoing solid results this quarter. Over the past 6 years, we have shown our strong focus on and commitment to MENA, its people and its culture. We strive to explore new products to meet MENA users' evolving needs and remain dedicated to facilitating digital transformation throughout the region. As a tech leader in MENA, we will continue to expand our services and stretch the boundaries of our business, while further deepening synergies among our different products and services to drive brand loyalty among users and improve our platform's brand influence. Once again, our vision is to build the most popular destination for online social networking and entertainment activities in MENA, and we remain steadfast in our pursuit of this goal.

Now I will turn this call over to our COO, Mr. Jeff Xu, for a closer look at our recent developments.

Jeff Xu: Hello, everyone. Thanks for joining us today. First of all, I am pleased to tell you that Yalla was recently invited to attend the sixth Future Investment Initiative in Riyadh, titled Investing in Humanity: Enabling a New Global Order. Hosted by the Future Investment Initiative Institute, the event brought together the world's foremost CEOs, policymakers, investors and entrepreneurs to discuss and shape the future of international investment and the global economy.

Yalla was honored to participate as a featured speaker on the From Seed to Unicorn: Empowering Youth Entrepreneurship panel, where we discussed the intersection of innovation, entrepreneurship, youth, and talent and shared Yalla's story with the local and international investment community. Yalla Group is proud to contribute to such events throughout MENA, helping to promote our region's talent, potential and unique local perspective to a broader audience, demonstrating our commitment to promoting a healthy and well-managed sector environment that facilitates the development of local digital economies.

Next, let's turn to our operations, as well as our products' performances this quarter. Our team's ongoing efforts to refine our content offerings and user operations further bolstered user engagement, as well as our paying ratio and advanced our monetization capabilities. As a result, we are pleased to report another robust quarter, with Yalla Group's total revenues of USD80.1 million, beating the higher end of the company's guidance.

In addition, our monthly active users increased 19.1% year-over-year, reaching 30.9 million. Yalla Group's paying users also increased to 11.5 million.

Now, a closer look at our casual game portfolio. Yalla Parchis ranked in the top 5 in terms of revenue in the board game category in 10 countries, including Columbia, Mexico, Chile and Spain. During Q3, we hosted a number of targeted events to encourage user activity on the platform. For example, our tomato fight event, which was inspired by the traditional Spanish festival la Tomatina, attracted participation by more than 60% of our daily active users, and improved diamond consumption on the platform by more than 20%. We will continue to find innovative ways to build the product's user community and strengthen its monetization capabilities.

For 101 Okey Yalla, after closely monitoring its operations for several months, we decided to add an independent Majlis or chat room function into the app, as the function has been proven effective in boosting our products' monetization capabilities. Beyond that, we also decided to increase our sales and marketing spend on this product, and to invest more to acquire IOS users. As a result, we have witnessed decent improvement in both 101 Okey Yalla's number of paying users and paying ratio, while its total revenue improved by more than 100% compared with that of the previous quarter. Although 101 Okey Yalla accounts for only a limited part of the Group's revenue, we still see this as an encouraging improvement in the product's current stage.

For Yalla Baloot, during the quarter, we continued to upgrade the product and launched several new game modes, fulfilling players' diverse needs and preferences as well as increasing app's

gamification. Yalla Baloot targets an important market in MENA, and we will continue to tailor the specification of its product design while collating user feedback.

With respect to monetization overall, we continue to explore innovative methods and channels across our portfolio. Let's look at Yalla Ludo, one of our flagship products, as an example. Yalla Ludo generally demonstrates great monetization potential, thanks to its widespread popularity and broad appeal. This quarter, we boosted its monetization even further via joint marketing efforts with our channel partner for the distribution of gift cards. This partner has launched a successful promotion campaign for Yalla Ludo in MENA, enabling us to reach more potential paying users. As a result, the channel's sales of Yalla Ludo gift cards grew by more than 30% compared with the sales before the campaign.

Interestingly, the majority of the sales came from first-time purchasers of Yalla Ludo gift cards, highlighting certain unfulfilled account recharging needs and presenting an opportunity for us to creatively attract new users while improving monetization across our gaming portfolio. We are encouraged by this progress and will further expand our payment methods to continuously improve our users' experience while creating more revenue streams for our company.

Before we move on to financials, I'd like to mention that we at Yalla Group were extremely honored and privileged to be the Gold Sponsor of City Talk, a new influencer marketing industry forum, which brought together more than 500 social media influencers from various countries in the Arab world in October in Jordan. While Yalla is a user-generated content platform, we have deep relationships in the Arab influencers' community, providing a mutually beneficial conduit for sharing ideas, opinions and experience. These connections empower us to keep up with current trends, identify new opportunities and remain part of the conversation online.

As MENA's largest online social networking and entertainment platform, we are also a valuable partner to influencers in promoting the development of the digital economy, a mission we all share.

As we reiterate every quarter, Yalla aspires to become the No.1 online social networking and entertainment platform in the MENA region. We have always been committed to providing the people of MENA with better access to a digital life. And we consistently enrich our product and service offerings and strengthen our partnerships with local channels to foster netizen communities throughout the Arab world. We are well-positioned to capitalize on potential growth opportunities in the MENA region and look forward to delivering value to all of our stakeholders as we strive to achieve our mission.

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, Jeff. Hello, everyone. Thank you for joining us. We delivered another outstanding set of financial results in the third quarter of 2022, with group revenues reaching a record USD80.1 million, up 12.3% year-over-year.

Thanks to our enhanced gamification and entertainment features, we also saw robust growth in paying users, driving our group's paying ratio to 37.4%.

Furthermore, we maintained healthy profitability with a GAAP net margin of 30.5%. And excluding share-based compensation, a non-GAAP net margin of 36.7%, all the while investing in innovation across our portfolio and strategically boosting our marketing spend. Going forward, we will continue to expand and integrate our Yalla ecosystem, optimizing operational efficiency, and explore new monetization avenues to propel our long-term growth and support sustainable returns to shareholders.

Now I would like to walk you through our detailed financials for the third quarter of 2022. Our revenues were USD80.1 million in the third quarter of 2022, a 12.3% increase from USD71.3 million in the same period last year. The increase was primarily driven by the broadening of Yalla Group's user base and enhancement to Yalla Group's monetization capabilities.

Our average MAUs increased by 19.1%, from 25.9 million in the third quarter of 2021 to 30.9 million in the third quarter of 2022.

Now let's look at our costs and expenses. Our cost of revenues was USD29.6 million in the third quarter of 2022, a 26.3% increase from USD23.4 million in the same period last year, primarily due to an increase in technical service fees resulting from the expansion of our product portfolio and an increase in salaries and benefits resulting from the expansion of our operation and maintenance team.

Cost of revenues, as a percentage of our total revenues, increased from 32.8% in the third quarter of 2021 to 36.9% in the third quarter of 2022.

Our selling and marketing expenses were USD12 million in the third quarter of 2022, a 9% increase from USD11 million in the same period last year, primarily due to higher advertising and market promotion expenses led by our continued user acquisition efforts and expanding product portfolio. Selling and marketing expenses, as a percentage of our total revenues, were 14.9% in the third quarter of 2022, decreasing from 15.4% in the same period last year.

Our general and administrative expenses were USD8.6 million in the third quarter of 2022, a 16.9% increase from USD7.3 million in the same period last year, primarily due to an increase in performance-based incentive compensation and an increase in professional service fees. General and administrative expenses, as a percentage of our total revenues, increased from 10.3% in the third quarter of 2021 to 10.7% in the third quarter of 2022.

Our technology and product development expenses were USD5.5 million in the third quarter of 2022, a 42.2% increase from USD3.9 million in the same period last year. This was primarily due to an increase in salaries and benefits for our technology and product development staff, driven by an increase in the headcount of our technology and product development staff to support all the development of new businesses and expansion of our product portfolio.

Technology and product development expenses, as a percentage of our total revenues, increased from 5.4% in the third quarter of 2021 to 6.9% in the third quarter of 2022.

As such, our operating income was USD24.5 million in the third quarter of 2022, compared with USD25.7 million in the same period last year. Excluding share-based compensation, non-GAAP operating income in the third quarter of 2022 was USD29.5 million.

Our income tax expense was USD0.79 million in the third quarter of 2022, compared with USD0.42 million in the same period last year.

Moving to the bottom line, our net income was USD24.4 million in the third quarter of 2022, compared with USD25.3 million in the same period last year. Excluding share-based compensation expenses, non-GAAP net income for the third quarter of 2022 was USD29.4 million.

Next, I would like to briefly go through our liquidity and capital resources. As of September 30, 2022, we had cash and cash equivalents of USD391.2 million, as compared with cash and cash equivalents of USD384.9 million as of June 30, 2022. This improvement demonstrates our ongoing commitment to streamlining and refining Yalla Group's operations.

On May 21, 2021, we announced the 2021 Share Repurchase Program. As of September 30, 2022, we have repurchased 2,302,141 American depositary shares, representing 2,302,141 Class A ordinary shares, from the open market with cash for an aggregate amount of approximately USD27 million.

In the fourth quarter of 2022, we expect our revenues to be between USD70 million and USD76 million.

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

This concludes our prepared remarks for today.