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Q1 FY2020 Investor's Conference Call August 2nd, 2019

SPEAKERS: Mr. François-Charles, Chairman and CEO;
Mr. Ganesh Murthy, Chief Financial Officer.

Operator:

Good morning ladies and gentlemen. I'm Ranjitha, the moderator of this call. Thank you for standing by and welcome to Onmobile Q1 FY'20 Investors Conference Call. For the duration of presentation, all participant's line will be in listen-only mode. There will be an introduction to the results followed by a Q&A session. Joining us today on the call are Mr. F. C. Chairman and CEO, Mr. Sanjay Bhambri, Mr. Ignacio Martin Velasco and Mr. Ganesh Murthy from management team.

Before we begin, I would like to mention that some of the statements made in today's call may be forward-looking in nature and may involve risks and uncertainties. For a list of such considerations, please refer to the earning presentation. Onmobile Global undertakes no obligation to publicly revise any forward-looking statement to reflect the future, likely events or circumstances. Please be advised this conference is being recorded today. I would now like to hand over the conference to Mr. F C. Over to you sir.

Francois-Charles:

Thank you. Thank you to all. Let me start by saying that it has been a very busier quarter in terms of new service launch. We launched 16 new services only in this quarter. We started with the Kids the brand-new Kids service in Europe. We launched many games clubs. We have a lot of sports service that were launched, some traction on digital contests also. So, really in our strategy to our many services and many geographies is really working out.

At this pace, I can share you that we are expecting that within the next two years, we will have about 100 new services live. So, just you understand the business case because I know you are looking at the quarterly results again, and as you can see, there is a bit of a decrease in revenues. But, I just want to share with you that when we launch a new service, we start from scratch. So, the first-year revenue of a new service is probably one-tenth or 20% of the service at maturity.

So, we expect about a good three years before these services can get the cruising speed. But obviously, with the number of services that we are launching right now, we are seeing that normally, we should just clearly have an increase in revenues in the coming quarters. Just to highlight also because as you know, we have done the acquisition of Appland, now it has been about the nine to ten months, and we are really focused on game subscriptions.

Just this quarter we had a 46% increase in game subscription revenues quarter-to-quarter. And back on the strategy that I was just mentioning that the earliest the service are, the maturity over time will increase and benchmarking with our competitor. So, if I

just highlight on gaming, for example, the average game club revenue that we have today for Appland – and keep in mind that Appland is dealing with the resellers, we are having people managing the services with the other operators, so we don't have a direct relationship with operators in some cases – so, the average revenue for Appland is \$3500 a month a day for a game club. And our competitors with mature clubs in this category is delivering about \$25,000 a month. So, we see a pretty impressive growth coming in front of us, obviously, and we are putting a lot of efforts on R&D to make the product even better, more engaging to make sure that we capture these revenues. But keep in mind that these clubs are really early in the process, so, just by getting more maturity will increase.

Also, we have games club that we signed directly as Onmobile. And one of them – just to give you an example, one of them that we signed last year now we're ranking in over \$150,000 a month of revenue. So, we are really seeing the maturity curve in some cases can deliver real revenues in gaming. The gaming market, I keep saying it, there is a very big market globally and will stay big. The key is to make sure we have our niche in there. And when we count the number of new services, that it is a game club or a new service on contests or kids, we really see that growth going from the first-year revenue to the third-year revenue really generating real revenues. So, with the 100 new services coming in in the next two years, this will have an impact on our revenue.

So, that is the highlight I wanted to give you as a start for this quarter. I'm now going to end up to Ganesh to talk about the financial results.

Ganesh Murthy:

Thank you F.C. Moving to the financials, our current quarter revenue registered a decline of 2.7% at INR 139.5 crores as against the previous quarter figure of INR 143.3 crores. Roughly, half of this decline was due to currency fluctuation. We had the Indian rupee appreciation in this quarter both against the euro as well as against the US dollar.

We also had a one-time reversal of INR 9.6 million for product development with one customer where the work was suspended. So, if we exclude the currency fluctuation and the one-time revenue reversal, our revenue decline would be around 0.7%. Our ongoing cost optimization initiatives has kept the Opex under control, and we have witnessed a 15% reduction in Opex quarter-on-quarter.

Headcount is down from 797 people at the end of last quarter to 759 people in the current quarter with savings expected to materialize from this action in the coming quarters. There is a higher

depreciation in the P&L, which is on account of adoption of the new accounting standard. So, from 1st April we have amended it to adopt Indian Ind AS 116, which is on lease accounting, and this involves a reclass of the rent to depreciation amounting to INR 11 million.

Now coming to the balance sheet items, our cash from operations was adversely impacted this quarter due to delays in receiving remittance from one large customer, and due to delay in raising invoices with another customer with whom we were negotiating a renewal of the contract. Now the good news is this contract has now been renewed and all the invoices have been raised.

Our cash balance continues to be robust at INR 251 crores, and we continue to remain debt-free. Now with these comments, I know hand over the call to the moderator for opening it up for questions. So, moderator over to you please.

Operator: Thank you. So, ladies and gentlemen, if you would like to ask a question, please signal by pressing star one on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. A voice prompt on the phone line will indicate when your line is open. Once again, please press star one to ask a question. We will pause for just a moment to allow everyone an opportunity to signal for questions.

We will take our first question from Arshad Mukadam from Vibrant Securities. Please go ahead.

Arshad Mukadam: Hi good morning. I wanted to know is the Appland revenue included in the total revenues?

Ganesh Murthy: Yes, Appland revenue is included in the total revenue.

Arshad Mukadam: Okay. So, then if we look at the gaming revenue trend, how much would be from Appland, sorry?

Ganesh Murthy: Now we do not disclose Appland separately. It is an integrated part and gaming revenue is not only Appland. So, we have gaming revenue from the Appland legal entity, plus also we have gaming revenues coming from various other legal entities, which were part of the erstwhile Onmobile, that is excluding Appland.

Arshad Mukadam: Okay, got it. So, I think as I have been studying at least for a few quarters and I think we have been concentrating on videos and games in terms of growth going forward. And as I look at the video

trend over the last few quarters, it has been on the decline. So, I just want to know where do we see the top line growth of the company coming from in the next few quarters because to be fair, it's only been going down recently from INR 150 crores.

Ganesh Murthy:

You are right; there has been overall decline due to various reasons. I won't get into them. But I think the growth in future is going to be coming mainly from our games revenue, subscription games. And if you understand a bit about this, there are two types of gaming products and services that we provide. One is where you download the games from the app store. And the second one which we launched last year, the subscription games which F C mentioned, which has grown by 47% quarter-on-quarter, is the subscription games, where a person takes a monthly or weekly subscription and he can download any number of games. So, that is the area of growth, that is the way the gaming market is moving towards subscription revenue, and that is where we see the growth in the future.

Arshad Mukadam:

Okay. The Tones business, it's been declining over the last two quarter. So, do we see any way we can cope this decline or is it a lost cause this business now?

Francois-Charles:

No, honestly, I know there is some region now we are growing actually in Bangladesh; most of the decline honestly was in India for many reasons now with the bundling where we are getting more and more involved in the bundling part of the package. So, I believe we are pretty much stabilized this decline now.

Arshad Mukadam:

Okay, thank you. My next question is on manpower. We have been doing really well in terms of reducing the number of employees we have, the count we have. So, I just want to understand the slight jump on the quarter basis in the absolute manpower. Is it like the incremental salaries or something like that?

Ganesh Murthy:

No, it is not incremental salaries. In fact, there has been no salary increment to employees. That slight jump that you see is primarily because last quarter we had a reversal of the variable pay. So, we accrue variable pay depending upon company performance. And since the company performance last year was below our targets, we had a reversal of the variable pay. And that is the reason why you see increase in the manpower cost.

Arshad Mukadam:

Okay. So, we can expect to see this number to go down?

Ganesh Murthy:

So, many of the figures that I mentioned about the headcount is actually the quarter end headcount. So, the full impact of the

reduced headcount 759 people at the end of June, but it was a higher figure in the month of April-May. So, the full impact of the reduction will actually be felt in quarter 2.

Arshad Mukadam: No, I get that. We have done really well in reducing the operating expenses over the last few quarters. I give you on that. So, I just had to understand also there is INR 21 crores outflow in trade payables also on the cash flow statement. So, why is that such a heavy figure, could you explain this please.

Ganesh Murthy: Sorry, you mean the figure is INR 21 crores, i.e. 207 million?

Arshad Mukadam: Yes.

Ganesh Murthy: So, that is the payable to normal creditors. There is nothing exceptional. Mostly, these are payments to our content providers. So, the content providers were paid, there was a whole bunch of them who were paid in just at the last week of June.

Arshad Mukadam: So, the payment happened in June itself because if you look at our cash flow statement, this is what has probably eroded our cash flows.

Ganesh Murthy: Correct.

Arshad Mukadam: If this payment were not made, then would probably be cash flow positive for the quarter.

Ganesh Murthy: Yeah, if you look at the previous quarter, you will see 135 million increase in the trade payables. So, there what happened is our contracts are all back-to-back with the content providers. So, we pay the content providers only after we received the revenue from the operators.

And since we received revenue a little late in the month of March, we paid them only in the month of April, and that was the reason why there was an increase in the trade payables at the previous quarter. Now that increase has been removed because now we have shifted to a normal payment cycle.

Arshad Mukadam: Okay, thanks for that. And I just had this one last question. In the balance sheet, I think you all have added this time the right-to-use assets 165 million. So, could you just explain to me what exactly this includes?

Ganesh Murthy: Yes, absolutely. So, as I mentioned, we have introduced from 1st April we are required to go by accounting policy Ind AS 116, which

talks about lease accounting. So, what happens is there is the value of our long-term leases, rentals basically, building rentals and office rentals, which are more than one year in duration. You need to find out the fair value of the future rent payments and bring that fair value as an asset in the balance sheet. So, that is the right-to-use asset INR 16.5 crores, which represents a fair value of the future lease payments.

And we also have to show that as a liability. So, if you will notice in the balance sheet, the current liabilities have increased from INR 86 crores to INR 106 crores. So, that represents the offset of the right-to-use asset. So, essentially, the fair value of the future rent payments is treated as an asset, and also treated as a liability.

Arshad Mukadam: Okay. I understand now. Thanks so much. That is it from my side.

Francois-Charles: Thank you.

Ganesh Murthy: Thank you.

Operator: Once again, ladies and gentlemen, if you would like to ask a question, please signal by pressing star one on your telephone keypad. Ladies and gentlemen, if you would like to ask a question, please signal by pressing star one on your telephone keypad. We will take our next question. I would request you to please state name before posing your question. We will take the next question again from Arshad Mukadam from Vibrant Securities. Please go ahead.

Arshad Mukadam: Yeah, hi again. I wanted to know if we made all of our payments for Appland acquisition, there was some variable payments that were needed to be paid, so, has that been paid off yet or that's left to be paid going forward?

Ganesh Murthy: No, that is not yet been paid. So, that earn out payments are – will be paid out in four tranches for in instalments from each first half. So, there is a payment due in August for the first half of this calendar year. Then there will be a payment for December half year and so on till 2020 December.

Francois-Charles: But keep in mind it is linked 100% on performance.

Ganesh Murthy: Correct.

Francois-Charles: So, we have to increase both the number of earnings and the revenue per month.

Arshad Mukadam: Okay. Got it. And if I may ask, how much of the cash is now India?

- Ganesh Murthy:** 60% of our cash is in India. That is the reason why it is only 60%. Last quarter it was 75% was in India. We had a major payment to be made of €4.3 million to be made to one of our large customers in Europe. So, that was – the payment happened on 1st July or 2nd July. And for that we had to transfer the funds to Europe in the last week of June.
- Arshad Mukadam:** Okay got it. And so, Appland is now debt-free, right, I'm guessing?
- Ganesh Murthy:** Appland is debt-free. I mean as a whole, Onmobile is debt-free. We have repaid – Appland did have debts at the time of the acquisition, but those were all paid out. From our perspective, it doesn't make sense. We have INR 251 crores of cash. So, it really doesn't make sense for us to burden our balance sheet by taking debt.
- Arshad Mukadam:** Got it. Also, so just could you tell me – did you have a rough figures of target manpower headcount going forward like, you all have been reducing it recently. So, what is the target you all have in mind?
- Francois-Charles:** Honestly, I think we are pretty much at the target now. With the number of services that we are launching, I mean we need people to be able to support all these deployments here. I think we are pretty much at a good optimal level.
- Arshad Mukadam:** Okay, that's good. Thank you.
- Ganesh Murthy:** But at the same time, I just wanted to add-on to what F C said when if we find – I mean this cost optimization is a constant endeavor. So, if we find any areas where we can adopt automation, increase the use of various automation tools, we do that and we try to optimize on the headcount.
- Arshad Mukadam:** Yeah, that's fair enough. Thank you. That's it from my end.
- Francois-Charles:** Thank you.
- Operator:** Once again, ladies and gentlemen, please press star one on your telephone keypad to ask questions. We will take our next question from private investor. Please state your name before posing a question. Go ahead.
- There is no response from this audio line. Ladies and gentlemen, if you would like to ask a question, I would request you to please press star one on your telephone keypad.

Francois-Charles:

Okay, no more questions. So, I'm going to just thank the investors for showing up on this call. Again, I'm saying that it has been a very successful quarter on launching new services. The next quarters also we are planning many new services to be launched and we are really working to increase that revenue per month for each of the services that we are launching. So, it will impact the revenues in the coming quarter. So, thank you very much and I look forward to speaking to you next quarter. Thank you.

Ganesh Murthy:

Thank you operator.

Operator:

Thank you. This concludes today's conference call. Thank you for your participation. Ladies and gentlemen, you may now disconnect your lines.