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WOWO - Q4 2014 Wowo Ltd Earnings Call

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Victor Anthony *Axiom Capital - Analyst*

Michael Jacobs *Axiom Capital - Analyst*

PRESENTATION

Operator

Hello, everyone, and welcome to the Fourth Quarter and Fiscal Year 2014 Earnings Conference Call for Wowo Limited. Today's conference is being recorded. At this time, I would like to turn the call over to Ms. Shayla Suen, IR Director of Wowo Limited, for opening remarks and introductions. Please go ahead.

Shayla Suen - *Wowo Limited - IR Director*

Thank you operator. Hello everyone, and thank you for joining us on today's call. Wowo Limited announced its fourth quarter and fiscal year 2014 financial results on Wednesday, May 13, after the market closed.

Our earnings release is now available on the Company's IR website at ir.55.com. Today, you will hear from Mr. Maodong Xu, our Chairman and CEO, who will give you an overview of the Company strategies, recent development and operational results, followed by the company's CFO, Mr. Frank Zhao, who will discuss financial results in more details.

Today, we also have Mr. Tiger Wu, our executive president in the call, who will be available to answer questions during the Q&A session following the call.

Before we proceed, I would like to remind you of our Safe Harbor statement. Please note that the discussion today may contain certain forward-looking statements, made under the Safe Harbor provisions of the US Private Securities Litigation Reform Act of 1995. These forward-looking statements are subject to risks and uncertainties that may cause actual results to differ materially from our current expectations.

To understand the factors that could cause results to materially differ in the forward-looking statements, please refer to our prospectus, filed with the SEC, on April 8, 2015.

We do not assume any obligation to update any forward-looking statements, except as required under applicable laws.

Now, it's my pleasure to introduce to you, Mr. Maodong Xu. Mr. Xu, please go ahead.

Maodong Xu - *Wowo Limited - CEO*

(interpreted) Thank you, Shayla

Welcome everyone to Wowo's Fourth Quarter and the Fiscal Year 2014 Earnings Call. We are pleased to have completed our successful IPO in April, and to be holding our first quarterly earnings call, as a NASDAQ listed public company.



And given my limited English-speaking ability, Frank will translate for me.

Wowo is an e-Commerce platform for local lifestyle service industry. Wowo provides a one-stop e-Commerce platform through which merchants can sell to their customers, make their own business decisions, adjust their merchandise offering, and how much to charge at an instant on their own, effectively maintain their relationship with their customers.

Transitioning from group buying model, Wowo has evolved into a leading local lifestyle service e-Commerce platform in 3 years. As our business model evolved, we also began focusing on our efforts on two areas to achieve a more sustainable growth path.

First, in order to build up a large merchant base more rapidly, we offered our platform service to all merchants for free and intentionally lower our commission rate with merchants.

Second, we began to support in-store payment by customers to ensure a superior merchant and the customer experience, which did not contribute to our total net revenue.

The implementation of these strategies has result in a significant growth of our merchant base from 35,000 in the first quarter of 2012 to over 117,000 in the first quarter of 2014.

We are pleased to report fourth growth 2014 financial results which reflect strong growth momentum. Fourth quarter revenue reached \$9.4 million, representing an increase of 9.4% from the same quarter of 2013. Net revenue from the storefront base grew to become our primary revenue generating stream, which is a healthier, more sustainable revenue stream for the Company. Net revenue from storefront sales increased to \$4.8 million in the fourth quarter of 2014, representing an increase of 46.4% in the same quarter of 2013.

There were favorable important operational developments for our business in the fourth quarter, which helped improve our business, mobile and monetization efficiency.

First, we continue to optimize our product ecosystem, particularly in mobile. We launched a major product upgrade in the third quarter of 2014 called Wang diantong, which is customized for our local paying merchants, to create and to manage their own brand APPs, scale their online stores via Wowo's operating platform and enable access to third party sales channels including Baidu Connect, Ali service and WeChat.

Additionally, this mobile app enables merchants to interact in real time with the users while looking for local deals. These new features allow our merchants to better manage their online stores and the client services efforts, as well as maximize sales opportunities.

This product upgrade has been very well received so far by local merchants, attracting more merchants, willing to pay storefront sales which helped drive our net revenue in the fourth quarter.

Apart from continuing to enhance the mobile user experience for merchants, we also continue to see strong mobile traffic growth from the customer on our own mobile app. Mobile traffic growth in China has grown rapidly in the past few years driven by the transition to smart phones. We are able to deliver superior user experience on our mobile platform as the local and the mobile concepts of our business naturally match together. In April 2015, the gross billings from the mobile have accounted for approximately 82% of the total gross billings.

Now, a second important operational development for our business in the fourth quarter is improved sales and service efficiency. Our local sales teams are rapidly becoming more efficient and we began to see positive results, with increasing customer renewals and greater adoption of our online operating services by merchants. As we continue to focus on sales efficiency, our revenue and the merchant base have increased, while in the meantime, the size of the local sales teams stayed around 2,000.

The third operational development in our business during the fourth quarter was our ongoing ability to enhance the user experience by attracting more merchants from our third-party vertical channels, and to provide more features. We have expanded the services function for our merchant

base by attracting service providers in specific vertical sectors onto the Wowo platform, and added new functions tailored for the specific industry. These include Ctrip, a leading online travel agency in China; Guevara, Mtime and Komovie, three leading cinema ticketing service providers.

In addition, we are developing our specific version on Wang daintong targeting the catering industry, providing many customer favored functions such as online ordering, delivery, reservation, and group buying.

Adding these additional providers and the functions enables our merchants to provide more services to their customers, enriching the customer experience, and increasing their sales opportunities going forward. As we continue to focus on variety of products and the service offerings, the number of service offerings on our platform has reached to over 480,000 in the fourth quarter.

As we look ahead, we are confident that our platform upgrade and the new value added services will drive our revenue growth in 2015. We will continue to focus on growing our merchant base, optimizing our product ecosystem, enhancing user experience, and increasing monetization in 2015.

For example, we intend to launch a new technology upgrade that enables merchants to open and manage their online stores on our platform using their own smart phones. We believe such initiatives can substantially increase the total number of online merchants on Wowo's platform, and ultimately lead to higher levels of paying merchants.

We are pleased to meet the needs of local merchants for alternative sales channels to expand their customer base, representing significant monetization potentials for Wowo along the way.

In summary, we will continue to work on these priorities as we go forward. We are pleased with the outcome of our public offering in April. Being a public company will allow us to enhance our service offerings to a broader range of merchants and customers, as well as attract and retain industry talent.

We will continue to invest and work hard to improve our competitive advantage in China's massive local lifestyle service market. The size of the local lifestyle service market in China is huge. According to the statistics for the service industry from the National Bureau of Statistics of the People's Republic of China, there are over 10 million service merchants in China as of December 2014, which are all our potential merchants for Wowo. By leveraging our ability to continually innovate and provide high-quality service, we aspire to move millions of merchants to our platform within the following years. And I'm confident that we can expand our leadership position in China's local lifestyle service markets.

On that note, Frank will now take you through the financials for the fourth quarter of fiscal year 2014.

Frank Zhao - *Wowo Limited - CFO*

Thank you, Mr.Xu.

Total net revenue increased to \$9.4 million in the fourth quarter of 2014, representing an increase of 9.4% from \$8.6 million in the same quarter of 2013. The increase was primarily driven by the increase of storefront fees which is a healthier and a more sustainable revenue stream for the Company. The percentage of net revenue from storefront fees increased from 37.6% in the same quarter of 2014 to 50.4% in the fourth quarter of 2014.

[And to that], net revenues from storefront fees increased to \$4.8 million in the fourth quarter of 2014, representing an increase of 46.4% from \$3.2 million in the same quarter of 2013. The increase was primarily driven by the increase in the number of paying merchants who have been receptive to the implementation of the one-stop shopping experience upgrade the Company rolled out in the third quarter of 2014.

Net revenues from commissions decreased by 12.9% from \$5.4 million in the same quarter of 2013 to \$4.7 million in the fourth quarter of 2014. The decrease in commission revenue was mostly due to the Company's efforts to lower the take rate or commission rate to attract more merchants to the Wowo platform.

The number of merchants on this platform increased by 53.3% to 117,889 in the fourth quarter of 2014 from 76,910 in the fourth quarter of 2013.

Net commission revenue was also impacted by the Company's support of in-store payment by customers to ensure superior customer experience, which was not included in gross billings, and therefore did not contribute to our total net revenue.

For the fiscal year 2014, while net revenue decreased by 17.0% to \$30.1 million from \$36.3 million in 2013, net revenues from storefront sales increased by 20.9% from \$10.0 million in 2013 to \$12.1 million in 2014.

Gross profit in the fourth quarter of 2014 was \$7.9 million, representing an increase of 16.8% from \$6.8 million in the same quarter of 2013. For fiscal year 2014, gross profit was \$23.0 million, representing a decrease of 22.4% from \$29.7 million in the prior year. Gross margin from the fourth quarter of 2014 increased to 83.9% from 78.6% in the same quarter of 2013. Gross margin for the full year 2014 decreased from 81.8% in the prior year to 76.6%.

Total operating expenses in the fourth quarter of 2014 decreased by 12.5% from \$17.8 million in the same quarter of 2013 to \$15.6 million. Non-GAAP operating expenses in the fourth quarter were \$15.2 million, representing a decrease of 13.7% from \$17.6 million in the same quarter of 2013.

The decrease is primarily due to a more effective marketing investment as our revenue contribution shifted from transaction based revenue to store front based revenue. Our marketing investment is focusing more on merchants awareness of business, merchant education, and the merchant conversion effort and less focused on acquiring traffic.

Marketing expenses decreased by 7.4% from \$2.3 million in the same quarter of 2013 to \$2.2 million in the fourth quarter of 2014, primarily because the Company reduced spending on certain low performance online advertising channels. Non-GAAP marketing expenses were \$2.2 million, representing a decrease of 7.8% from \$2.3 million in the same quarter of 2013.

Selling, general and administrative expenses decreased by 0.2% from \$13.5 million in the same quarter of 2013 to \$13.4 million in the fourth quarter of 2014. Non-GAAP selling, general and administrative expenses decreased by 1.5% from \$13.2 million in the same quarter of 2013 to \$13 million in the fourth quarter of 2014. The decrease of selling, general and administrative expenses was primarily driven by reduced office expenses and a lower provision for bad debts related to prepayments to merchants during the fourth quarter of 2013.

Total operating expenses for fiscal year 2014 were \$66.7 million, an increase of 8% from prior year. This was primarily due to approximately a \$4.8 million increase in share-based compensation charge and a slight increase in sales, marketing and G&A expenses, partially offset by a decrease in impairment of intangible assets. Non-GAAP operating expenses excluding share-based compensation expenses for fiscal year 2014 were \$60.9 million, a slight increase of 0.2% from \$60.8 million in 2013.

Loss from operations in the fourth quarter of 2014 decreased to \$7.7 million from \$11.1 million in the same quarter of 2013. Non-GAAP loss from operations in the fourth quarter of 2014 decreased to \$7.3 million from \$10.8 million in the same quarter of 2013. For fiscal year 2014, loss from operations was \$43.7 million, compared to \$32.1 million in the prior year. Non-GAAP loss from operations was \$37.9 million, compared to \$31.2 million in 2013.

Net loss attribute to Wowo Limited in the fourth quarter of 2014 was \$7.7 million, compared to \$11.1 million in the same quarter of 2013. Non-GAAP net loss attributable to Wowo Limited was \$7.3 million in the fourth quarter of 2014, compared with \$10.8 million in the same quarter of 2013. Non-GAAP net loss per diluted ADS or American depositary shares, each of which represents 18 ordinary shares, attributable to ordinary shares was \$0.52 in the fourth quarter of 2014 compared to \$0.72 in the same quarter of 2013.

For fiscal year 2014, net loss attributable to Wowo Limited was \$43.9 million, while non-GAAP net loss attributable to Wowo Limited was \$38.1 million.



Upon our successful IPO in April, Mezzanine equity, i.e., preferred shares, were converted into common shares and debt due to major shareholders were converted into common shares at the IPO price. As a result, our balance sheet was significantly deleveraged and we are free from short- and the long-term liabilities resulting in a much stronger and solid balance sheet.

Looking into 2015, we expect continued growth in the number of merchants using our platform services and continued growth of storefront fee revenue as a percentage of our total revenue.

As for our outlook, we expect our Q1 2015 revenue to be in the range of [\$6.5 million to \$6.8 million and 18% to 23%] (corrected by company after the call) increase over Q1 2014. This year-on-year growth will be driven by a continued growth of storefront fees.

I'd also like to point out that the first quarter is typically our slow quarter seasonally, given the Chinese New Year holiday.

This concludes our prepared remarks for today. Operator, we're now ready to take some questions. Operator?

QUESTIONS AND ANSWERS

Operator

Thank you, sir. We'll now begin the question and answer session.

(Operator Instruction).

Your first question comes from the line of Victor Anthony from Axiom Capital. Please go ahead.

Victor Anthony - Axiom Capital - Analyst

Yes, thanks. Hoping that you can hear me because I've had a hard time hearing throughout the prepared script. So hopefully these questions haven't been answered yet. Perhaps I'll ask some basic factual questions.

One, on your gross billings, what was the growth rate there? What percent of that was attributed to mobile?

Maodong Xu - Wowo Limited - CEO

(interpreted) In 2014, in January 2014 is \$440 million.

We are encouraging customer to pay in store so we didn't account the offline transactions to GMV.

In the last month, April of 2015, 82% of the transaction or traffic were from mobile.

Victor Anthony - Axiom Capital - Analyst

Okay. Now, the second question I had was on your paying merchant penetration rate. What was that on the quarter? And maybe you can help me you're your storefront fees per paying merchant? It's kind of interesting to see how that was trending.



Frank Zhao - *Wowo Limited - CFO*

Now, Victor, is that as the number of paying merchants in April?

Victor Anthony - *Axiom Capital - Analyst*

Correct.

Frank Zhao - *Wowo Limited - CFO*

And also the storefront base in April, right?

Victor Anthony - *Axiom Capital - Analyst*

For paying merchant, yes, correct.

Maodong Xu - *Wowo Limited - CEO*

(Spoken in Foreign Language).

Frank Zhao - *Wowo Limited - CFO*

Victor, sorry, can you say that -- what's your question again?

Victor Anthony - *Axiom Capital - Analyst*

I'm having a hard time hearing him, sorry. What was that?

Frank Zhao - *Wowo Limited - CFO*

Victor, I'm just trying to understand your question correctly. Are you asking the paying merchants and also the storefront base in Q4 or in ...

Victor Anthony - *Axiom Capital - Analyst*

No. In the fourth quarter.

Maodong Xu - *Wowo Limited - CEO*

Again, fourth quarter?

Victor Anthony - *Axiom Capital - Analyst*

Yes. Fourth quarter, yes.



Maodong Xu - *Wowo Limited - CEO*

(Spoken in Foreign Language).

Frank Zhao - *Wowo Limited - CFO*

The number of paying merchants now in Q4 has reach to 117,000. And the number of paying merchants has reached about the 12.4% of our 117,000 online merchant. And also the storefront base from Q4.

Yes, the storefront fee from Q4 has reached to \$4.7 million. And as a percentage of revenue has increased to 50.4%.

Victor Anthony - *Axiom Capital - Analyst*

Yes. I was just looking on per paying merchant rate, but I could get it out of that. The next question I had was really on your gross margins. There was kind of a meaningful jump in your gross margins. Why was that?

Frank Zhao - *Wowo Limited - CFO*

The gross margin for Q4?

Victor Anthony - *Axiom Capital - Analyst*

Correct.

Frank Zhao - *Wowo Limited - CFO*

For the Q4, the gross margin was 82%.

Victor Anthony - *Axiom Capital - Analyst*

Yes. But that increased quite meaningfully, so I was trying to get at why...

Maodong Xu - *Wowo Limited - CEO*

(Spoken in Foreign Language).

(Interpreted) The increase of our gross margin comes from our efficiency and in the [editing] and in our back office work and also the improvement of our infrastructure works.

Victor Anthony - *Axiom Capital - Analyst*

Okay. Thanks. [I'll get behind there] and let someone else get on. Thanks.

Frank Zhao - *Wowo Limited - CFO*

Okay. Thank you, Victor.

Operator

(Operator Instructions)

Your next question comes from analyst [Michael Jacobs] from Axiom Capital. Please go ahead.

Michael Jacobs - *Axiom Capital - Analyst*

Congratulations, guys. It gave me great pleasure knowing how hard you worked to get public in the US, to hear this first quarter call. And my question is -- the IPO was strategic rather than financial. Have you seen any benefits both with your merchants and with the market in general in China from being public and from accomplishing the IPO?

Frank Zhao - *Wowo Limited - CFO*

(Spoken in Foreign Language).

(Interpreted) We are a service provider to the local life service merchants and we believe in the branding for the local life service merchant and to expanding our coverage to the local service merchant is very important to our business. And our IPO, our successful IPO, no doubt will bring the recognition of the Company and enlighten our branding over the industry, over this space. And we believe the IPO, the successful IPO. And we'll have our branding and we will attractive more merchants to our platform.

Michael Jacobs - *Axiom Capital - Analyst*

Great.

Frank Zhao - *Wowo Limited - CFO*

Michael, any more questions?

Michael Jacobs - *Axiom Capital - Analyst*

That's all for me.

Frank Zhao - *Wowo Limited - CFO*

Thank you.

Operator

(Operator Instructions) There are no further questions at this time. Mr. Xu, please continue.

Frank Zhao - *Wowo Limited - CFO*

This concludes our first earnings call as a public company. Thank you for participating on our call. We're looking forward to updating you on the progress of our business in the coming weeks, and months ahead. Thank you and have a good day for those who are based in the US, and have a good night for those who are based in Hong Kong or mainland China. Thanks.

Operator

That does conclude our conference for today. Thank you all for participating. You may all disconnect.

Editor: Portions of this transcript that are marked (interpreted) were spoken by an interpreter present on the live call. The interpreter was provided by the Company sponsoring this Event.

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