Q2 2023 Earnings Prepared Remarks

August 21, 2023

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Zhao Bin, founder, chairman and CEO

Thanks operator, and welcome everyone to our earnings call.

Our revenue for the second quarter was 15.3 million dollars for Agora, down 5.6 percent year on year, mainly due to a challenging global macro environment and tightening financing conditions of certain customers. Our revenue was 131.5 million Renminbi for Shengwang, down 11.7 percent year on year if excluding revenue from the disposed customer engagement cloud business and K12 academic tutoring sector, mainly due to a slowing economy and fast evolving regulations in certain downstream verticals.

As of the end of this quarter, we had 1,560 active customers for Agora and close to 4,000 for Shengwang, an increase of 24 percent and 5 percent, respectively, compared to one year ago.

Now moving on to our business, product and technology updates for the quarter.

First, starting with Agora. We recently announced our partnership with ActiveFence, a leading global provider of AI-driven content detection and moderation services. ActiveFence's solutions keep end users safe from the widest spectrum of online harms, unwanted content, and malicious behavior, including adult content, bullying and harassment, child abuse, hate speech, illegal goods, violence, and more. We believe content moderation is particularly important for real-time engagement applications, given that content is generated and consumed in real time.

Through our extensions marketplace, ActiveFence's content moderation tools allow developers to add live audio and video content moderation functionality to their applications easily, without significant changes to their development processes. By detecting and removing all kinds of unwanted harms in real-time, Agora and ActiveFence can help customers better handle emerging online safety and compliance challenges, while boosting end-user engagement in a safer and more trusted environment.

On the use case side, over the past few quarters, we have seen an increase in real-time engagement adoption and usage from vertical social networks, or applications for interest-based communities. In typical use cases, creators, experts or influencers in a specialized area, such as meditation, yoga, astrology, religion, sports or creative arts, engage with their fan base through video calls or interactive livestreaming sessions.

A good example is Astrotalk, a prominent online astrology platform operating in over 60 countries with a network of over 5,000 astrologers. By leveraging Agora's technology, Astrotalk introduced an innovative use case that enables video calls between clients and astrologers to be broadcasted simultaneously to multiple potential customers. The objective was to create a platform that would show astrologers providing live predictions to clients. When customers observe others talking with the astrologer, they are more inclined to engage with the same astrologer. As a result, Astrotalk has experienced a remarkable threefold growth in active sessions following the launch of this feature.

Moving on to Shengwang. In the past quarter, we upgraded our solution for high-definition video calling and livestreaming. Previously, customers had to separately integrate our video-related products, features and third-party extensions, such as video enhancement, proprietary codecs, super resolution, beautification and other video effects, and it often took substantial time to find the most suitable architecture and specification for the customer’s unique use case, in order to deliver a balanced end user experience considering video quality, latency, fluency, functionality and device compatibility.

With our new use case-oriented solutions, customers can now easily access best practices tailored to their specific use cases, such as single-host livestreaming, host PK, host-audience interaction, multiple-host livestreaming and live shopping. Customers not only experience a shorter development time but also benefit from an enhanced user experience. This ultimately leads to improved end user retention and better monetization opportunities for our customers.

For example, a dating platform recently adopted our comprehensive solution to upgrade their one-on-one and livestreaming video from standard definition to high definition. In addition to the increase in video resolution, our solution also improved video quality in environments with poor or uneven lighting, provided video noise suppression, perceptual video coding and beautification. As a result of the high-definition upgrade, the average user duration increased by more than 10%. Meanwhile, hosting matchmakers and the dating platform itself also generated higher tips and revenue.

In early July, Shengwang was chosen as one of the 26 leading companies to showcase AI innovations at the 2023 World Artificial Intelligence Conference. Shengwang demonstrated its AI-powered noise suppression capabilities based on deep learning algorithms, which can effectively remove more than 100 types of unwanted background noises and echoes, ensuring a distraction-free and more immersive experience for end users.

Our AI noise suppression has been widely used by our customers across verticals such as telehealth, remote collaboration, social and gaming. For example, a voice social platform realized a 5% increase in average session lengths after integrating our AI noise suppression in their application.

Before concluding my prepared remarks, I would like to invite all of you to our upcoming RTE conferences.

On Agora side, the RTE program this year will consist of three events. We will launch with RTE Live Shopping, a month-long webinar series focused exclusively on this rapidly evolving space. Regional events for RTE India and RTE APAC will take place on October 5th. RTE India will be a fully virtual event highlighting how RTE technology is facilitating the evolution of new communities within Faith Tech/Astrology, Social, Media & Entertainment, Live Shopping, and Gaming. RTE APAC programs will be hosted in Korean and Indonesian languages, featuring key leaders and discussions around Metaverse, Education, and Live Shopping. We are excited to continue growing our global RTE community and fostering the spirit of innovation through our conferences.

On Shengwang side, the conference will be held in Beijing from October 24th to 25th. This year's conference will center around how the future of RTE will be shaped by generative artificial intelligence and high-definition immersive experiences. Together with industry-leading experts and practitioners, we will explore and envision the possibilities and advancements that these technologies will bring to RTE.

With that, let me turn things over to Jingbo, who will review our financial results.

Jingbo Wang, CFO

Thank you, Tony. Hello everyone.

Let me start by first reviewing financial results for the second quarter and then I will discuss outlook for the third quarter of 2023.

Total revenues were $34 million in the second quarter of 2023, a decrease of 16.9% compared with the same quarter last year, and a decrease of 6.6% quarter over quarter.

Agora Revenues were $15.3 million in the second quarter of 2023, a decrease of 5.6% year-over-year, and an increase of 1.3% quarter-over-quarter. The year-over-year decrease was primarily due to reduced usage of our products and customers' increased pricing sensitivity due to challenging macroeconomic environment starting from the second half of last year. The quarter-over-quarter increase was primarily due to usage growth and emergence of new use cases such as vertical social networks as Tony just mentioned.

Shengwang Revenues were RMB131.5 million in the second quarter of 2023, a decrease of 19.8% year-over-year, and a decrease of 9.9% quarter-over-quarter. If excluding revenues from the disposed CEC business and K12 academic tutoring sector, Shengwang Revenues decreased 11.7% year-over-year, and 8.8% quarter-over-quarter, which was primarily due to slowing general economic conditions and fast evolving regulations in certain downstream markets.

Dollar-Based Net Retention Rate for Agora is 108%. Dollar-Based Net Retention Rate for Shengwang is 91%, excluding revenues from the K12 academic tutoring sector.

Moving onto cost and expenses. For my following comments, I will focus on non-GAAP adjusted financial measures, which exclude share-based compensation expenses, acquisition related expenses, amortization expenses of acquired intangible assets, income tax related to acquired intangible assets, impairment of goodwill, depreciation of property and equipment and amortization of land use right.

Adjusted gross margin for the second quarter was 67.2%, which was 2.6% lower than Q2 2022, mainly due to a change in product mix, and was flat compared to Q1 2023.

As mentioned in previous earnings calls, we restructured and reduced our global workforce in Q4 2022, and we have continued to implement effective expense controls. As a result, adjusted R&D expenses were $16.6 million in Q2, decreased 37.4% year-over-year. Adjusted R&D expenses represented 48.8% of total revenues in the quarter, compared to 64.8% in Q2 last year.

Adjusted sales and marketing expenses were $7.1 million in Q2, decreased 34% year-over-year. Sales and marketing expenses represented 20.9% of total revenues in the quarter, compared to 26.3% in Q2 last year.

Adjusted G&A expenses were $6.2 million in Q2, decreased 9.5% year-over-year. G&A expenses represented 18.2% of total revenues in the quarter, compared to 16.6% in Q2 last year.

Adjusted EBITDA was negative $6.6 million, translating to a 19.5% adjusted EBITDA loss margin for the quarter, significantly lower than the adjusted EBITDA loss margin of 37.4% in Q2 last year.

Investment loss was $1.9 million in Q2, primarily due to loss on investments in certain private companies of $4.9 million, which was offset in part by the fair value change in equity investments of $3 million.

Non-GAAP net loss was $6.6 million in Q2, translating to a 19.4% non-GAAP net loss margin for the quarter, compared to a net loss margin of 50.8% in Q2 last year and 25.1% in Q1 this year.

One extraordinary P&L item in this quarter is the impairment of goodwill. In Q2, we completed the integration of Easemob's operations, after which we only identified one reporting unit. Considering the negative impact on market demands as a result of a challenging global macroeconomic environment and regulatory changes in certain sectors, we performed quantitative impairment tests on goodwill and recognized the full impairment of goodwill in relation to the Easemob acquisition, which is $31.9 million. As of the end of Q2, there was no more goodwill outstanding on our balance sheet.

Now turning to cash flow, operating cash flow was negative $5.3 million in Q2, compared to negative $23.8 million last year. Free cash flow was negative $5.6 million, compared to negative $24.2 million last year.

Moving onto balance sheet. We ended Q2 with $391.6 million in cash, cash equivalents, bank deposits and financial products issued by banks. Net cash outflow in the quarter was mainly due to free cash flow of negative $5.3 million, and share repurchase of $21 million.

Since the board approved our share repurchase program in February 2022 and as of June 30, 2023, we have returned approximately $82.0 million to shareholders through share repurchases, demonstrating the board's commitment to safeguarding shareholder value and its confidence in the long-term prospect of the Company. As of June 30, 2023, the Company had approximately 97.5 million ADSs outstanding, reflecting a reduction of approximately 14.9 million ADSs, or 13% reduction of total shares outstanding, from January 31, 2022 before the share repurchase program started.

So far, we have completed 41% of our US$200 million share repurchase program, which will expire at the end of February 2024, and we intend to continue to undertake this meaningful capital return to our shareholders.

Now turning to guidance. For the third quarter of 2023, we currently expect total revenues to be between US$34.5 and 36.5 million. This forecast reflects our current and preliminary views on the market and operational conditions, which are subject to change.

In closing, we are confident about the long-term prospect of the global market for Real-Time Engagement technology, and we are well prepared for near term uncertainties and challenges. Thank you to both Agora and Shengwang teams for your hard work and to our investors for your trust. Thank you everyone for attending the call today.

Let's open it up for questions.