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NQ - Q3 2011 NetQin Mobile Inc Earnings Conference Call

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PRESENTATION

Operator

Good morning and thank you for standing by for NetQin Mobile Incorporated Third Quarter 2011 Earnings Conference Call. At this time all participants are in a listen-only mode. After management's prepared remarks there will be a question and answer session.

Today's conference is being recorded. If you have any objections you may disconnect at any time. I would now like to turn the call over to your host for today's conference, Mr. Mattan Lurie, NetQin's Director of Investor Relations and Corporate Development.

Mattan Lurie - NetQin Mobile Inc. - Director - IR & Corporate Development

Hello and welcome to NetQin Mobile Incorporated's third quarter 2011 earnings conference call. The Company's earnings results were released yesterday and are available on the Company's IR website, ir.netqin.com, as well as on newswire services.

Today you will hear opening remarks from Dr. Henry Yu Lin, NetQin's Founder, Chairman and CEO, followed by NetQin's Chief Strategy Officer, Will Jiang, and Chief Financial Officer, Suhai Ji, who will take you through the operational and financial results for the third quarter of 2011 and give guidance for the fourth quarter and full year of 2011. After their prepared remarks Dr. Lin, Mr. Jiang and Mr. Ji will be available to answer your questions.

Before we continue please note that the discussion today will contain certain forward-looking statements made under the Safe Harbor provisions of the US Private Securities Litigation Reform Act of 1995. These forward-statements are subject to risks and uncertainties that may cause actual results to differ materially from our current expectations. NetQin does not assume any obligations to update any forward-looking statements except as required under applicable law.

Also please note that some of the information to be discussed includes non-GAAP financial measures as defined in Regulation G. The most directly comparable US GAAP financial measures and information to reconcile these non-GAAP financial measures

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to NetQin's financial results were prepared in accordance with US GAAP are included in NetQin's earnings release which has been posted on the Company's IR website at ir.netqin.com.

Finally, as a reminder this conference is being recorded. In addition, a webcast of this conference call will be available on NetQin's Investor Relations website. I will now turn the call over to NetQin's Founder, Chairman and CEO, Dr. Lin.

Dr. Henry Yu Lin - *NetQin Mobile Inc. - Chairman, CEO*

Thank you, Mattan, and welcome to everyone on the call. I'm happy to report that we have had another strong quarter in which we delivered record revenue and beat the high end of our previous guidance. Even against the backdrop of continuous global economic uncertainty our business and user growth haven't experienced any slowdown. And in fact our growth momentum remains as strong as ever.

We continue to benefit from a record increase in global smartphone shipments and the tremendous ability of mobile Internet applications. Mobile users are increasingly aware of the severity of today's mobile Internet security risks and are implementing mobile security solutions in their phones.

NetQin continues to be well positioned to seize this global market opportunity.

The third quarter marked our second straight record-breaking quarter since our IPO in May of this year, which gives further evidence to the management execution, capability at NetQin. And we are confident that we will continue to deliver strong results give our solid business fundamentals and outstanding growth prospects.

In addition to our impressive third quarter results the last few months also featured several key business developments and operational achievements. Now I would like to hand over to Will Jiang our Chief Strategy Officer who will give you more details on those achievements.

Will Jiang - *NetQin Mobile Inc. - Chief Strategy Officer*

Thank you, Henry, and good morning to everyone on the call. As Henry mentioned we did have a very strong quarter in terms of business execution and I would like to highlight some of the key developments.

First our flagship mobile security product was recently evaluated by the prestigious West Coast Labs. It measured our mobile antivirus capability against eight other mobile security providers including Symantec, McAfee, AVG, Kaspersky, Lookout, F-Secure among others. The competitors were measured across ten key areas. This was a very comprehensive study which tested the ease of installation, effectiveness of malware scanning, real-time protection, account data backup functions and remote-wipe capabilities.

We are very proud of NetQin's outstanding performance in all categories, particularly our 96% detection rate of the threat samples used in the testing process, which was 55% more effective than the next best security solution tested. Our leadership in technology is validated and this will also further increase our influence in the mobile ecosystem.

The report concludes that NetQin indeed has the best overall mobile security solution available and West Coast Labs awarded its Checkmark Certification to NetQin's Mobile Security 5.0. This is another strong endorsement from a third party industry participant who is putting their reputation and credibility behind NetQin's product. The report right now is publicly available for download at West Coast Labs' official website and on NetQin's official IR website.

Second, we continue to invest and expand our R&D capabilities. In the third quarter we established NetQin's research center in the US in collaboration with one of the world's leading experts on mobile security, Professor Zhang of North Carolina State

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University. The center's primary focuses include identifying and monitoring mobile security threats, which will further strengthen our leadership in security capabilities and global research footprint.

Already this joint effort has enabled us to first identify and resolve several significant mobile malware threats, including the most recent AnserverBot attack. Third, regarding product developments, we updated most of our existing products in the third quarter and launched yet another addition to our growing family of products, NiceDay. It is a user-friendly smart calendar application for iOS and Android devices.

NiceDay provides user with calendar management and synchronization, entertainment and restaurant accommodations. It also integrates with Sina's microblogging services, Weibo. Within 40 days of launch NiceDay was already the number one productivity application in China's iTunes app store.

Fourth, we continue to make progress in our international expansion and have made important hires to lead this expansion effort. We recently recruited Mr. Geoff Casely, a mobile industry veteran previously at Nimbuzz in UK, to spearhead our European and Middle East expansion. Geoff is the second industry veteran to join us at the managing director level following our other hire from Motorola veteran, Mr. Chris Stier to head up the Americas.

And last, we saw continued market traction with new partnerships. We announced in the last quarter a global go-to market agreement with Brightstar and mobile security agreement with Taiwan Mobile. Both these framework agreements gave us strong endorsements from the leading industry players and will continue to provide consumers with easier and more widespread access to our mobile security application and services.

The mobile security agreement with Taiwan Mobile will enable us to offer our mobile security services for Android users in Taiwan via their official applications store and also through pre-installation in selected Android smartphones distributed by Taiwan Mobile. These applications are already available and are currently being downloaded by consumers in Taiwan.

Through our new relationship with Brightstar we expect to immediately benefit from Brightstar's global network, which includes over 210 carrier relationships around the world reaching more than 80,000 points of sales. Although we're not yet in the position to quantify the financial impact of these two deals we believe both agreements are of strategic importance to our Company, enabling us to better position ourselves in a more global mobile ecosystem.

Above are just some of the few key developments I would like to highlight and I will now turn the call over to our CFO, Suhai Ji, to speak to the financials and operational results.

Suhai Ji - NetQin Mobile Inc. - CFO

Thank you, Will, and hello to everyone on the call. At the outset please note that unless stated otherwise all the numbers I will discuss today are in US dollars.

In the third quarter we once again saw robust growth in both our operating and financial metrics. First, regarding our operating metrics we reached new highs again in all three sets of numbers that we disclose.

Our accumulative registered user accounts were about 123 million at the end of the third quarter of 2011, compared with 60 million at the end of the third quarter of 2010 and 103 million at the end of the previous quarter. That's about 104% year-over-year growth and a 19% sequential growth.

The breakdown between China and overseas user accounts are now 64% versus 36%, compared to 69% versus 31% at the end of the third quarter of 2010 and 65% versus 35% at the end of the previous quarter. So the overseas user base is growing faster from a smaller base.

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Our average monthly active user accounts were about 43 million at the end of the third quarter of 2011, compared with 21 million for the third quarter of 2010 and 36 million in the previous quarter. That's about 103% year-over-year growth and 17% sequential growth. Active user accounts continue to make up roughly 35% of the registered user accounts so the breakdown between China and overseas for active user accounts are about the same as registered user accounts.

Our average monthly paying user accounts were 5.0 million at the end of the third quarter of 2011, compared with 2.8 million for the third quarter of 2010 and 4.2 million in the previous quarter. That's about 79% year-over-year growth and 18% sequential growth. The breakdown between China and overseas paying accounts are 70% versus 30%, respectively, compared to 80% versus 20% for the third quarter last year and 72% versus 28% for the previous quarter.

So it's obvious that our overseas paying users now account for a greater proportion of our overall total paying users, but the conversion ratio from active to paying users remained roughly confident on an overall basis at about 12%. The conversion ratios for both China users and overseas users were almost unchanged at about 13% and 10%, respectively, for the past two quarters.

The strong increase in our user base was again driven primarily by the growth in the smartphone industry and the proliferation in mobile Internet applications, including mobile security and productivity products. It also reflects our execution ability to establish effective user acquisition channels and the delivered user-friendly innovative products to drive user adoption.

Now moving on to the financials, total net revenues in the third quarter were \$11.3 million, an increase of 110% from \$5.4 million in the same period in 2010 and 28% from \$8.9 million in the previous quarter. The significant year-over-year and sequential increases in revenues were mainly due to the strong growth in revenues from premium mobile Internet services.

Net revenues from premium mobile Internet services in the third quarter were \$10.3 million, up 122% year-over-year and 34% sequentially. The increases were primarily due to the strong and steady growth in the number of paying user accounts, which reflected growth in the number of registered and active user accounts, as well as increased use of our premium services, particularly among our overseas paying user accounts, which generally pay a higher subscription fee.

Revenue contribution from overseas users now accounted for 49.1% of total net revenues from premium mobile Internet services in the third quarter compared with 41.4% in the third quarter of last year and 49.5% in the previous quarter. In terms of average revenue per user, or ARPU, as measured on a quarterly basis, our branded quarterly ARPU in China and overseas users together improved from \$1.82 for the second quarter to \$2.05 for the third quarter, compared with \$1.69 for the third quarter a year ago. ARPU for domestic China users increased significantly from \$1.27 to \$1.50.

That's because we have converted most of the pay-per-use users in China who only pay RMB2 per use to updated virus library to monthly subscription-based users who pay RMB5 per month. The pay-per-use users now accounted for less than 10% of the total paying users in China.

ARPU for overseas users increased slightly from \$3.24 in the second quarter to \$3.34 for the third quarter, compared with \$3.58 for the third quarter a year ago. So overseas ARPU tends to fluctuate because it depends on the pricing strategy we have in each country as we set our prices between \$2.00 to \$5.00 per month in different countries according to local market conditions.

Net revenues from other services in the third quarter of 2011 were \$1 million, up 32.7% year-over-year and down about 15% sequentially. The year-over-year increase was primarily due to the growth in revenues from secured download and delivery services for mobile applications produced by third parties. As we experienced faster growth in our core business segment, our mobile, on premium mobile Internet services, net revenues from other services as a percentage of total revenues declined to 9% from 13% in the previous quarter.

Before moving on to the cost of revenues and operating expenses I want to refer you to our disclosure on non-GAAP financial measures which was included in our official Press Release. The only difference between our GAAP and non-GAAP numbers are share-based compensation, or SBC expenses. SBC expenses are included across cost of revenues and operating



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expenses on a GAAP basis, but are excluded to derive our non-GAAP numbers. Most of the SBC expenses are incurred in operating expenses line items and we have included a reconciliation table in our earnings release showing the detailed calculations.

So cost of the revenues in the third quarter of 2011 was \$2.2 million, up 64% year-over-year and 21% sequentially. The increases were primarily due to increased customer acquisition costs and higher staff costs from salary and headcount increases. The SBC amount in cost of revenue is insignificant so there is little difference between GAAP and non-GAAP figures.

As a result, gross profit in the third quarter was \$9.2 million, up 125% year-over-year and 30% sequentially. Gross margin was about 80.7% in the third quarter of 2011, up from 75.4% in the same period last year and relatively flat from the previous quarter. We expect gross margin to stabilize between 76% to 81%. As stated in the previous earnings calls, the gross margin for our business has a lot to do with our revenue recognition policy and how we collect revenues from China and overseas' users; thus from an analytical point of view management places less emphasis on gross margin than on operating margin, especially non-GAAP operating margin.

Now on to the operating expenses, for the third quarter of 2011, third quarter of 2010 and second quarter of 2011 we recorded total SBC expenses of \$2.6 million, \$0.7 million and \$3.2 million, respectively, across the three operating expenses line items.

Compared with the third quarter of 2010 the larger SBC expenses this quarter were largely due to the options and the restricted stock granted to certain employees before the Company's May IPO and in the second quarter of this year compared with the last quarter, i.e. the second quarter, the sequential decrease in SBC expense was due to the smaller impact from the immediate vesting of certain options upon IPO in the second quarter. And we expect SBC expenses for the fourth quarter to be around \$2.5 million, not counting on any additional options or stock granted by the Company.

For these reasons and to make the quarterly comparison more consistent I would like to address the following line items on a non-GAAP basis which excludes SBC expenses. Non-GAAP selling and marketing expenses increased 36% year-over-year and 50% sequentially to \$1.3 million in the third quarter of 2011. The year-over-year and sequential increases were primarily due to higher marketing and advertising spending, higher staff costs from salary increases and the greater traveling and entertainment expenses, partially offset by lower office-related expenses.

For example, in the third quarter, we launched advertising campaigns on focused media, the elevator screens, and on certain bus media in Tier 1 cities in China, which drove up the market expenses significantly. Non-GAAP general and administrative expenses increased 371% year-over-year and 40% sequentially to \$2.1 million in the third quarter of 2011. The year-over-year and the sequential increase were primarily due to higher staff costs from salary increases, greater office-related expenses and increased traveling and undetermined expenses.

In the third quarter we hired more senior staff for overseas offices which drove up the staff costs considerably. And our business expansion in overseas markets also gave rise to higher office-related expenses and traveling expenses.

Non-GAAP R&D expenses increased 43% year-over-year and 6% sequentially to \$1.04 million in the third quarter of 2011. The increases were primarily due to higher staff costs from salary increases and to a lesser extent increased traveling and entertainment expenses. So as a result non-GAAP total operating expenses were \$4.4 million in the third quarter of 2011, compared with \$2.2 million in the same period 2010 and \$3.4 million in the previous quarter.

Our non-GAAP operating income was \$4.7 million in the third quarter of 2011, up 147% year-over-year and 28% sequentially. Non-GAAP operating margin remained essentially the same at 41.6% for the third quarter and second quarter of 2011 compared with 35.4% in the third quarter of 2010.

For the third quarter we also recorded significant growth in certain below the operating line items such as foreign exchange gains and interest income, both on a year-over-year and sequential basis. We had a foreign exchange gain of \$1.6 million,

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primarily attributable to the appreciation of RMB against the US dollars when a portion of our IPO proceeds was converted into RMB and placed in bank deposits during the second and third quarter of this year.

And our interest income was \$0.5 million, which was primarily due to the higher deposit positions resulting from the May IPO proceeds. Income tax expenses were \$0.8 million and the effective tax rate was 1.8% in the third quarter of 2011, compared with the income tax expenses of \$0.2 million in the third quarter of 2010 and the income tax benefit of \$0.2 million in the second quarter of 2011. The low effective tax rate was primarily due to the preferential tax treatment enjoyed by certain subsidiaries of the Company.

Net income attributable to NetQin was \$4.3 million in the third quarter, compared with \$1 million in the same period in 2010 and \$1.1 million in the previous quarter. Non-GAAP net income attributable to NetQin, which excludes SBC expenses, was \$7 million, compared with \$1.7 million in the same period last year and \$4.3 million in the previous quarter.

I would like to highlight that starting in the third quarter this year and going forward net income attributable to NetQin will be exactly the same as net income attributable to NetQin common shareholders given all of the Company's outstanding preferred shares were automatically converted to common shares immediately upon the completion of our IPO in May.

On the EPS basis our third quarter GAAP net income per ADS is about \$0.10 and the non-GAAP net income per ADS is about \$0.15. To ensure maximum financial transparency we have continued to disclose the full set of three financial statements, including our cash flow statement.

Our operating cash flow for the third quarter was a net inflow of \$2.6 million, compared with a net cash outflow of \$0.8 million in the same period a year ago and an inflow of \$3 million in the previous quarter. And our deferred revenue has grown further to \$6 million from \$4.6 million at the end of the previous quarter, which gives us better visibility and more confidence in future revenues.

As a last point, I would also like to update you on the status of our senior management and director share purchase program that was announced on June 16th of this year. We announced that our CEO, COO and two board directors intended to use their personal funds to purchase up to an aggregate total of \$2 million worth of NetQin ADS in open market transactions over a six-month period.

As of end of the third quarter, September 30, 2011, those officers and directors have collected, purchased a total of 122,700 ADS, amounting to approximately \$700,000. So the average purchase price per ADS is about \$5.70. They may continue to buy the Company's ADS, subject to applicable legal restrictions and other factors as they continue to believe in the long-term success of NetQin.

So looking forward to the fourth quarter and beyond, we expect net revenues to be in the range of \$12.4 million and \$12.7 million, representing year-over-year growth of 97% to 102% and quarter-over-quarter growth of 10% to 12%. For the full year of 2011 we are raising our guidance from the previously issued \$38.3 million to \$38.8 million to \$40.2 million to \$40.5 million, representing year-over-year growth of 127% to 129% from the previous year of 2010.

So in conclusion we indeed had an excellent third quarter and for the second straight time after our IPO in May we delivered another quarter above promise. We remain very confident on our business fundamentals and look forward to bringing more exciting news and progress to our shareholders when we report our fourth quarter and full year 2011 results next year.

So this concludes my remarks and I will now turn the call over to the operator to open the lines for questions. Operator?

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QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions). Your first question comes from Andy Yeung of Oppenheimer. Please ask your questions.

Andy Yeung - Oppenheimer & Co. - Analyst

Hi. Good evening, Henry, Suhai and Will. Thank you for taking my questions. My first question is about monetization. As you mentioned, your quarterly ARPU growth developed \$2.05 per quarter. And you also mentioned that some of the conversions are for domestic users from pay-per-view to subscriptions have helped boost the ARPU. And I just wanted to know like if there's any mixed shift in your payment channel on prepaid cards that may also boost that ARPU? And also how high do you think both the domestic ARPU and overseas ARPU can get to?

Suhai Ji - NetQin Mobile Inc. - CFO

Thanks, Andy, and I will address your questions. Yes indeed, our ARPU has improved quite a bit on a blended basis from about \$1.82 for quarter in the second quarter to about \$2.05 in the third quarter. And that's on a blended basis. In particular in China our ARPU has increased significantly, as I mentioned on the call earlier. It went from \$1.27 to \$1.50. And that's again is due to the conscious decision for the Company to try to convert as many as pay-per-use users to on a subscription, monthly based users.

And right now that total number of pay-per-use users has come down below 10%. And that was the major reason to drive up the domestic ARPU. Of course ARPU also has to do with the payment channels, either through the prepaid cards or through the carrier channel.

And we for the third quarter think the mixes we see are higher, increased proportion of prepaid cards from the previous quarter, the majority in China as we have stated before still coming from the carrier and XP, and that's through the majority of people would choose to pay. And then for overseas ARPU, again, as I mentioned it tends to fluctuate a little bit as we monetize in different markets and use a different price.

So it's harder to predict the trend because if product goes up and down from time to time depending which new market we entered and start to monetizing. So in terms of a future trend I would say in China because we have fixed the price unchanged since the fourth quarter of 2009 that was the last time we actually raised the price from RMB4 from to RMB5 per month. And we haven't done that for increase any price for two years.

So unless we increase the price and in my model I just factor in the sort of consistent ARPU to be conservative, and also we definitely try to optimize our payment channels, but that has a lesser effect as compared to the pay-per-use users' conversion and a price increase. And for overseas we do use \$2 to \$5 and per month. And it depends on which country we enter and that ARPU will tend to fluctuate, so hopefully this answer to your question.

Andy Yeung - Oppenheimer & Co. - Analyst

Yes, it does. And then also just about your expenses, and you mentioned that you did some marketing campaigns during the quarter in China. Do you have any other significant marketing campaigns scheduled for this 4Q and in coming quarters both domestically or in overseas? And in terms of operating expenses targets what's your longer term target for operating expenses as a percentage of revenues?

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Suhai Ji - NetQin Mobile Inc. - CFO

Yes. Thanks, I will again address this question. Yes, our operating expenses, especially the non-GAAP operating expenses have gone up about 33% over the previous quarter. The bulk of the contribution comes from the selling and the marketing expenses which went up 50% from our previous quarter. And the non-GAAP G&A expenses went up 39% and R&D expenses went up 9%.

I think in the third quarter, as I mentioned, we did more advertising. For the first time we did some brand advertising using focused medias, elevator panels and also certain bus media in the Tier 1 cities. And in the second quarter we, as you probably saw from our last [ter and is co] we actually had the decrease in marketing expenses. So I think in terms of sales and marketing it's hard to predict a trend because we make that decision on a quarter by quarter basis.

I think in the fourth quarter we probably are going to focus more on the product development and also, as you may be aware, we are doing some kind of rebranding as well. So we will launch our new brand for especially an overseas market in January next year. So before that, especially in the overseas market I don't think we are going to incur heavy marketing expenses for the next quarter, but in the first quarter 2012 you should see an uptick again in marketing expenses.

So we make that decision based on our business needs and we do that on a quarter-on-quarter basis. And longer term I think operating margin as you saw, especially the non-GAAP operating margin this quarter is almost the same as last quarter at about 42%.

I think we want to for this year and next year we probably want to maintain no lower than this margin, but also we want to keep some flexibility as we enter new markets and incur more sort of marketing spending. And we believe that 42% is already a very healthy operating margin that we can maintain. And as you saw our net margin was actually much higher than that because we have other income coming as well. So towards the end of this year I think we want to maintain if not go even higher at this level, even though we could have gone much higher, but we want to remain the flexibility.

Andy Yeung - Oppenheimer & Co. - Analyst

Got it. And then one final question about the smartphone operating system landscape, obviously Android is doing quite well these days and so maybe you can give us some color on the distribution of your new account by operating systems. That would be helpful. Thanks.

Will Jiang - NetQin Mobile Inc. - Chief Strategy Officer

Hi, Andy. This is Will. Android still represents actually the fastest growth in our smartphone mix. Symbian is still growing. IOS momentum really picked up last quarter in China after the release of NiceDay. It's a Chinese-only version.

In fact, our NiceDay did peak as the number one productivity app on the iOS iTunes store. So we are actually planning to release our Windows phone mobile security probably in Q4 as well. So basically to answer your question we think that the overall macro environment with Android becoming more and more dominant in a smartphone our market share we do expect Android roll outs to continue. Symbian will eventually be phasing out with the replacement of Windows phones, along with IOS will remain stabilized.

Blackberry we haven't seen any significant growth mainly due to the macro environment with Blackberry's own market share decrease. So basically we look forward to a strong overall growth in the Android market as our brightest point.

Andy Yeung - Oppenheimer & Co. - Analyst

Great. Thank you.

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Operator

Your next question now comes from Mark Murphy of Piper Jaffray. Please ask your questions.

Mark Murphy - Piper Jaffray - Analyst

Yes. Thank you. Congrats on the results. I was just noticing here that your sequential growth accelerated to 28% in Q3 and wondering to what do you attribute that acceleration, whether it was a function of your consumer marketing campaign or --

Will Jiang - NetQin Mobile Inc. - Chief Strategy Officer

Sorry, Mark. Hey, Mark, Mark?

Mark Murphy - Piper Jaffray - Analyst

Yes.

Suhai Ji - NetQin Mobile Inc. - CFO

Sorry, okay. Hold on one second. I think there are some investors saying they could not get in on the call. So just hold on one second. Let me -- let us check on that, okay? Just hold on for one minute. Yes hi, Mark, sorry we were just addressing some of the technical issues apparent from the numbers that were messed up. Some investors cannot get in, but anyway so can you just repeat your first question? I'm sorry.

Mark Murphy - Piper Jaffray - Analyst

Sure. So I was just noting that your sequential growth accelerated to 28% in Q3 and I'm wondering what you would attribute the acceleration to, whether it was due to some of the partnerships that you've signed maybe in the past year or was it more a function of overseas strength or your -- could it have actually been your consumer marketing campaign in China producing some results, or some other factors? There just in other words I'm just wondering what was it that you think was incrementally stronger in Q3 than in Q2.

Suhai Ji - NetQin Mobile Inc. - CFO

Sure, yes. I think. As you know that we completed our IPO in the middle of Q2 I think we definitely had a very strong brand boost, especially the people in China. They realized we are actually a public listed company. That raised our profile considerably.

And in Q3 we see actually strong growth from China and that's also the ARPU has increased quite a bit. And also that has to do with what I earlier mentioned, the marketing campaign we did in the third quarter. More people are becoming aware of our brand and more people are willing to try our product.

So I think it's really a combination of things, but the bottom line of the driver is still really the continued growth of the smartphone shipment in China and globally and people's awareness of the mobile security is on the rise. And so our revenue model is very simply. It's purely driven really by the number of users that we attract to use our products and services.



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Mark Murphy - Piper Jaffray - Analyst

Okay. Thank you. I wanted to ask next about the test results from West Coast Labs. You had this 96% identification rate. I think we would have assumed that perhaps some other competitor could at least do a halfway decent job of that, maybe 70% or 80% recognition, but instead it looked like two of the competitors actually found 0% of the threats. And the second best competitor was only identified about 41%.

And it doesn't seem very valuable to consumers if you can only identify 41%. So I think my question is do you think that this report from West Coast Labs will make it easier for NetQin to win future partnerships because presumably any of the handset makers or the carriers want to use an effective product?

Will Jiang - NetQin Mobile Inc. - Chief Strategy Officer

Well, Mark, you're absolutely correct. In fact this -- after this report is published we received a lot of partners inquiries regarding the report and this just shows that our leadership in the field is definitely undisputed.

And we believe the real reason behind of such big leadership in terms of our malware detection accuracy really has to do our intellectual property surrounding risk ranked proprietary engine, along with our capability of detecting malware faster and quicker than anyone else. This also shows that most of our competitors products are mainly wrapped around a in a way not effective engines and really they can't really do a job, a good job protecting consumers.

So once again many of the partners who are either already working with us or plan to work with us do look at this report very seriously and we certainly do believe this will help us to strengthen our relationship and further boost our pipeline in terms of partnerships.

Mark Murphy - Piper Jaffray - Analyst

And, Will, which types of partners did you get inquiries from after the report came out? Are you talking about major global handset makers? Are you talking about regional carriers or more of the distributors or something else?

Will Jiang - NetQin Mobile Inc. - Chief Strategy Officer

In fact we're getting inquiries from all of the above, so this report is West Coast Labs is a very well known, very well established, prestigious testing facility. So this report is widely distributed and so all of the above, equal participants are looking at this report very seriously.

Mark Murphy - Piper Jaffray - Analyst

Okay, good. Thank you. And the last question I wanted to just go back to the Android platform. And I think in Q2 you had estimated the number of new Android malware varieties that you had seen in Q2. And I was just wondering if you happened to have any estimate of that number of new Android malware that you saw in Q3, or if you don't happen to have that handy, just any commentary on how rapidly is the malware volume growing? And did you see anything new in terms of the sophistication or the nature of the malware on the Android platform in Q3?

(Technical difficulty)

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Operator

Ladies and gentlemen, due to technical difficulty our conference will resume shortly. Please continue to stand by. Thank you for your patience. Thank you for holding. You are now back in the conference room. Please go ahead.

Will Jiang - *NetQin Mobile Inc. - Chief Strategy Officer*

Mark, would you please repeat the question? We were just dropped earlier.

Mark Murphy - *Piper Jaffray - Analyst*

Well, I was wondering -- I was asking about the Android platform, Will, and that I was wondering if you could estimate the number of new Android malware that you saw in Q3, because I think in Q2 you had tried to estimate that for us. I think it was over 1,000 or a couple 1,000. And so I'm just wondering if you could estimate how rapidly is that volume growing or and if you don't have that data could you talk just qualitatively about how quickly it's growing? And is there anything new in terms of the sophistication or the nature of the malware that you're seeing on Android?

Will Jiang - *NetQin Mobile Inc. - Chief Strategy Officer*

Certainly, Mark. In fact we've just recently concluded our mobile security report for Android platform for Q3. In fact, compared to Q2 we saw another spike in terms of newly discovered malware. It has already reached 2,700 malwares in Q3.

I'm talking about the number of new malware detected in Q3. This compared to nearly 2,000 in Q2 and around 1,000 in Q1. And in fact another number I can share is that these malwares that were detected in Q3 directly impacted or infected over two million handsets, or two million users who are using Android phones.

So really the threat is getting graver and we're in the grave danger in terms of more and more users getting infected. Another number we can share with you is that for the end server box, which was first discovered and announced by us near the end of August, also impacted directly more than 100,000 users in China.

So we like to actually we are being -- this current report is written in Chinese. We are in the process of translating this into English and we'll be published pretty soon in English media.

Mark Murphy - *Piper Jaffray - Analyst*

Okay. Thank you very much. That's all I had for now.

Operator

Your next question comes from Mike Walkley from Canaccord. Please ask your questions.

Michael Walkley - *Canaccord Adams - Analyst*

Great. Thank you. Can you guys hear me?

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Suhai Ji - NetQin Mobile Inc. - CFO

Yes, yes, just fine.

Michael Walkley - Canaccord Adams - Analyst

Okay. Okay, great. And congrats on the strong execution and then on building out your management team. Suhai, can you just help us in our models how we should think about R&D and G&A growth both in the Q4 and just kind of longer term?

Suhai Ji - NetQin Mobile Inc. - CFO

Yes, sure. You mean the operating expenses and the or specific on G&A and R&D? I discussed the sales and marketing already, right?

Michael Walkley - Canaccord Adams - Analyst

Exactly, yes, just because you did a good job on sales on marketing giving different timing of ad campaigns how that could that fluctuate quarter to quarter and sounds like it will go back up maybe again in Q1, but down in Q4, but just on the trajectory of R&D and G&A is obviously you guys are adding a lot of senior management to your team around the world as you continue to build out to your management team.

Suhai Ji - NetQin Mobile Inc. - CFO

Exactly. On G&A expenses I think third quarter was a 40% increase from last quarter and as you saw like we just mentioned that we had a significant hires in overseas market in last quarter alone. We appointed a managing director for the Americas and another one for EMEA for the Europe, Middle East and Africa.

So we are still continuing to invest. We believe one of the key elements of success in overseas expansion is really building a great team to lead that effort. So we will continue to invest and continue to hire the right people that will probably drive the cost up because hiring someone outside of China will be more expensive then doing it domestically. And so we see the G&A expenses we will stay, probably depending on our hiring plans, we will stay around maybe the percentage of total net revenue and budgeting maybe somewhere around 15%, 14%, 15% for non-GAAP G&A expenses as a percentage of revenue.

And then for the R&D that's where you see the real the leverage accounting our R&D expenses only increase about 6% from the previous quarter, again, because the bulk of our R&D is actually in China and also our R&D capability is highly scalable because even we are launching different applications on different platforms that incremental cost of the additional R&D expenditure is actually quite marginal. And that being said, we still continue to invest in R&D.

For example, we established a security lab in the US in the last quarter. And I think R&D will continue to account for maybe around maybe 10% of our total revenue going forward. And we expect that percentage to actually decrease over time as we realize the scalability of R&D.

Michael Walkley - Canaccord Adams - Analyst

Great. Thank you, Suhai. That's helpful, and just another quick question for you on the model. Is the 7.5% still a good tax rate to be thinking about for 2012?



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Suhai Ji - NetQin Mobile Inc. - CFO

Yes. I think that's -- I think to be conservative 7.5% is a good number to use. Of course we are still a high tax company and supported by the government. And we enjoy certain preferential tax treatment and for when certain policies expired we try to renew it, but I think 7.5% is a conservative number and that that is the number I am using in my model as well.

Michael Walkley - Canaccord Adams - Analyst

Okay, thanks. And, Will, just to follow up on the NiceDay app, I was very impressed with it. We visited your offices last month and good to see the strong take up already. Can you walk us through kind of your plans of how this drives future revenue growth besides creating maybe a more loyal customer base?

Will Jiang - NetQin Mobile Inc. - Chief Strategy Officer

Well, Mike, so NiceDay in fact, yes, when you visited NiceDay it was around number 16 on the app store and it peaked at number one after your visit. So really NiceDay provides a nice measurement of the active user community that we currently have. And it does open up the possibility of generating platform revenue to our Chinese-based users.

So currently we are not directly monetizing off NiceDay base and [plea] expanding user base and also increasing user stickiness, but in the long term we do see a huge potential like within the United States. You open up the further of possibility in bringing more recommendation and merchant revenue to our revenue mix.

Michael Walkley - Canaccord Adams - Analyst

Great. Thanks, and just one last question just on overall one of the scenes from our trip to China is clearly seeing an acceleration of smartphone growth in the region. Is there any update on OEM partnerships, or how you are getting preinstalled on phones that might be selling well or any color you can just share on a attach rates with the growing smartphone growth over there? Thank you.

Will Jiang - NetQin Mobile Inc. - Chief Strategy Officer

Sure. We do see our pre-installation user acquisition channel growing quite nicely. In fact as in the most recent quarter roughly over 20% of our users are coming through from pre-installation. And we also have a very busy pipeline in the works to sign up more handset OEMS in the future and we will announce them accordingly based on when the agreement is signed.

Michael Walkley - Canaccord Adams - Analyst

Great. And congratulations on the results and thanks for taking my questions.

Operator

Ladies and gentlemen, we have now reached the end of our question-and-answer session. I would now like to turn the call over to our host, Mr. Mattan Lurie. Thank you. Please go ahead.



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Mattan Lurie - NetQin Mobile Inc. - Director - IR & Corporate Development

Great. Well we'll conclude by thanking everyone for joining on the call and please feel free to reach out to us directly by emailing investors@netqin.com should you have any questions. This concludes NetQin's earnings call.

Operator

Ladies and gentlemen, that does conclude our conference for today. Thank you once again for your participation. You may all disconnect.

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