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NQ - Q4 and Full Year 2012 NQ Mobile Inc. Earnings Conference Call
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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the NQ Mobile's Fourth Quarter and Full Year 2012 Earnings Call. At this time, all participants are in a listen-only mode. There will be a presentation followed by a question and answer session.

(Operator Instructions)

I must advise you that this conference is being recorded today, Thursday the 7th of March 2013. I would now like to hand the conference over to your first speaker today, Michele Ma, NQ Mobile's Director of Investor Relations. Please go ahead.

Michele Ma - *NQ Mobile Inc. - Director - IR*

Hello, everyone, and welcome to NQ Mobile's Fourth Quarter and Fiscal Year 2012 Earnings Conference Call. The Company's earning results were released earlier today, and are available on the Company's IR website at ir.nq.com, as well as on news wire services.

Today, you will hear opening remarks from NQ Mobile's co-CEOs, Dr. Henry Lin and Omar Khan, followed by our Chief Financial Officer, Suhai Ji, who will take you through the Company's operational and the financial results for the fourth quarter and fiscal year 2012, and give guidance for the first quarter, and the full year of 2013. After their prepared remarks, Dr. Lin, Mr. Khan, Mr. Ji, our Chief Strategy Officer, Will Jiang, and the Chief Product Officer, Gavin Kim 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 provision 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 expectation. NQ Mobile does not assume any obligation to update any forward-looking statements except as required under applicable law.

Also please note that some of the information to be discussed include non-GAAP financial measures as defined in Regulation G. The most directly comparable US GAAP financial measures and information reconciling those non-GAAP financial measures to NQ Mobile's financial results prepared in accordance with US GAAP are included in NQ Mobile's earning release.



Finally, as a reminder, the conference is being recorded. In addition, a webcast of this conference call will be available on NQ Mobile? Investor Relations website.

I will now turn the call over to NQ Mobile? Founder, Chairman and Co-CEO, Dr. Lin.

Henry Lin - *NQ Mobile Inc. - Chairman & Co-CEO*

Okay. Thank you, Michele, and welcome to everyone on the call. The end of this quarter marked our first full year as a public company, and please to report that NQ Mobile once again we've earned outstanding quarter with record revenues. For the full year of 2012, we grew revenues by 126% from \$41 million last year to over \$92 million this year exceeding the high-end level our previously issued guidance.

This outstanding performance demonstrates our relentless focus on execution to take advantage of the record growth of the smartphone industry, and rightful awareness and importance of mobile security and privacy solutions globally.

Throughout the quarter, NQ Mobile had continued to execute our state strategy of expanding our core business from a consumer mobile security company into a mobile internet service company through the complete integration of NationSky asset. Through our NationSky business, NQ Mobile now delivers mobile device management, and managed mobility services to over 1,200 companies in China.

Feiliu also continues to deliver outstanding results, now responsible for operating 5 of the top 100 grossing mobile games iOS in China. As a whole, NQ Mobile's portfolio now includes internet mobile security, and mobile games and advertising for consumer market., and NQ Mobile's security mobile device management and managed mobility services for the enterprise market.

Looking forward to the future for NQ Mobile now seems even brighter. The depth and breadth of our full mobile internet security portfolio positions us to effectively monetize the growth of the mobile internet for both consumers and enterprises worldwide.

2012 was the characterized as a year for business expansion, challenge, and business process maturation, and outstanding financial performance. It is with confidence that we look forward to the year 2013.

I'd like to hand the call over to my partner, and NQ Mobile's co-CEO, Omar Khan, who will give you more details on some of the key developments in our business.

Omar Khan - *NQ Mobile Inc. - Co-CEO*

Thank you, Henry, and hello to everyone on the call. It was quite an amazing first year as co-CEO of NQ Mobile. Henry and I set out with a very ambitious set of targets and plans for 2012. I'm very proud of the record-setting results that we achieved in 2012 achieving the initial targets we set for the year.

As Henry stated, we achieved \$92 million in net revenue in 2012, again exceeding the high-end of our latest guidance. Even without taking into account the revenue contribution of Feiliu and NationSky, we achieved outstanding organic growth rates in our consumer security business of 92% year-over-year to a total of \$79 million.

Growth remained strong both in China and the international markets. The international market once again accounted for 54% of the consumer security business in the fourth quarter.

A year ago, enterprise was an insignificant part of our business. I'm proud to report that in the third and fourth quarters, enterprise accounted for 17% and 22% of our business, respectively. Our NationSky subsidiary now serves over 1,200 enterprises -- enterprise customers in China.



In the fourth quarter, we added Citibank, DBS Bank, Cosco, which is a shipping company out of China, as well as Generali China Life Insurance with customers in China. In addition, we continued to execute our synergy between our core NQ business and NationSky. We added enterprise mobile security to the solution framework that NationSky offers its customers.

Finally, we recently announced NQSky, our mobile device management platform. We are very excited by the customer interest we've seen, now being piloted by multiple large enterprise customers in China. In my discussions with TIOs, their top concern in the adoption of BYOD, or bring-your-own-device to work, and mobilizing their workforce, is application and data security.

This is exactly why we see the opportunity to differentiate our MDM platform by incorporating a robust end-point security framework. As one of our key team members likes to say, we're putting the security back into mobile device management.

As Henry mentioned, we completed the acquisition of Feiliu in the fourth quarter. We not only see strong growth ahead for our mobile games and advertising business, but we also see significant synergies with our consumer security business. We have already begun the integration of marketing, user acquisition, and the operations function between the two businesses.

In addition, we are planning to implement a payment method for our mobile security application where users who are mobile gaming consumers will be able to obtain a credit that can be used for paying for premium mobile security features.

We also continue to leverage Feiliu's interesting social communities and digital storefront for our user acquisition. Stay tuned for additional product synergy that we have on our road map.

We will continue to report top line revenue for each segment -- consumer mobile security, and mobile games and advertising. But the full P&L will be reported as the consumer business for NQ Mobile because of the synergies and integration that we're undergoing.

The investments we have made in the global expansion of our business in 2012 included the recruitment of a top-tier team, building out our international headquarters in Dallas, Texas, and driving our distribution relationships with global partners. All have been a phenomenal success.

We continue to deliver results on the international front, building our strong retail component of our business with access to over 1,600 retail stores in the US, and over 2,800 locations worldwide. Recently, we announced additional retail partnerships with Diamond Mobile and 4G Wireless, both authorized Verizon retailers.

Performance at retail was strong during the holiday period with TCC, The Cellular Connection, and A Wireless, both achieving over 20% attach rates in the month of December. With a strong pipeline of new retail partners that have yet to be announced, we expect to continue to grow our retail footprint throughout 2013.

We also continue to receive strong validation from carriers in the international markets for our products and services. Last month, we announced that US Cellular will begin offering Family Guardian under the name of US Cellular Family Protector to its 5.9 million customers.

Most recently, NQ Mobile and America Movil, the world's third largest mobile operator in terms of subscribers, announced that the operator will offer NQ Mobile Security, NQ Mobile Vault, and NQ Family Guardian to America Movil's 256 million subscribers in 18 countries, including Mexico and Latin America.

We have continued to win awards and accolades for our products. NQ Family Guardian and NQ Mobile Security were both awarded top 25 apps at TES.

In the fourth quarter, we also announced the collaboration with the FCC, the Federal Communication Commission on their smartphone security checker.



Finally, our technology continues to be a key differentiator of NQ Mobile. In January, we discovered the most significant mobile crack using our RiskRanker technology called Bill Shocker. Bill Shocker infected over 620,000 users in China by taking remote control of users' smartphones, sending SMS messages without the user's knowledge. It was spread through hacked and non-legitimate versions of applications, such as QQ Messenger, and Sohu News distributed through third-party app stores.

Malware activity has continued to grow at aggressive rates. In 2012, we discovered over 65,000 new unique malware, up from 25,000 the year prior. The US has now become a top five infected market with malware originating from a global landscape.

Looking forward, as Henry states, NQ Mobile's future now shines even brighter with the complete list of our product offerings, our unprecedented access to consumers and enterprise customers globally, and our continued leadership and technology and innovation, NQ Mobile is well-positioned to effectively monetize the growth of the mobile internet for both consumers and enterprises globally.

With that, I now turn the call over to our CFO, Suhai Ji to speak to the third quarter -- the fourth quarter financial and operational results.

Suhai Ji - NQ Mobile Inc. - CFO

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

We finished the year 2012 with a strong fourth quarter, and this marks the seventh consecutive quarter that we delivered on or above promise to our shareholders. In the fourth quarter, we again saw strong user growth, and reached new highs in all three sets of operating metrics that we discuss.

Our accumulated registered user counts reached about 283 million at the end of 2012, up 93% year-over-year, and 17% sequentially. Overseas users now account for 42% of the total registered users, up from 38% at the end of 2011, and 41% at the end of the previous quarter.

Including Feiliu's 67 million registered user counts, we had total registered user counts of 351 million as of December 31, 2012.

Our average monthly active user counts were about 98 million for the fourth quarter of 2012, up 87% year-over-year, and 16% sequentially. Active user counts continue to make up about 35% of the registered user base, and the breakdown between China and overseas are similar to that of registered user counts, and those ratios have been quite consistent for past two years.

Including Feiliu's 13 million average monthly user counts, we now have a total average monthly active user counts of 110 million for the quarter ended December 31, 2012.

Our average monthly paying user counts were 8.9 million for the fourth quarter of 2012, up 57% year-over-year, and 8% sequentially. Overseas paying users now account for about 34% of the total paying users, compared with 29% for the same period last year, and 32% for the previous quarter.

So the conversion ratio from active to paying users was 9.1% for the fourth quarter 2012, compared with 9.7% in the previous quarter, and that mostly due to the decline paying ratio in China from 11.2% to 10.3%. And this is because in the fourth quarter, we have converted, successfully, most of our pay-per-use users to subscription users, so they paying users number growth slowed, but the ARPU increased. Pay-per-use users now account for less than 1% of the total paying users in China.

We also experienced faster active user growth outside of China than paying users, as we have yet to turn a payment option in certain markets, despite an increase in the number of active users. As I discussed in the previous earnings call, we'll continue to experience fluctuations in both directions as we expand globally, and adopt different market strategies. As of December 31, 2012, our subsidiary, NationSky, had over 1,200 enterprise customers.



Now moving on to the financials. Net revenues in the fourth quarter of 2012 were \$30 million, up 134% year-over-year, and 16% sequentially. Excluding enterprise revenue from NationSky, net revenue was \$23 million, up 82% year-over-year, and 10% sequentially. We only had one month of Feiliu's revenue, thus the impact was insignificant. The increases were mainly due to the strong growth in consumer mobile security revenues, and enterprise revenues.

Consumer mobile security revenues increased 69% year-over-year, and 7% sequentially to \$19.6 million in the fourth quarter of 2012. Revenue contribution from overseas users accounted for 54% of consumer mobile security revenues in the fourth quarter of 2012, compared with 50% in same quarter year ago, and 54% in the previous quarter.

In terms of average revenue per user, or ARPU, as measured on a quarterly basis, our branded quarter ARPU were \$2.22 for the fourth quarter of 2012, compared with \$2.05 for the same period a year ago, and \$2.24 for the previous quarter. ARPU for domestic China users were \$1.55 for the fourth quarter of 2012, compared with \$1.46 for the same period a year ago, and \$1.52 for the previous quarter.

So, the increase in China ARPU was because, as discussed earlier, we have converted most of the pay-per-use users in China, who only pay RMB 2 per use to update their virus library to monthly or longer in a subscription users, who pay at least RMB 5 per month. The pay-per-use users now accounted for less than 1% of the total paying users in China in the fourth quarter.

ARPU for overseas users was \$3.51 for the fourth quarter of 2012, compared with \$3.48 for the same period a year ago, and \$3.75 for the previous quarter. Just like the conversion ratios from active to paying for overseas users, overseas ARPU also tends to fluctuate because it depends on the pricing strategy that we set in each country, and the timing when we turn billing switch.

For example, the price in Southeast Asia is actually lower than the Middle East, and the price in Mexico would be lower than the United States. Enterprise mobility revenues increased 49% sequentially to \$6.7 million in the fourth quarter of 2012 due to the strong growth in enterprise business, and new customer gain.

Mobile games and the advertising revenues were \$0.7 million for the month of December in the fourth quarter of 2012, and Feiliu acquisition was closed on November 30, 2012. So, only the December month of its financials was consolidated. As Omar mentioned earlier, while we will report Feiliu's revenue separately in terms of mobile games and advertising revenues, we will not have separate P&L breakdown, given it's being integrated into mobile business, and we'll share the same marketing and operation cost base.

Other revenues in the fourth quarter of 2012 were about \$3 million, up 148% year-over-year, and 3% sequentially. The year-over-year and sequential increases were primarily due to the growth in revenues from secure downloads of anti-virus services for mobile applications produced by third parties. But as the other three revenues, mainly consumer mobile security, enterprise mobility, and mobile games and advertising, continue to grow bigger, we expect other revenues to become less meaningful over time.

Net -- for the fiscal year of 2012 net revenues were \$91.8 million, up 126% from \$40.7 million on 2011. Excluding revenue contribution 2012 of \$12.6 million from the NationSky acquisition in the second quarter, and \$0.7 million from Feiliu in the fourth quarter, net revenues were \$78.6 million, up 93%. the significant increases were mainly due to the strong growth in consumer mobile security revenue.

Consumer mobile security revenues were \$67.9 million in fiscal year 2012, up 88% from \$36.2 million in 2011. Revenue contribution from overseas users accounted for 53% of consumer mobile security revenues in fiscal year 2012, compared with 49% in 2011.

Before moving on to the cost of revenue and operating expenses, I want to refer you to our disclosure on non-GAAP financial measures, which were 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 included across cost of revenues and operating expenses on a GAAP basis, but are excluded to derive our non-GAAP numbers. Most of the SBC expenses were incurred operating expense line items, but we have included a reconciliation table in our earnings release showing the detailed calculation.



Cost of revenues in the fourth quarter of 2012 was \$9.7 million, up 278% year-over-year, and 22% sequentially. The year-over-year increase was primarily due to the impact from NationSky and Feiliu acquisitions, increased customer acquisition costs to drive user growth, higher staff cost from increased headcounts and salaries, and higher revenue sharing with mobile payment service providers consistent with the increase of revenue from them.

The sequential increase was primarily due to the impact from NationSky and Feiliu acquisitions, partially offset by lower customer acquisition cost to meet annual expenditure budgets.

Gross profit in fourth quarter of 2012 were \$20.4 million, up 98% year-over-year, and 14% sequentially. Gross margin was 67.8% in fourth quarter of 2012, compared with 80.1% in same quarter a year ago, and 69.2% in the previous quarter. Excluding the impact from NationSky, gross margin was 79.5% in fourth quarter of 2012, compared with 78.5% in the previous quarter. NationSky's gross margin in fourth quarter was about 26.8%, compared with 24.6% in the previous quarter, and the cost of revenue for NationSky, primarily consist of hardware device procurement cost.

For fiscal year 2012, cost of revenues was \$25.7 million, up 220% from \$8.1 million in 2011. The increase was primarily due to the impact from NationSky and Feiliu acquisitions, increased customer acquisition cost, higher staff cost from salary and headcount increases, and higher revenue sharing with mobile payment service providers.

Gross profit in fiscal year 2012 was \$66 million, up 103% from \$32.6 million in 2011. Gross margin was 72% in fiscal year 2011 -- 2012, compared with 80.2% in 2011. Excluding the impact from NationSky, gross profit for NQ Mobile in 2012 was \$62.9 million, up 93%, and the gross margin was 79.4%.

Now onto the operation expenses. For the fourth quarter of 2012, fourth quarter of 2011, and third quarter of 2012, we recorded total SBC expenses of \$7.5 million, \$7.8 million, and \$3.4 million, respectively across the three operating expense line items. The significant year-over-year increase in SBC in the fourth quarter was primarily due to the SBC impact of newly hired executives, and the employees, and the acquisition of NationSky.

Compared with the third quarter of 2012, the SBC expenses declined slightly in the fourth quarter, and we expect SBC expenses to continue to decline in 2013. 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 in the fourth quarter of 2012 were \$4.2 million, up 74% year-over-year, and down 12% sequentially. The year-over-year increase was primarily due to higher marketing and advertising spending, and higher staff costs from headcount and salary increase, partially offset by lower share-based compensation costs. The sequential decrease was primarily due to a lower marketing and advertising spending, and lower share-based compensation cost.

Non-GAAP selling and marketing expenses were \$15.1 million for fiscal year 2012, up 150% from \$6 million in 2011. The increase was primarily due to increased marketing and advertising spending, higher staff cost from salary and headcount increases, and higher traveling and entertainment expenses.

Non-GAAP general and administrative expenses in the fourth quarter of 2012 were \$5.5 million, up 240% year-over-year, and 37% sequentially. The year-over-year and sequential increases were primarily due to the higher staff cost, higher legal and professional fees, and the cost associated with Feiliu acquisition, while the sequential increase was primarily due to higher legal and professional fees, and higher staff costs.

Non-GAAP general and administrative expenses were \$16.2 million in fiscal year 2012, up 165% from \$6.1 million in 2011. The increase was primarily due to the high staff cost from salary and headcount increase, higher legal and professional fees, higher consulting fees, and higher traveling and entertainment expenses.

Non-GAAP research and development expenses were \$2.8 million in the fourth quarter of 2012, up 92% year-over-year, and 23% sequentially. The year-over-year and sequential increases were primarily due to the higher staff costs from salary and headcount increases. Non-GAAP research and



development expenses were \$8.1 million for fiscal year 2012, up 86% for \$4.4 million in 2011. The increase was primarily due to higher staff cost from salary and headcount increases, and higher traveling and entertainment expenses.

Non-GAAP operating income was \$7.9 million in the fourth quarter of 2012, up 63% year-over-year, and 15% sequentially. Non-GAAP operating margin was 26.2% in the fourth quarter of 2012, compared with 37.5% in the same quarter a year ago, and 26.4% in the previous quarter. Excluding the impact from NationSky, non-GAAP operating margin was 30.7% in the fourth quarter of 2012, compared with 29.8% in the previous quarter. So, we're beginning to see a stabilization in the uptick in operating margin.

Operating margin for NationSky was about 10.3% in the fourth quarter of 2012, quite -- pretty much flat from the 10.3% in the previous quarter.

Non-GAAP operating income for fiscal year 2012 increased 65.4% year-over-year to \$26.8 million from \$16.2 million in 2011. Excluding operating income contribution of \$1.3 million from NationSky, non-GAAP operating income increased 57.4% year-over-year to \$25.5 million.

We continue to report foreign exchange gain and interest income in the fourth quarter of 2012. Together they added \$1.6 million to the bottom line, compared with \$1.5 million in the same period a year ago, and \$0.6 million in the previous quarter. The foreign exchange gain and interest income were mostly due to the appreciation of RMB against US dollars, and higher bank deposit balance resulted from the IPO proceeds and the positive cash flows.

For the full year 2012, foreign exchange and interest income together accounted for \$3.3 million, compared with \$4.3 million in 2011.

The company also recorded a gain of \$2.9 million in other income in fourth quarter of 2012 from staff acquisition of Feiliu's remaining equity stake on November 30, 2012. Subsequently, Feiliu became the wholly-owned subsidiary of NQ Mobile. As a result, the company remeasured the fair value of the previously owned 26.4% equity interest at the acquisition date, and recognized a gain of \$2.9 million, accordingly.

Income tax benefit was \$0.07 million in the fourth quarter of 2012, compared with an income tax expenses of \$0.05 million in the same quarter a year ago, and \$0.3 million in the previous quarter. Income expense was \$0.4 million, and the effective tax rate was 4.3% for fiscal year 2012, compared with income tax expenses of \$0.1 million in 2011. The low effective tax rates were primarily due to the preferential tax treatment enjoyed by certain subsidiaries of the company.

Net income attributable to NQ Mobile was \$4.9 million in the fourth quarter of 2012, compared with \$3.9 million in the same quarter (sic - see press release) a year ago, and \$0.3 million in the previous quarter. Non-GAAP net income attributable to NQ Mobile was \$12.3 million in the fourth quarter of 2012, up 88% year-over-year, and 52% sequentially. Excluding the net income contribution of \$0.4 million from NationSky, the non-GAAP net income for NQ Mobile increased 82% year-over-year, and 50% sequentially to \$11.9 million.

Net income attributable to NQ Mobile for fiscal year 2012 decreased 8% year-over-year to \$9.4 million from \$10.3 million in 2011, mainly due to the significant increase in share-based compensation expenses recorded in fiscal year 2012.

Non-GAAP net income attributable to NQ Mobile for fiscal year 2012, increased 62% year-over-year to \$34 million from \$20.9 million in 2011. Excluding net income contribution fiscal year 2012, up \$1.2 million from NationSky, non-GAAP net income increased 59% year-over-year to \$33.3 million.

On a fully diluted EPS basis our fourth quarter 2012 GAAP earnings per ADS was about \$0.09, and the non-GAAP earnings per ADS was about \$0.23. For full year 2012, GAAP earnings per ADS was about \$0.18, and non-GAAP earnings per ADS was about \$0.66.

So, looking forward we expect net revenue to be in the range of \$32.8 million and \$33.3 million for the first quarter of 2013 (sic - 2013), and to raise the full year 2013 net revenue from the previously issued range of \$150 million to \$155 million to a new range of \$178 million to \$183 million. So all of this the new guidance for the full year 2013 that includes between \$33 million and \$35 million for our enterprise business, and the rest will be our consumer business.

So, this concludes my remarks, and I will now hand it over the call to Operator, and open the line for questions.

QUESTIONS AND ANSWERS

Operator

Ladies and gentlemen, we will now begin the question and answer session. (Operator Instructions). Your first question comes from Mark Murphy of Piper Jaffray. Please ask your question.

Mark Murphy - Piper Jaffray - Analyst

Yes, thank you very much. Congratulations on a solid finish to the year. Omar, I wanted to ask you regarding the America Movil announcement. How long did it take to land the agreement, and how long do you think it's going to take for -- if you're pursuing future partnerships of that kind of scope and scale, how long do you think kind of the sales cycle is on these transactions?

Omar Khan - NQ Mobile Inc. - Co-CEO

Thanks, Mark, for the question, and appreciate your comments. The -- America Movil, here's what I can tell you. I mean from the day I joined in January of 2012, I can tell you it was at the top of my priority list. It's something that we've been working pretty actively for at least the last 13 months.

And so, carrier deals, especially when they're this broad and this integrated in terms of how we've structured this, how we're going to market definitely take multiple quarters to orchestrate, to negotiate, to launch, as well as all of the development work that has to be done, especially if there's branding work to be done.

America Movil, as an example, has all of our three flagship products in the deal, as well as there's rebranding efforts, and multiple channels that need to be supported. It's really -- I'd love to give you a formulaic answer. It's really quite dependent. Carrier deals generally take longer because of their processes, their selection processes as well as the integration work that's generally required. And America Movil is probably fairly typical for a large -- this time line is fairly typical for a large carrier deal that's this broad with this much integration.

As you saw last year, we got Cricket, got in a shorter time frame. So, I would say it ranges anywhere from -- something this broad could range anywhere from a couple of quarters to four to six quarters to take through the entire process. And then the other part of it, I think just to finalize the answer to your question, is also the launch process. It's a fairly broad scope in terms of 18 countries. We're going to start the launch in Mexico, and then move onto other countries within Latin America. We'll start that launch in the next several weeks. And then that launch -- that process will continue throughout the year and beyond.

So, I hope that answers your question, Mark. Feel free to ask a follow up. But you get a sense of how long we've been working on this, how important it was. It was my number one priority since I joined, as we were reviewing business development every single week, if not more frequently.

Mark Murphy - Piper Jaffray - Analyst

So, Omar, on the same topic, are you aware of how much testing in terms of product testing they did, and maybe, who did you compete against to win this business, and I'm also interested in why do you think they ultimately chose NQ Mobile over all the other competitors out there in the world?



Omar Khan - *NQ Mobile Inc. - Co-CEO*

Yes, I mean, I can't specifically talk about which competitors -- they did evaluate us against multiple competitors. I can tell you that. It's folks that you would expect in terms of them evaluating as the large provider they are, and they went to significant feature, functionality testing process, evaluation process in terms of how in the end we were selected.

I would tell you that here's some of the things that really differentiated us during the process. One is the breadth of our products and services. The fact that with one provider, we can launch security services for the consumer, privacy services with the consumer, as well as Family Guardian or Family Protection services were definitely an advantage to us. So, the scope of our product breadth of being able to partner with one provider and address multiple consumer segments and multiple channels at one time definitely is one factor.

The other part of it, frankly, is technology. The performance of our technology, as well as the experience we have globally. Our customer base, being as large as it is to a customer like America Movil, which is extremely large. There is definitely an advantage. And then, another part of it is, they're being a mobile carrier, they valued our experience as a mobile company, and the mobile DNA that we have, and that we bring them in terms of the understanding how the eco-system works, as well as how the technology works on the mobile front. And I think that's extremely important. Those are all factors that I know that during the process came up and were, and how they valued it.

Mark Murphy - *Piper Jaffray - Analyst*

Thank you. And also for Suhai on the same topic of America Movil, how much of a contribution, if any, are you factoring here into the updated revenue guidance for 2013, I guess maybe particularly in the back half of 2013? I'm trying to understand how much of the guidance increase maybe is -- well, I think we have a rough idea how much is Feiliu, how much is just kind of ongoing strength of the rest of the business, and then how much might be relating to America Movil, if you might be able to share that?

Suhai Ji - *NQ Mobile Inc. - CFO*

Yes, Mark, so usually we do not encourage analysts to do the deal based modeling, but we do factor in this deal in our overall revenue contribution. And we usually just start with a conservative assumption, because this deal has yet to be launched, even though it's very imminent, but we will see how it -- the traction comes out, and we will adjust our guidance accordingly, depending on -- I mean, we have multiple deals, right, that we have announced. More than just America Movil, even though it's the most significant one.

But, as the launch starts, as we see the data comes in, we will adjust our forward-looking guidance accordingly. But we will start with a conservative estimate.

Omar Khan - *NQ Mobile Inc. - Co-CEO*

Similar to what we've done in the past, Mark, I think we talked about that some on a previous call. We start with a baseline set of assumptions around take rates, around market size take rates, pricing, et cetera. And then, we've got a range. Obviously, we have factored in the deals that we've announced into the guidance that we've given. But then what we do is we validate the assumptions over time after we launch to a make sure that they're coming in as planned. We jointly validate those cases with the carriers, or the retailers, as we do it.

And so, we do factor in a baseline case in our guidance, but again, we like to see exactly how it performs in the field. So that then we on a quarterly basis, we'll update the guidance based on the internal assumptions, and the actual empirical data.

Mark Murphy - *Piper Jaffray - Analyst*

Okay, great. I wanted to ask you, as well, on the retail stores, where do you think you are in the roll out here? Kind of what inning do you think we're in. And just at a high level for the US market, do you think that this retail store strategy is sufficient to get you to the scale that you want, or do you feel at some point that you would need to secure a partnership with more of a sizable US carrier if that's possible?

Omar Khan - *NQ Mobile Inc. - Co-CEO*

Mark, let me ask Gavin's here with us as well. He, obviously, looks after the commercial end of the business in the international market, and I'm going to ask him to give you an update on the retail businesses, sort of where we stand, as well as the rest of your questions.

Gavin Kim - *NQ Mobile Inc. - Chief Product Officer*

Hi, Mark. So, in the US, to be specific, we have launched with 900 retail stores currently. In fact our current announced relationships gives us access and coverage to about 1,600 some odd retail stores. Again, this is a very good specific number.

We continue to see retail partners consistently reporting in, and at least a 20% attach rate. Obviously, it varies on a month-over-month basis. But on the average, we generally see the 20% attach rate as kind of the golden number.

Currently, we are trying to drive higher. One of the means by which we're doing that is, we have a -- now with a few quarters of experience behind us working with these US retail partners, we've kind of gotten down the size of rolling out retail. We've moved away from kind of what I've called learning into more of an experiential kind of process. And I think we're really quite proud of this fact.

I think before we've told you that moving these big large retail partners to a point where they're actually driving a 20% attach rate has been really a month-over-month learning process for us. And it's taken -- our experience today is roughly three-quarters, one full year of experience level with these guys.

We're now at a place where we can turn on a retail partner and get them to that 20% attach rate in a very, very compressed time frame. And so, it's more a time scale of a few months as opposed to what we were traditionally doing.

Going back to what we're doing to improve that though, the retail partners have now been very vocal with us, and we're learning through this process. We've got a new, it's called the face true, our retail programs that are now coming to bear. We've effectively created a retool of our entire point-of-sale material and training programs. We've updated also, and we will be updating our retail security products to [share with those future] features that have been requested by the channels.

And also, we're launching a new retail software tool that will help, really, at that last two seconds with the customers, where they're actually activating the product with the -- on the customers' devices. It will help to facilitate that entire process.

Our plan is to roll up that new retail, it's called our Phase 2 program in April. So really our target is April 15, and that will go across all our channels, not just the 900, but it will be inclusive of the 1,600 that we haven't yet exposed -- haven't been exposed to.

Just to talk to your specific question about, do we see it being a scalable business for us. We are a fairly aggressive business development. We have a very aggressive business development pipeline. I think you'll see that we're closing, and we're bringing new deals to the table that are effective here. Large, we are specifically focusing on those retail partners that have store coverage in the orders of 100 or more. And for us that is a scalable model.

And to talk about it, the retail channel for the US market as a whole is, in terms of total distribution for smartphones, as we discussed before, is north of 40% with total smartphone in distribution. And so, our view of it is as we continue down this path, it's obviously going to grow and drive



additional revenue to our business as we continue to announce relationships. Clearly, we haven't stopped our business development pipeline as a whole, and the efforts for us to actually work with large carriers, but we have the experiences with America Movil, as an example, it takes a while.

Mark Murphy - *Piper Jaffray - Analyst*

Great. Thank you, Gavin, and thanks everyone for taking my questions.

Operator

Your next question comes from Mike Walkley of Canaccord Genuity.

Mike Walkley - *Canaccord Genuity - Analyst*

Okay, thank you. Omar, it was great to see you at Mobile World Congress. Just on NationSky with the MDM, can you share with us how you see that maybe coming outside of China into enterprises outside of China, and how you see that business for enterprise expanding long term?

Omar Khan - *NQ Mobile Inc. - Co-CEO*

Given our enterprise business specifically around mobile device management is going to be focused in China for the near term. We're focusing on hardening it, developing it, for the China business. The mobile security framework, however, is something that we are bringing outside of China through our partnerships with Bachs and GEMA.

So I won't preclude the fact that MDM for us can have a market outside of China, but for now we are focused 100% on making sure that we launch it, harden it, and scale it within the China market, and then focus on bringing -- focus right now on bringing our mobile security framework to enterprises outside of China through partnerships like Bach as an example. So that's really the current plan that we'll talk about.

Mike Walkley - *Canaccord Genuity - Analyst*

Okay, thanks. And just going back to the question Mark asked on the America Movil win, I know you don't have to model by customer, but can you just kind of walk us through the go-to market strategy? Are they going to launch all three of your services at once, or is it kind of one launch per country, and how much is that requiring on your end? Do you have to have a lot of people in market to help these launches?

Gavin Kim - *NQ Mobile Inc. - Chief Product Officer*

Yes, hi. This is Gavin again. I can give a brief review of what we're doing. So, America Movil is launching actually a total of all of our products in various packages. The configuration that we're using is, you can think of it as a base set of services that will be offered, really, as a set of premium services. They will all largely go out with a 30-day free trial, after which the consumer will have the opportunity to opt-in or continue their premium subscription.

They are going to be including this as a part of full visual marketing campaign, customer service outreach, SMS marketing, as well as, in the future as we roll out, will include and be inclusive of additional opportunities like preload, et cetera. Now this is also going to apply to all, again, to all products, so Security Vault and Family Guardian.

Omar Khan - *NQ Mobile Inc. - Co-CEO*

To answer the last part of your question, it will be a phased roll out where we're going to target the largest countries first. Obviously, Mexico and Brazil make up an overwhelming majority of the Latin America market, and that's where the primary focus will be, Mike. So you'll see a tremendous scale coming just from those first two launches actually.

Mike Walkley - *Canaccord Genuity - Analyst*

Okay, yes, it makes a lot of sense. It's helpful. Thanks. Suhai, just a question for you on the -- on Feiliu, can you just remind us what the gross margin is for that business, as we expect it to be in for full quarter? And also just for your first quarter, with the full first quarter of Feiliu, should we expect overall operating expenses to go up sequentially?

Suhai Ji - *NQ Mobile Inc. - CFO*

Yes, I think as we discussed on the call, I think Feiliu is being fully integrated into NQ and it will be part of our consumer business. So we will disclose the top line revenue generated from the mobile game and advertising business. But on the cost basis, we do not break them out. But as we discussed before at the time when we announced the acquisition, within Feiliu, the margin profile will be similar to NQ. So it's not as drastically different from our enterprise business such as NationSky.

Mike Walkley - *Canaccord Genuity - Analyst*

I guess on the OpEx, how many people came on. I know they're only there for a month, so we'll have the employee base for three months, just trying to help think about like R&D, and those type of line items sequentially.

Suhai Ji - *NQ Mobile Inc. - CFO*

Yes, it's about 120 people that came on board from the acquisition. Yes.

Mike Walkley - *Canaccord Genuity - Analyst*

And then just the strong 2013 raised guidance, is there any breakdown from including Feiliu versus the core business, or do you have any outlook for Feiliu? I think you said at your Analyst Day some numbers. Just trying to back into the change in the guidance.

Suhai Ji - *NQ Mobile Inc. - CFO*

Yes, I think I said earlier on the call, I think between consumer and enterprise, we would have like 33 to 35 range for the enterprise business. And for the consumer, between the consumer security -- consumer mobile security, and mobile game and advertising, it will be roughly 120 to 121 for the core NQ business, and 25 to 28 for the mobile game and advertising.

Mike Walkley - *Canaccord Genuity - Analyst*

Okay, great. Thank you. I think that's it for me for now. Oh, just one question overall, strong results for the quarter and the year, made some acquisitions. How should we think about the portfolio where it stands today? Do you guys, with a lot of cash in your balance sheet, do you think you still need to make more acquisitions to grow the platform, or is it more focused on executing on the platforms you have in place over the next course of 2013?

Omar Khan - *NQ Mobile Inc. - Co-CEO*

So, Mike, we're pretty much focused on integration right now. I mean, we've brought in quite a bit of capability both from a technology and from a go-to market perspective, and our focus right now is to drive integration and scaling of those businesses, as well as the synergies between the businesses, and that's really where our focus is.

We'll continue to look for opportunities and be opportunistic for really small tuck-in type stuff, but nothing on the order of magnitude of what we've done last year. Really, we're heads down and focused on integration and value creation based on the businesses we've already acquired.

Mike Walkley - *Canaccord Genuity - Analyst*

Right. Good luck in 2013. Thanks for taking my questions.

Operator

Your next question comes Andy Yeung of Oppenheimer. Please ask your question.

Andy Yeung - *Oppenheimer & Co. - Analyst*

Hi. Thank you for taking my questions. My first question is actually about your M&A strategy. Last year you have made a number of acquisitions and investments, including NationSky, Feiliu and Hesine. So, can you give us some color in terms of your investment and M&A strategy for 2013? What are the areas that you're looking at if you're doing investments?

Omar Khan - *NQ Mobile Inc. - Co-CEO*

Yea, I think, Andy, we just addressed part of that as well. For 2012, we feel very confident and comfortable with the acquisitions that we made. We feel like we're in a very good place. Our focus for 2013 is really about integration and scaling.

So the businesses that we've acquired, we're focused on value creation to integration of those businesses, and driving synergies between them. That applies to the three that you said. For 2013, that's really our core strategy. We're not looking to continue on that type of trajectory in terms of acquisitions.

We have a strong balance sheet, as you indicated. We're going to be opportunistic to look for small technology or enhancement type investments. But really small from a scale perspective. We're really from a large business perspective or large acquisition perspective, very much focused on integration of what we've already brought into the portfolio. We're very comfortable with what they bring to us today.

Andy Yeung - *Oppenheimer & Co. - Analyst*

Okay, got it there. And then next question is about customer acquisition channels. Obviously you have expanded internationally and you have also, we recently signed up several number of carrier deals. Can you help us understand a little bit about the mix of channel that you use to acquire new customers in terms of OEM preload, app store download, direct download, retail network carrier? Just help us understand what's the distribution of customization channel.



Suhai Ji - *NQ Mobile Inc. - CFO*

Yes, Andy, I would take this question. I think we only discussed three primary channels, some of those will be launching to the offline, for example, the preload, and even the retail network, that will be the offline channel. And also online channel includes the viral marketing, and that's still people come to our mobile website to download software directly. Also, other digital market. So, going forward, I think our view is roughly like one-third each in terms of the contribution to the new users.

Andy Yeung - *Oppenheimer & Co. - Analyst*

Okay, got it. Got it. And then one final question, which is a housekeeping question regarding G&A expenses. There was a little jump in G&A expenses during the quarter. It seems to be that some one-time items related to Feiliu acquisition. Can you help us understand how much that is one-time and how much that increases ongoing?

Suhai Ji - *NQ Mobile Inc. - CFO*

Well, are you looking at the GAAP basis or the non-GAAP basis? Because --

Andy Yeung - *Oppenheimer & Co. - Analyst*

Non-GAAP basis, yes.

Suhai Ji - *NQ Mobile Inc. - CFO*

Yes. And we think we have already built in the senior executive team, even from the Feiliu acquisition. So we think there is a leverage, especially on the non-GAAP basis from G&A, and that's -- and also on a non-GAAP, we did not factor out the expenses related to the acquisition of Feiliu, such as the professional fees, the legal fees that we pay. So that will be included in the fourth quarter as well, and that's why there is a higher G&A expenses in the fourth quarter.

So, going forward, we are actually discussing with our auditor to break out those kind of one-time expenses, and to lump all those together into the non-GAAP measure, other than the SBC expenses as we get larger and larger in size.

Andy Yeung - *Oppenheimer & Co. - Analyst*

Okay. Okay, great. All right, thank you so much.

Operator

Your last question comes from Fred Ziegel of Topeka Capital Markets. Please ask your question.

Fred Ziegel - *Topeka Capital Markets - Analyst*

Hi guys. Back to America Movil for a second, there's been some discussion about driving smartphones below \$100 around the Mozilla operating system, which apparently some people are planning on beginning to offer in Latin America in the second half of the year. My question is, is that OS on your radar screen?

Gavin Kim - NQ Mobile Inc. - Chief Product Officer

So, hi. We -- so while we can't necessarily comment on American Movil's overall device strategy or their launch plans, we can say that certainly our services can be applied to any of their product device programs. We've been working closely with American Movil, obviously for -- through the plan up and the bring up of this launch, and we have a very specific prioritized set of funded operating systems and funded devices that we're rolling out with them, and we'll continue to track their operating system priorities as we move through Latin America and Mexico.

Fred Ziegel - Topeka Capital Markets - Analyst

I think their biggest mobile operator competitor, which is Telefonica, is also a partner. What's the relationship with Telefonica?

Gavin Kim - NQ Mobile Inc. - Chief Product Officer

The announcement we made with Telefonica, and the work that we're doing with them today is largely -- so it's two aspects. One is it's a -- we're working with them on their storefront product as a -- they are an application distributor for us. In addition, we are also working with them, and their specific building platform that they call BlueVia, and so we've done the integration work with them.

We see Telefonica's storefront product is really an open market -- think of it as an open market distribution platform for us to reach their customers through them. But I think you can think of it as really no different to us in the way we -- in terms of our strategy, say, like Google Play. The difference with American Movil is they are actually more of a strategic value-add provider. It's their brand, their product and they're distributing this on our behalf.

Fred Ziegel - Topeka Capital Markets - Analyst

A question for Suhai, ex-NationSky, I think you said gross margins were up about 100 basis points quarter-over-quarter. My question is really more on the operating line. Do we ultimately get back to the early days of mid to high 30s ex-NationSky, or where do you think that sorts out in the next two to four quarters?

Suhai Ji - NQ Mobile Inc. - CFO

Yes. If you look at the past couple of quarters, I mean at least we are stabilizing the margin. I mean we're beginning to see the leveling off of the operating expenses as a percentage. And that's also because we have largely set off -- I wouldn't say completed the investment phase, but we have laid out the infrastructure in place to grow our international business, and we want to be conservative. We think 30% is for the bottom line.

And as our overseas revenue, international revenue tick up, we will realize the scalability in that, and we will improve our margins. So we will, I think in the next couple of quarters, it will begin to tick up. But hopefully we give a more detailed guidance as we see the traction from the international revenue.

Fred Ziegel - Topeka Capital Markets - Analyst

30% is kind of the baseline, and then we'll see what leverage you get from there. Is that a fair way to think about?

Suhai Ji - NQ Mobile Inc. - CFO

Yes.



Fred Ziegel - *Topeka Capital Markets - Analyst*

Okay. Okay, thanks.

Operator

There are no further questions. I will now return the call to Michelle Ma, NQ Mobile Director of Investor Relations for closing remarks.

Michele Ma - *NQ Mobile Inc. - Director - IR*

Thank you, operator. If there's no further question at present, we'd like to conclude by thanking everyone for joining us on the call. We welcome you to reach out to us directly by emailing to investors@nq.com, if you have any questions or requests for additional information, and encourage you to visit our Investor Relations website at ir.nq.com. This concludes NQ Mobile's earnings call.

Operator

Ladies and gentlemen, that does conclude our conference for today. Thank you for participating. You may all now disconnect.

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