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Snap Interactive, Inc.

2016 Annual Results Earnings Conference Call

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CORPORATE PARTICIPANTS

Michael Pritchard, *Investor Relations, Haynes and Boone*

Alex Harrington, *Chief Executive Officer*

Judy Krandel, *Chief Financial Officer*

PRESENTATION

Operator:

Good day, and welcome to the Snap Interactive Incorporated 2016 Annual Results Conference Call. Today's conference is being recorded.

At this time, I'd like to turn the conference over to Mr. Michael Pritchard, Company Counsel from Haynes and Boone. Please go ahead, sir.

Michael Pritchard

Thank you. Good afternoon, and welcome to the Snap Interactive Fourth Quarter and Full Year 2016 Earnings and Business Update call. Again, my name is Michael Pritchard, and I am with Haynes and Boone, Outside Counsel to Snap. Hosting the call today are Alex Harrington, Chief Executive Officer and Judy Krandel, Chief Financial Officer.

Before I turn the call over to Management, I would like to remind everyone that earlier today we issued a presentation to accompany this call. The presentation can be accessed on the Company's website, snap-interactive.com, under the Quarterly Earnings tab of the Investor Relations section or by following the link on Snap's homepage.

I'd like to inform everyone in attendance that certain statements made during today's conference call that are not statements of historical fact, including those concerning future plans, objectives, goals, strategies or performance, and those related to the Company's operations following the completion of its merger with AVM Software Inc., also known by its doing business as named Paltalk, are forward-looking statements. These statements reflect the good faith beliefs and judgments of the Company and are based upon currently available information only as of the date of this conference call.

These statements are subject to risks, uncertainties and other factors that could cause actual results to differ materially from current expectations. These factors include those described in the Risks Factors section of the Company's periodic reports that are filed with the Securities and Exchange Commission. Forward-looking statements are not guarantees of future performance and the Company expressly disclaims any obligation to update earlier statements as a result of new information, except as required by law.

Certain non-GAAP measures may be discussed during today's presentation, including Adjusted EBITDA and certain other metrics, excluding non-recurring expenses related to the Company's merger with AVM. These metrics have been calculated consistent with the manner in which they are defined in Snap's periodic reports filed with the Securities and Exchange Commission and have each been reconciled to the nearest applicable GAAP measure in this presentation and in Snap's earnings release, which is also available under the Press Releases tab of the Investor Relations section of Snap's website, snap-interactive.com.

With that, I'll turn the call over to Alex Harrington, Snap's Chief Executive Officer. Alex, the call is yours.

Alex Harrington:

Thank you, Michael, and thank you, all, for joining us on today's call. I encourage all of you to access the Q4 2016 earnings call presentation, available on www.snap-interactive.com. It's on, in addition to the place where Michael mentioned, it's also on the home page, if you scroll down on the left-hand side.

For those of you with the deck in front of you, please advance to Slide 5 for our strategic overview. Two thousand and sixteen was a transformative year for Snap and we entered 2017 poised to leverage our established presence, proven technology and growing customer base in the live video space, which is one of hottest growth segment of the consumer internet.

As most you know, we completed the merger with Paltalk in October, which added strategically valuable video assets and technology to our Company and significantly increased our business scale and Management depth. As we progress through this presentation, there will be some recurring themes that I want to highlight for you now.

First off, we believe live video technology is creating an explosive growth opportunity as new consumer behaviors are disrupting the present social networking and messaging spaces and new businesses will emerge, powered by live video.

Secondly, largely as the result of the recent merger, we believe we have the key component to capitalize on this trend; a proprietary live video technology platform, a global footprint and significant user scale. We think these valuable assets give us competitive advantage to build solutions that are responsive to rapid evolution in the market, but we can also build scale by M&A as we are an experienced acquirer that can become a consolidator in a fragmented industry. More on all of these points later.

As a result of the merger, we diversified our product array from two products at pre-merger Snap to now nine products across video social networking as well as interactive dating. In addition, the broadened product array now has strength not only in English speaking markets around the world, but also the Middle East and Southeast Asia.

So, today our product portfolio includes video social networking, as you'll see on Slide 6, business units, Paltalk, Camfrog and Tinychat, which together host one of the world's largest collection of live video community. These products all help users connect with friends and meet new people via video chat affinity group, with each product serving different geographies and demographics. For example, Paltalk is stronger among in older audience and in the US and Middle East, while Camfrog addresses a more youthful audience with strength in Southeast Asia.

Moving on to Slide 7, the Company also operates three interactive dating products with FirstMet as the most established general-audience dating product, primarily serving users 35 and older. In addition, we have The Grade, a female-friendly swiping app, targeting millennials, and we recently beta-launched 50 More, our newest dating app, targeting the fast-growing 50-plus demographic.

Turning to Slide 8, another important thing to know about Snap is that we have a substantial, commercial and technology platform that we believe will enable us to capitalize on the emerging growth trends in video. Systemically, our battle-tested proprietary live video technology platform supports millions of users viewing and publishing live video streams.

Delivering seamless live video and audio is exceptionally hard and we have four locus' of tech talent supporting the Company, including highly skilled low-cost teams in Russia and India. As of March of this year, we have approximately 183,000 active subscribers and usage in more than 180 countries.

The merger also enhanced our Management team, bringing on Jason Katz, an accomplished entrepreneur and pioneer in video social networking products as our Chairman, President and Chief Operating Officer. We believe this deep Management bench and established commercial base give us a running start in launching new products and optimizing the products we have with the exciting opportunities that lie ahead.

Turning to Slide 9, our mission over the next three years is to build the Company's presence as a leader in social products delivering live video experiences in a mobile world. As we've just discussed, we believe we have the means to execute on this and will share in the coming slides why we think that's such an exciting opportunity.

Moving on to Slide 10, as mentioned this thing, this live video technology, that our Company has spent the last 16 years investing in and protecting—sorry, perfecting—happens to be the technology of the moment and we believe that live video represents an outsized growth opportunity, but don't take my word for it.

Last month, Mark Zuckerberg of Facebook repeated his assertion that, "video is a megatrend on the same order as mobile" and sure enough, Facebook is jumping on the live video bandwagon. Just in December 2016, launched what they described as the most requested Facebook messenger feature ever and what was that feature? Group video chat.

Then, there's a 2016 report by Cisco which projected that by 2019 online video will be responsible for 80% of global Internet traffic. That's a monumental share, and pre-revenue live video startups right now are getting rapid adoption and jaw-dropping amount of funding from VCs because private investors are seeing an explosive growth opportunity in live video and, for those businesses that sees the opportunity, there is a potential for new unicorn-type success stories.

The last point on Page 10 highlights a new model that has recently emerged in Asia and is growing incredibly fast. It's called Live Streaming and, moving to Page 11, we get into more detail about it. Live Streaming is a model where users themselves become video broadcasters from their mobile phones and establish a pure audience of fans. These newly-minted live-streaming stars then receive virtual gifts as appreciation from their fans, the proceeds of which are shared between the Company and the broadcaster. This has become a $5 billion industry in China out of nothing in just a few years and is growing fast in other markets.

Two key points about live streaming that make it very exciting and very applicable to Snap: one point is that live streaming has emerged at the intersection of interactive dating and live video. It is dating companies such as China's MOMO and Singapore's Paktor who are taking leading positions in the markets, and MeetMe in the US has also announced they are entering the market this year. That this market is so accessible to dating companies and plays to our strength in live video is very promising to us. The next point which bears repeating is that the growth figures in the live streaming market are eye popping.

MOMO's reported Q4 2016 revenue grew year-over-year 524% to $246 million and whereas live streaming in 2015 in the fourth quarter represented 2.5% of revenue, it now represents 79% of revenue. So, this is not an isolated case. Live streaming is blowing up across the Board.

With all of this market backdrop in mind, turning to Slide 12, we discuss Snap's strategy to address the live video market opportunities. As previously stated, we believe live video technology will potentially remake the business landscape for all apps with text or voice messaging capability, everything from social networking to customer service to distance learning to professional collaboration tools, there will be new winners in all of these fields who capitalize now on the new technology.

That means it's a wide-open playing field, which gives a huge scope of business opportunity to anyone who is a live video expert. However, we believe that focus is necessary to succeed and our execution strategy will be focused on the high-growth market segments where we have demonstrated strength.

Our three-pronged efforts will concentrate on: one, live video social networking; two, live video social discovery; and three, live video—live streaming entertainment. The first of these, live video social networking, we outline on Slide 13. Snap currently operates three social networks with video at its core, Paltalk, Camfrog and Tinychat. The market is quickly evolving and users grow more excited about mobile video as part of their everyday life. It’s clear that there is a significant opportunity for a more mobile-centric live video app. We see it in the growth of Facebook Live, which reported 400% growth usage between May and October of 2016 and when we look at the live group video app, Houseparty, which inside it’s first year hit 2 million monthly active users and raised $50 million capital before having any apparent revenue model. We can see that there's a lot of growth in the market.

All of these companies and their investors are betting that group mobile video chat may become a new standard of communication among the youth generation and we're making that bet, too. At Snap, we've been developing a new mobile-first live group video chat product that we expect to launch later this year.

Turning to Slide 14, and Snap's strategy for live video social discovery. First off, social discovery describes the segment of companies that provide social applications for meeting new people of which interactive dating is a prominent segment. We are working to merge the best practices of live video and interactive dating. We believe that video will become pervasive in social discovery apps, even though today it hardly exists. We want to be an innovator here. Using a three-phase approach, first we are integrating dating features into our live video chat app. Then, we will introduce video capability into our main stream dating app, and finally, in the medium to longer term, we are planning on launching a new video-centric dating and social discovery app.

Turning to Slide 15, and the third segment of our live video growth strategy, we are going after the live streaming market. We are going to be leveraging the live video products we already have. We currently operate three video apps that are well-positioned to do this. Ribbit Live, a video streaming app with a concentration of users in Southeast Asia, Tinychat, a social video app with a large audience of millennials in the US and Firetalk, a recently launched video streaming app designed for content creators to cultivate and monetize their audience. With this market blowing up and new competitors emerging all the time, there is no time for delay. We are in development on expanding our services into this market presently with launches later this year.

Now that we've covered our strategy to address the emerging live video market opportunities, we'll take a quick sidebar on Slide 16 to address our intellectual property portfolio. AVM has historically made large investments into proprietary technology for video and voice communication. We've developed a portfolio of 25 patents, principally related to video conferencing and video game technology. These patents, in addition to supporting our products, have also been a source of licensing income and the Company has generated tens of millions of dollars based on the strength of these patents. We expect to generate licensing income in the future as well.

In December of 2016, we initiated legal action against Riot Games, Inc., and Valve Corporation, with respect to their online game, League of Legends and Defense of the Ancients 2. It is important to point out that this is not a significant diversion of Management time or Company capital. However, if we prevail, the licensing proceeds will provide valuable capital to fuel our previously mentioned growth strategy.

Now that we've discussed organic growth opportunities, turning to Slide 17, we now touch on the growth potential presented by M&A. Across the industry, we see a fragmented landscape with a long tail of smaller players with less than $20 million of revenue that in many cases are too small to attract M&A interest from the largest players who are the typical acquirers.

We believe with our track record and experience of growing through acquisition that we can be a consolidator for smaller but attractive companies of this sort in the video and social discovery space. We also believe our public vehicle and public currency makes us an attractive merger candidate, providing the opportunity for liquidity for target shareholders.

We continue to approach M&A with discipline considering targets that meet or exceed a set of stringent criteria including financial consideration such as scale of revenue and EBITDA margins for a Company that deepens our technology portfolio or our leadership.

With that, I would now like to turn the call over to Judy Krandel, our CFO, for a detailed review of our financial results. Judy?

Judy Krandel:

Thank you, Alex, and thanks to everyone today for joining us on the call. Before I begin, I would like to remind everyone that on October 7, 2016, we completed our previously announced merger with AVM Software. The merger has been accounted for as a reverse merger under the acquisition method of accounting for business combinations with AVM being treated as the accounting acquirer of Snap.

Accordingly, the financial results I will discuss reflect the operations of AVM for the period of January 1 through October 7, 2016, and the operation of the post-merger Company for the period of October 8 through December 31, 2016. These results for the fiscal year ended 2016 are compared to the financial results for pre-merger AVM for fiscal year 2015.

Turning to Slide 19, I would like to touch upon our financial highlights. We are excited to report that we have resumed revenue growth at Snap in 2016. Not only is our topline growing, but we had approximately $1 million of Adjusted EBITDA after adding back one-time merger-related expenses.

We have a solid debt-free balance sheet with cash bank balances increasing in the first quarter of 2017. We undertook critical steps towards the goal of a listing on a national securities exchange which I will discuss a little later, and finally, of course, we are continuing focusing on merger integration and cost reduction.

Turning to Slide 20, I would like to begin reviewing Snap's financial performance in the fourth quarter and the full year 2016. Total revenues for the fourth quarter of 2016 were $7 million, up 51.5% from the same period last year. The increase in revenues from the prior year were predominantly due to pre-merger Snap, which contributed as of the merger date of October 7, 2016.

AVM revenues in the fourth quarter were up slightly from the prior year. Revenues for the quarter were comprised of $6.2 million from subscriptions and $843,000 from advertising. Revenues for the full year 2016 were $20.9 million compared to $20.1 million in 2015, an increase of 4.3%.

Subscription revenue for the year increased 6.4% to $18.6 million and advertising revenue for the year declined 9.7% to $2.3 million. Like this quarter, the increase in subscription revenue was due to the contribution of pre-merger Snap, which was offset by a decline in AVMs subscription revenue of approximately $1.1 million, predominantly in the first half of the year.

We believe that the decrease in AVM's subscription revenue was driven in part by product's outages and inconsistency in service in our primary datacenter. We made the strategic decision to close a major AVM datacenter and transition to cloud hosting services. This move was completed in February 2017 and our service disruptions have decreased as a result. To a small degree, we also believe revenue was affected by increased industry competition. That being said, we continue to innovate and believe the opportunity to create new and differentiated live video consumer products is enormous. In fact, it was that foresight that drove us to seek a merger partner as established in live video as AVM. It will take time for these initiatives to manifest itself in the core business, but we are excited for our future. The decline in advertising revenue for the year was driven primarily from the loss of one advertising partner at AVM and the elimination of a third-party toolbar distribution partner. We have begun working with a new advertising partner and continue to focus on advertising and expect to build upon our business going forward.

As shown on Slide 21, Adjusted EBITDA was approximately $12,000 in 2016 versus approximately $671,000 in 2015. Excluding one-time merger related expenses in 2016, Adjusted EBITDA was approximately $1.1 million or about 5.2% of revenue versus 3.3% in 2015.

The Company was able to leverage overall cost, primarily driven by product development productivity and our move to cloud hosting services. This server move also drove reduced headcount in the information technology support areas. This move was completed in February of this year and we do expect to see some continued cost improvement as a result of this outsourcing in 2017 versus 2015.

As you can see on Slide 22, cash flow from operations declined to a loss of approximately $407,000 for the year ended 2016 from approximately a positive $96,000 in 2015. Excluding non-recurring merger-related expenses, net cash from operations increased to $698,000, which was an improvement of $602,000 over the prior year.

Turning to Slide 23, as of December 31, 2016, we had $4.2 million in cash and cash equivalents and zero debt. Cash decreased from December 31, 2015, primarily from the repayment of all of pre-merger Snap's debt, including a $3 million convertible note as well as one-time merger expenses of $1.1 million.

Management expects improved cash results this year and, in fact, bank balances have increased since year-end 2016. As of March 17, 2017, bank balances were approximately $4.7 million, up approximately $600,000 from December 31, 2016 and we expect positive cash flow to continue.

As noted on Slide 24, Snap is seeking a listing on the National Securities Exchange and the benefits that come with that listing. We want to continue building the credibility that we have strived for in maintaining very high financial standards. We hope to improve our trading liquidity and improve the ease of capital raising if and when that becomes a priority. To this extent, we completed a 1-for-35 reverse stock split and in my position as the Chief Financial Officer, expanded the Board of Directors to seven including four independent Board members and formed both an Audit and Compensation Committee.

As noted on Slide 25, we continue to expect further benefits from the merger integration in 2017. We are focused on revenue enhancements from cross-selling opportunities and best practice sharing. There are further cost reductions to be realized as we reduce rent by consolidating a real estate location, eliminate any remaining duplicate costs from the outsourcing of our data center and continue consolidating vendor relationships.

We are truly excited about our deeper Management bench in a unified organization structure and, of course, the broad experience and enhanced corporate governance from our expanded Board of Directors. In summary, Snap is in one of the strongest financial conditions it has been in for many years with a solid cash position with positive cash flow from operations in 2016 before one-time merger expenses. Although we plan to invest in additional people and resources to grow our business, we will continue to focus on self-sustainability, profitability and cash flow, and now I would like to return the call back to Alex.

Alex Harrington:

Thanks, Judy. In closing, and before we open the call for questions, I would just like to reinforce our excitement for the upcoming year 2017. The merger has been transformative for the Company, not only in terms of improving our financial position and scale, but also enhancing the strategic growth opportunities available to the Company.

Live video is an exciting growth market and we believe our existing products and the underlying technology give us a leg up in pursuing the opportunities I've outlined in this presentation. Whether through organic growth or one or more strategic acquisitions, we believe the Company is well-positioned for success in 2017 and beyond.

With that, I'd like to open the call up for questions.

Operator:

Thank you. If you would like to ask a question, please signal by pressing star, one on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, please press star, one to ask a question at this time. We will pause for just a moment to allow everyone an opportunity to signal for questions.

There appears to be no questions at this time. Mr. Pritchard—actually, correction, Mr. Harrington, I'll turn the conference back over to you, I apologize.

Alex Harrington:

No problem. Thanks, everyone, for listening today. We look forward to speaking again later this year with each quarterly update. If you have any further questions, don't hesitate to email our Investor Relations at ir@snap-interactive.com. Thanks, again.

Operator:

That does conclude today's presentation. Ladies and gentlemen, thank you for your participation. You may now disconnect.