



PeerStream, Inc.

Second Quarter 2019 Earnings Conference Call

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CORPORATE PARTICIPANTS

Stephanie Prince, *PCG Advisory*

Alex Harrington, *Chief Executive Officer & Principal Financial Officer*

PRESENTATION

Operator:

Good day everyone, and welcome to the PeerStream Inc. 2019 Earnings and Business Update Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Stephanie Prince of PCG Advisory. Please, go ahead, ma'am.

Stephanie Prince:

Thank you, Augusta, and good afternoon, everyone. Welcome to the PeerStream Second Quarter 2019 Earnings and Business Update Call. With me on the call today is Alex Harrington, Chief Executive Officer and Principal Financial Officer of PeerStream.

I'd like to remind everyone that earlier today, we issued a presentation to accompany this call. The presentation can be accessed in the Company's website at peerstream.com, under the Quarterly Earnings tab of the News section, or by following the link on PeerStream's homepage. Before I turn the call over to Management, I'd like to inform everyone 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, are forward-looking statements. These statements reflect the good faith, belief, and judgment of PeerStream's Management 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 Risk Factor section of the Company's periodic reports filed with the Securities and Exchange Commission. Forward-looking statements are not guaranteed for future performance, and the Company expressly disclaims any obligation to update earlier statements as a result of new information, except where required by law. Certain non-GAAP measures may be discussed during today's presentation including Adjusted EBITDA. Adjusted EBITDA has been calculated consistent with the manner in which it is defined, and PeerStream's periodic reports filed with the SEC. Adjusted EBITDA has been reconciled to the nearest applicable GAAP measure in this presentation and in PeerStream's earnings release which is also available under the Quarterly Earnings tab in the News section of PeerStream's website, which once again is peerstream.com.

I'd now like to turn the call over to Alex Harrington. Alex?

Alex Harrington:

Thanks, Stephanie. Thank you all for joining us today. As Stephanie said, I encourage you all to access the Earnings Call presentation available on our website, www.peerstream.com. For those of you following along in the presentation, we're going to be leaping to Page 3 to first review some strategic updates.

In addition to a review of Q2 financial performance on this call today, we're going to give a qualitative update on both the secure communications software licensing business, which was introduced to market last year, and our consumer video chat apps business which was the foundation of our business started now more than 20 years ago, and it serves nearly half a billion end users over that time. The secure communications business which grew out of work we did in 2018 and through the first half of this year for our foundational client, ProximaX, now is targeting government and enterprises in the \$45 billion software segment of the information security industry, that estimate coming from Gardner.

This is a really big market opportunity with constantly evolving technology and near constant pressure from hackers and regulators, and the timing to approach this market is excellent. On Page 4, we're going into greater depth on our offering. The solution PeerStream is developing, is really two complimentary product, which together offer solutions for maximum security in voice, video, text and data communication. These products are not designed for mainstream consumer use, but for the most sensitive communication situation; military, intelligence, emergency response, or highly confidential corporate communications.

The first part of the solution is PeerStream Protocol, or PSP for short. This is a data routing technology that not only protects the content of a client's communication but also the metadata around the transmission. Which means, importantly, that the identity of the sender and the recipient is protected as well as the content. This is an important innovation omitted from many security systems that only protect the content.

The second product is Backchannel, which is the front-end complement to PSP. Backchannel is the app or set of integration tools that allow end users to view and send communications in a hyper-secure way. We're integrating hardware level encryption features that protect your messaging even if your phone operating system gets hacked.

Advancing to Page 5, we have an update on our progress today. In this last quarter, we've been focused on building partnerships, establishing a significant sales pipeline and evolving the software to meet market demand. Our partnership, (inaudible) Telefonica and Rivet, announced earlier this year, are focused on expanding our capabilities such as access to the hardware security features that I mentioned, and tapping into client relationships. For example, working with existing government contractors can radically shorten the timeline to get government business.

Arguably, the top priority recently has been up to sign up new clients. In the last four months since we've narrowed our focus to singularly concentrate on secure communications for government and enterprise, we have found customers to be very receptive and we built our pipeline to more than 40 active customer dialogues. Among these are government contract opportunities with military and other departments that could result in significant multi-year deal.

Now, these are new products and we're new to government enterprise sales so we cannot pinpoint the timeline to close any particular deal. But we would be ready to serve customers as soon as the fourth quarter of 2019.

Also, super important right now is the software development work we're doing to adapt our product to the customer's feedback we're getting over the course of the last quarter. We originally built the software for a narrow set of use-cases for one customer at ProximaX, and now we're broadening the capabilities to be responsive to the market and make the software more ready to license.

On Page 6, we segue to the video chat side of the business. We continue to see opportunities to reinvigorate our video chat product particularly Paltalk and Camfrog which are the largest contributors to revenue. Though these products are mature, they're remarkably resilient due to recurring revenue streams and loyal customer basis. In Q2 2019, we have been investing in an array of projects to improve the quality of video delivery, the attractiveness and usability of the product and a host of optimizations and feature additions designed to improve retention and monetization. One such enhancement is outlined on Page 7.

We recently announced that we are launch partners with YouNow in Props; a crypto project designed as a reward currency for loyal end users of an independent network of apps. Paltalk and Camfrog will be joining that independent network as among the first apps to integrate the Props token-based user reward system. We intend to create incentives for users to perform beneficial community building activities, with the potential to improve our user retention and monetization. Apart from the integration costs, the reward currency cost PeerStream nothing and we reap the full benefit of the potential user loyalty improvement.

So it feels like a great opportunity, and even further, PeerStream also earns Props for its participation. So we get directly a potentially valuable cryptocurrency stake. One major difference about Props from the other crypto projects, is that the SEC has qualified YouNow's RegA+ offering of Props tokens. This is the first consumer token offering to attain this qualification. We view this as a huge development in the crypto industry, and it reinforces the sustainability and legitimacy of the project. So we're very excited to be a part of it.

With that, we'll segue to the financial starting on Page 8. First, just a reminder about our financial presentation, we sold our dating services business in January 2019, and now those operations are reported as discontinued operations in our financial statements for both current and past periods.

Now, moving on to the year-over-year revenue comparison on Page 9, Q2 2019 revenue of \$4.9 million decreased 16.3% versus Q2 2018, and each revenue line which contributed to that decline. Subscription revenue, the biggest line item witness a 12.3% year-over-year decline. But as we'll see in the sequential comparison, that trend has improved. Technology services revenue which was down 18.2% is expected to be lumpy especially at this early stage of the business. Again, this revenue stream is almost entirely from one client ProximaX and the technology services agreement with that Company.

Next, we'll move on to Page 10, which covers sequential quarterly revenue. We see here that when compared to Q1 2019, Q2 total revenue has stabilized and subscription revenue is even slightly up, reversing a downward trend. Though we don't expect this to be a permanent trend reversal, it's an important step towards the reinvigoration of the video chat business that we've been building towards.

Technology services revenue was approximately flat in this sequential quarterly comparison. It should be noted however, that Q2 marked the final period of recognition of ProximaX revenue from the 2018 prepayment. ProximaX has represented substantially all of technology services revenue to date, and without it we would expect the remainder of the year will likely see a steep drop in this revenue line. I would further note however, that nearly all of the 2019 ProximaX revenue has been non-cash. So its non-recurrence will not impact cash flow in the current year.

We mentioned that technology services revenue is unpredictable and lumpy. We remain optimistic about the year—about the near term potential of converting our secure communications customer prospect pipeline into sizable revenue-bearing contracts, though it's difficult to pin down the timing of this conversion. Even if we land a contract as soon as Q4 2019, the vast majority of revenue would likely be recognized in 2020 and thereafter.

On Page 11, we discuss earnings. Q2 net income in the year-over-year comparison improved \$2.3 million driven by 2019 cost cutting, and the non-recurrence of two 2018 items, a token fair value write-down of approximately \$2 million, and losses from discontinued operations of approximately \$571,000.

Total expenses in Q2, decreased 14% as compared to Q2 of 2018 as a result of continued cost discipline and there's more future upsides since those expense reductions were not fully solved in the quarter. The expense reductions focused on mostly G&A and headcount. Net income from continuing operations for the quarter improved \$1.6 million year-over-year. Q2 2019 Adjusted EBITDA hit approximately \$1 million which decreased by approximately \$292,000 on the year-over-year comparison. However, the sequential quarterly comparison shows significant improvement over the \$500,000 of Adjusted EBITDA reported in Q1 of 2019. That improvement was driven in part by the expense reductions I mentioned.

Next, we'll move to Page 12, to review cash flow dynamics. Net cash flow for the three months ended June 30, 2019 was approximately negative \$627,000. But this is sequential quarterly improvement of approximately \$659,000 as compared to the first quarter of 2019. The negative cash flow dynamics in the first half of 2019 are in part due to expenses and fulfilling the ProximaX contract, and those expenses have now transition to R&D for secure communications. But those expenses were unmatched with cash flows in 2019, since substantially all ProximaX revenue recognized in 2019 was prepaid in 2018.

Cost-cutting played a big role in reducing the cash burn between the first quarter and the second quarter of 2019, and we're endeavoring to drive that burn still lower. Cash, and cash equivalents were approximately \$4.6 million at June 30, 2019 and we had zero debt, and approximately \$647,000 of operating lease obligations. So for now, that concludes our prepared marks. We're excited about the future growth prospects of the business, and I'd love to answer any questions that our attendees might have.

Operator:

Thank you. The question-and-answer session will be conducted electronically. To ask a question, please press star, one on your phone at this time. If you're on a speaker phone, please make sure your mute function is turned off to allow the signal to reach our equipment. Again, that is star, one to ask a question. We'll pause for just a moment. Press star, one if you would like to ask a question. Mr. Harrington, it appears we have no questions. I'd like to turn it to you for any additional or closing remarks.

Alex Harrington:

Well, thanks to all for joining today. Please do let us know if you have any questions after the fact. We'd be delighted to answer them, and we're looking forward to future communications with our shareholders, so we'll be in touch. Thank you so much.

Operator:

Let us conclude to this conference. Thank you all for your participation. You may now disconnect.