



CITRON COMMENTS ON MOBI CALL AND PIPER NOTE — AND REITERATES PRICE TARGET OF \$3.

Update: May 4, 2011: post- Conference Call Comments:

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In its research note this morning, Piper Jaffray raised their target for MOBI from 12 to 15, stating concerns for its fundamentals are "overblown".

Citron calls Piper liars and challenges them on this issue.

What is the truthful Company Description?

(We removed the Piper commentary — as expected Piper required that we take down their research page.)

Piper's note repeats MOBI's claim that **"It operates the leading mobile app store in China."**

This statement is not true. The company CFO claimed it was based on "independent" research, but on today's conference call, admitted it was a 2009 study **commissioned and paid for by the company.**

If Piper cannot describe the company accurately, they have no business claiming to publish analysis of it, much less raise multiples or targets.

As the links on the Citron report (below) demonstrated yesterday, this claim by MOBI is **100% FALSE.** Even the company has backed off that language in its company description in today's PR. Citron challenges MOBI, or Piper for that matter, to show a single credible and independent source verifying that MOBI's app store is in fact the "top mobile app store in China" – or in the top 10, for that matter.

If in fact they were the #1 mobile app store in China, it would only prove the obvious – that they are doing a **very bad job of monetizing it!**

If they were what they say, **their revenues would be ramping sharply through the roof right now**, while the cheap feature phone market is at its peak.

Instead, revenues were flat to lower last quarter, and will apparently not materially improve this quarter. Meanwhile, it's their expenses that are ramping sharply higher as they add headcount to service their patchwork "payments network".

In light of these obvious facts, Piper's justification for raising its target is to (drum roll) ... **increase the multiple?!?** Talk about "nothing new"!!! Not on Wall Street.

Piper says "Nothing new" and Citron agrees

Piper says there is "nothing new" ... A statement we agree with. It is the same company that couldn't make payroll just eight months ago until its IPO got done at \$8, and traded thereafter at \$6 per share. Its not generating new revenue or profits either. Its competitive position with regard to the China mobile handset market isn't new since then.

We challenge anyone to argue that the future penetration of feature phones is going to be greater than that of smart phones in China.

Citron has great respect for Gene Munster. We are surprised and disappointed that this piece of sloppy research would go out with his name under it.

MOBI's market in their own words

MOBI states that their market is composed of "young, uneducated and poor" Chinese youth. The CFO got excited describing his market buying "virtual homes and virtual furniture".

Wake up people! Their market can't buy real furniture, but they're going to spend increasing millions in MOBI's virtual fantasy world?

The CFO also commented people don't like to pay for game apps on Android – they like the free ones – but still claims they'll be paying up for games on Maopao – real soon now!

Future of mobile phone business in China

This is the future of mobile phones in China, and it is foolish to pretend otherwise:

<http://www.businesswire.com/news/home/201105040061Increases-Smart-Phone-Market-Leadership-35>
[<http://www.businesswire.com/news/home/201105040061Increases-Smart-Phone-Market-Leadership-35>]

It is obviously the platform that developers are clamoring to make their hot new games for — a large, worldwide market, not a niche market held captive between China wireless operators and certain handset manufacturers.

MOBI claims it is a technology company

Look at their R&D spend last quarter and the last year.

Citron sticks to its opinion that MOBI addresses a low-spending niche market in China, with a rapidly obsolescing technology platform which has already seen its best days, and reiterates its generous \$3 target.

Citron asks Piper – what is the expression for “buggy whip” in Chinese?

Cautious investing to all..... and be particularly skeptical of pied pipers!

Original report:

Citron Reports on Sky-Mobi Limited (NASDAQ:MOBI) With a Price Target of \$3....read to understand.

Citron Research understands and respects the recent surge in pre-eminent Chinese internet stocks. While the financials of many of these companies might not be compelling today, some offer unique business models and the potential to establish their dominant competitive positions in their spaces, driven by China’s rapidly growing internet user base. Whenever you get these manias, many companies “ride along on the coattails”. In the case of Sky-Mobi Limited (NASDAQ:MOBI) the company has manipulated the truth to hide their dying business model.

What MOBI Is:

Sky-Mobi sells games and other applications for low-end “feature phones” (i.e NON-smart-phones) in China. Their non-game products include chat applications for several social network websites.

The company currently has no position in the smart phone or high-end cell phone business. The company operates an application store, but so does every major cell phone manufacturer.

Nokia and Android-based phones are garnering major market shares in the high-end and smart-phone markets, where MOBI does not compete... and leaves it facing irrelevance.

What MOBI Is Not

MOBI is **not** a leading application store in China. Even more important, MOBI is **not** a play on the Chinese mobile internet / social networking market. MOBI is **not** a tech company and does **not** have market share or disruptive technology.

The stark reality is that “feature phones”, which MOBI's business addresses, are inexpensive phones that **DO NOT** browse the internet, **DO NOT** have **maps, GPS** or **local search**, and are not capable of forming social networks, or participate in locally targeted crowd marketing apps like Groupon. They enable Chinese feature-phone users to text-chat with one another while playing simple graphical games on small screens. Users can also post text messages onto certain social network platforms like Facebook and Twitter.

Within the next couple of years, a new and cheaper generation of larger screen touch-screen Android-based smart-phones will sweep into the China cell marketplace, delivering this functionality. MOBI is just another wannabe in this market. There is no investment thesis in MOBI gaining a foothold in this new market against many better-capitalized competitors from its current business model.

IPO or Bust – (It was the bust)

The first sign of trouble with MOBI was evident as its IPO date approached. In the same week that YOKU and DANG represented some of the hottest IPOs of 2010, the Sky-Mobi IPO was a total dud.

First, the IPO, which [attempted to raise \\$150 million](http://www.avcj.com/avcj/news/1899843/sequoiabacked-sky-mobi-files-usd150-million-nasdaq-ipo) [\[http://www.avcj.com/avcj/news/1899843/sequoiabacked-sky-mobi-files-usd150-million-nasdaq-ipo\]](http://www.avcj.com/avcj/news/1899843/sequoiabacked-sky-mobi-files-usd150-million-nasdaq-ipo) had to settle for \$58 million (gross) due to lack of demand , but even so, pricing had to be [set at the low end](http://seekingalpha.com/article/241194-china-s-sky-mobi-prices-ipo-at-bottom-of-range) [\[http://seekingalpha.com/article/241194-china-s-sky-mobi-prices-ipo-at-bottom-of-range\]](http://seekingalpha.com/article/241194-china-s-sky-mobi-prices-ipo-at-bottom-of-range). Then it broke syndicate, finishing [down](#)

25% on its first day of trading

[<http://www.businessweek.com/news/2010-12-11/china-s-sky-mobi-bona-post-biggest-1st-day-u-s-slumps-of-2010.html>],

contending for the record of the worst IPO first day performance of 2010. Then, it fell a further 20% in the following days (during the extremely strong December 2010 rally). There was just no demand for this stock, and it bottomed around \$5 a share.

The problems at MOBI were evident as stated in this article from a China Tech Journal, which stated that MOBI better go public now and raise money because their business was about to be made obsolete.

<http://www.c114.net/news/16/a568999.html>
[\[http://www.c114.net/news/16/a568999.html\]](http://www.c114.net/news/16/a568999.html)

"Sky's not a good time, Song Tao said that the company unable to pay wages for several months, has been exhausted state."

— translation courtesy of Google Translate

(Song Tao is MOBI's Founder, Chairman, Chief Exec. Officer, Member of Audit Committee and Member of Corp. Governance & Nominating Committee)

Conclusion: Some companies go public to thrive, but Sky-Mobi went public to survive. This was just five months ago....has anything really changed?

How the Company is Lying to Investors

MOBI claims to be the "largest App store" in China. THIS IS A LIE – It is not even close to the truth. [Here is the real list of top App stores in China:](#)

[<http://thenextweb.com/asia/2011/01/20/nokia-ovi-store-is-the-top-application-store-in-china/>]

<http://thenextweb.com/asia/2011/01/20/nokia-ovi-store-is-the-top-application-store-in-china/>
[\[http://thenextweb.com/asia/2011/01/20/nokia-ovi-store-is-the-top-application-store-in-china/\]](http://thenextweb.com/asia/2011/01/20/nokia-ovi-store-is-the-top-application-store-in-china/)

MOBI also claims that it is a leading mobile social network in China....another lie.

Here's the list of top social networking sites in China ...

No MOBI here [<https://1.bp.blogspot.com/-LuH3xUDo0PE/TZ3haCXGVjI/AAAAAAAAABuw/wFGJl15-SNS-table-1024x789.jpg>] :

Or here

[http://www.readwriteweb.com/archives/china_to]
:

Or here:

[<http://www.buzzom.com/2011/04/top-five-social-networking-sites-in-china/>]

Or even among the top 15 here:

[<http://techrice.com/2011/03/08/chinas-top-15-social-networks/>]

Here's what they say in **their own** filings about their nascent attempt to stimulate social network-based business:

“We anticipate that community-based applications with social network functions, such as mobile social games, will generate an increasing percentage of our revenues in the foreseeable future. However, **we began operating pilot test mobile social games in 2008 and only have limited experience in this area.**”
(emphasis is Citron's)

Metrics Show Lies ... and Doom

"Figures don't lie, but liars figure." – *Samuel Clemens*

In MOBI's most recent fiscal quarter, ending March 2011, it claims its registered members roll has grown from 12.5m to 58.6m — a stunning increasing of 368.8% year over year. Is it too good to be true? Sorry, it is.

The problem with its “registered members” is that the number of **inactive members** is growing even faster. MOBI's filings don't compute the number of inactive members, but it does count “active members”, using a very weak definition. To be

counted as “active”, a member has to visit their app store **just two times** during the same month – and **ONLY FOR ONE MONTH** in a three month reporting period. Nevertheless, while their active user count grew 10.64% q over q, **their “inactive” (or staled out) members grew 35.2%, to a whopping 47.6 million.** Yes folks, the little number they don’t disclose is that **83% of their “registered members” are inactive, even by their own weak definition of “active membership”.**

This demonstrates that “membership doesn’t have its rewards” when it comes to MOBI. The notion that members somehow comprise a nascent pool of monetizable online community is an intentionally created mis-perception. In English we call that a lie.

Not to mention that cell phone sales in China grew 57% in 2010, mostly smart-phones. It is tough to believe that MOBI during that time could grow members 400% — exclusively from non-smart phone users.

http://articles.timesofindia.indiatimes.com/2011-01-24/hardware/28369506_1_china-mobile-mobile-phones-3g
[\[http://articles.timesofindia.indiatimes.com/2011-01-24/hardware/28369506_1_china-mobile-mobile-phones-3g\]](http://articles.timesofindia.indiatimes.com/2011-01-24/hardware/28369506_1_china-mobile-mobile-phones-3g)

As we saw this week with the restated Renren user numbers, it is not uncommon for Chinese internet statistics to exaggerate membership numbers.

<http://www.nytimes.com/2011/05/02/business/global/02>
[\[https://www.nytimes.com/2011/05/02/business/global/02\]](https://www.nytimes.com/2011/05/02/business/global/02)

The disconnect between perception and reality is clearly outlined in MOBI’s reported numbers. For example, the company typically makes headlines out of huge percentage gains in non-monetizable (and notoriously unreliable) numbers such as numbers of downloads. **But they don’t mention that average revenue per download has plunged – their reports not only fail to mention it, they don’t even calculate it!**

	3 Months — Sept 2010	3 Months — Dec 2010	Pctg Difference	Com
Downloads	719 million	846 million	+ 17.6 %	Wo Big Hea
Revenue per Download	.031c USD	.024c USD	(22.3 %)	Shh not men this. (MC does repc calc num
Site visits	3.3 billion	3.5 billion	+ 6.6 %	
Total Revenues USD	25.994m	24.210m	(6.86 %)	Cont reve Hell
Gross Profit USD (Total Revs less Cost of Rev	7,326 m	7,367 m	0.56%	Flat
Profit from Ops	224	(919)		Dov 1.14

				q ov
R&D expense USD	1,936 m	1,935m	0.0%	No c
Sales Mktg	1,809 m	2.076 m	+14.75%	Up digit
G&A USD	3.393 m	4.273m	+25.91%	Up digit

The company has become a financial disaster since IPO — and it wasn't so great beforehand.

The most charitable way to spin these changes is that the company is already experiencing “the law of large numbers”, in a sector subject to brutal competition, short-lived fads, and a roar of competitive “noise”. Its most profitable days were when it was operating on a shoestring with very limited capital, with a couple of hot game titles.

More likely, it was a very poor candidate for IPO, and is now relegated to a small niche in the cell phone add-on space which has already seen its best days. Even after doubling headcount over the last year, they have been unable to ramp revenues; while they face plateau'd revenues, they're absorbing declining margins on every front.

Financials are terrible compared to KONG

At its peak last week, MOBI sported a market valuation north of \$700 million dollars with \$79 million dollars in cash, and no long term debt.

KONG had a market valuation of around \$325 million dollar with \$157 million dollars in cash and 3.5 million USD long term debt. MOBI and KONG's respective enterprise values are \$621 million and \$172 million. Even though MOBI commands a hefty valuation when compared to

KONG, it doesn't appear MOBI has a substantially different business model from KONG

Comparable Valuation of MOBI and KONG

(All figures USD)	MOBI	KONG	
Shares Outstanding	32.17	37.31	
Market Cap	697.2	326.1	
Current Share Price	21.67	8.74	
Cash USD mrq	69.7	139.2	
Enterprise value	627.5	186.9	MOBI priced 235% higher than KONG
Revs last qtr	24.2	36.1	MOBI 32.97% less than KONG
Revenues trailing 12 months	96.9	149.6	MOBI 35.3% less

			than KONG
Profit / loss from operations last q (before adjustments)	-0.9	4.9	MOBI 5.8 million less than KONG
Profit / loss from operations trailing 12 months	1.0	4.0	MOBI 3 million less than KONG

MOBI sports an enterprise value more than **twice that of KONG**, but KONG shows it is a better value by every metric of revenue and profit, both for the most recent quarter and year. In fact, **KONG is valued at 1.14 times its 2010 revenue while MOBI is valued at 7.7 times its 2010 revenue – over 6 times higher!**

EVEN though Kong is a better business, (it sells some iPhone games) if we were generous to MOBI and gave it the same valuation as KONG at 1x revenue, the stock price would be \$3 – Hence our target.

Risks all over the business ...read for yourself.

Citron knows what normal risk factors look like. Most companies state the boiler plate language that we see over and over. But not MOBI — at least they were honest about the risks. If you read the prospectus you see a company that is being attacked on all sides of their business model.

<http://sec.gov/Archives/edgar/data/1500252/0000950123>
<https://sec.gov/Archives/edgar/data/1500252/0000950123>

Squeezed by the Cell Phone Companies:

“Such measures make it more burdensome for users to purchase applications and content through our application store. As a result, some users purchased fewer applications and less content through Maopao or even ceased purchasing. In addition, when more SMSs need to be transmitted to effect the same volume of transactions, we face more billing and transmission failures. All these adversely affected our revenues. In addition, in September 2010, China Mobile began implementing another set of new measures which require users to send triple confirmation SMSs before a transaction can be effected.”

Hurt by the handset manufacturers:

“Handset companies often pre-install other mobile application stores in addition to Maopao, which could adversely affect purchases of applications and content on Maopao, resulting in a decrease in our revenues. In addition, certain handset companies may consider entering the mobile application store market, and our relationships with such handset companies may be adversely affected as a result.”

Problems with billing:

“These situations are known in the industry as billing and transmission failures. In the fiscal year ended March 31, 2010 and the six-month period ended September 30, 2010, the monthly MR amounts we received from mobile network operators were approximately 20% to 30% lower than the monthly MO amounts recorded on Maopao ...”

Competition they can't overcome:

“New technologies in our industry could render the technologies and product offerings that we are developing or expect to develop in the future obsolete or uncompetitive, thereby potentially resulting in a decline in our revenues and market share.”

Then on April 27, Nokia invaded their space:

<http://www.pcworld.com/businesscenter/article/226>
[\http://www.pcworld.com/businesscenter/article/226

Which all leads to the key statement:

“Our failure to anticipate or successfully implement new technologies could render Maopao uncompetitive or obsolete, and reduce our revenues and market share.”

If this it wasn't onerous enough, MOBI is in the shadow of the PRC government regulators too. To create an alternative to being dependent on billers to collect user fees, MOBI created its own form of payment, called “K-Currency”.

“Our item-based revenue model may cause additional concerns with PRC regulators who have been implementing regulations intended to limit the total amount of virtual currency issued by online game operators and the amount of purchase by an individual game player. The restrictions imposed by the above rules may result in lower sales of our virtual currency, and could have an adverse effect on our revenues from games. If our operations or the applications and content on Maopao are deemed to have violated any of these rules and regulations, we may be subject to penalties and our results of operations may be materially and adversely affected.”

Conclusion

The company reports just one more time – next week – before expiration of MOBI's (six month) stock lockup looming just next month.

Citron believes that this company is doomed and will eventually trade below whatever cash they might have left. This is a terminal business model. How does one say buggy whip in Chinese?

Cautious Investing To All

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