

uCloudlink Group Inc. – Earnings and Revenue Beat Expectations with New Product Launches and Potential Opportunities

uCloudlink Group Inc. (NASDAQ:UCL)

Share Price: \$2.22

Current Valuation: \$10.00



Key Statistics

52 Week Range	\$1.17-\$6.60
Avg. Volume (3 months)	7,142
Shares Outstanding	36.98M
Market Capitalization	\$82.09M
EV/Revenue	0.8x
Cash Balance*	\$20.26M
Analyst Coverage	2

*Cash balance as of Q3 2023

Revenue (in \$mm)

Dec - FY	2021A	2022A	2023E
1Q	17.7	15.6	18.0
2Q	19.2	18.0	22.0
3Q	19.3	18.2	23.9
4Q	17.6	19.6	24.2
FY	73.8	71.5	88.0

Earnings Per ADS (in \$)

Dec - FY	2021A	2022A	2023E
1Q	(0.54)	(0.27)	0.06
2Q	(0.29)	(0.22)	(0.02)
3Q	(0.25)	(0.15)	0.09
4Q	(0.54)	(0.03)	0.07
FY	(1.61)	(0.64)	0.19

Stock Price Chart



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Investment Highlights

- UCL Surpasses Q3 Earnings and Revenue Estimates** - uCloudlink reported its financial results for Q3 2023, with total revenues of \$23.9 million, up 31.0% year over year, *exceeding our estimate of \$23.7 million*. The increase was primarily due to a 31.9% YoY increase in services revenues driven by the accelerated recovery of international travel and a 29.0% YoY increase in product sales from an expanded product offering backed by the company's cloud SIM technology and HyperConn solution. Overall gross margin was 51.2%, compared to 47.7% in the same period of 2022. Total operating expenses increased from \$7.9 million to \$9.2 million, as the company strengthened its sales force to promote its newly launched products. UCL's net income was \$3.5 million, or \$0.09 per basic and diluted ADS, in Q3 2023, *beating our estimate of \$0.45 million or \$0.01 per basic and diluted ADS*. This compares to a net loss of \$4.6 million, or \$0.15 per basic and diluted ADS a year ago. *We model steady growth in the company's core UCL 1.0 business and product sales, driven by the accelerated recovery of international travel and new product launches to capture market share. Meanwhile, the company has the potential to expand profit margins and further improve profitability through a diversified product mix.*
- New Products Launched Offering Long-Term Growth Potential** – The company launched various new products during the quarter, bringing its average daily active terminals to a record high of 325,078, with its market share continuing to soar. The new products including what the company believes is the world's smallest GPS-enabled portable Wi-Fi terminal and the GlocalMe SIM card that allows users to obtain multiple global data plans covering ten major destination countries on demand. The company aims to improve user experience and expand market share by upgrading product features – adding AI services to its Wi-Fi products, which have been popular with Chinese outbound tourists. Although Chinese outbound travel remained soft, UCL's market share has increased significantly there, with its revenues from mainland China accounting for 17.2% of total revenues in the quarter, compared to 2.4% in the same period last year.
- Progress in IoT and Fixed Broadband Unlocking Additional Opportunities** – In Q3 2023, a major MNO's devices utilizing UCL's cloud SIM technology-powered IoT solutions entered the Japanese market, marking the company's significant progress in the IoT field. UCL is expected to work with major IoT module manufacturers on integrated cloud SIM technology and prepares to launch 5G Customer Premises Equipment (CPE), a new offering to meet the fast-growing demand for home and office internet connectivity, which is seeking to gain additional market share in the fixed broadband market.
- Valuation Update** – Our valuation for UCL remains \$10.00, combining discounted cash flow and comparable company analysis, which is contingent on the company maintaining its successful execution.

Company Description

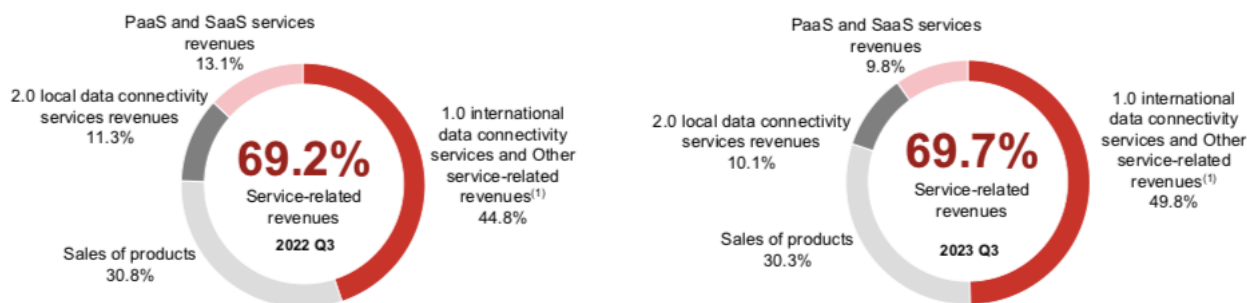
uCloudlink operates as an innovative mobile technology company that offers the world's first and leading mobile data traffic sharing marketplace to users globally. Leveraging its integral cloud SIM technology, it allows users to enjoy a smooth mobile connectivity experience without limitation to one MNO. uCloudlink was incorporated in 2014 and is headquartered in Kowloon, Hong Kong.

Third Quarter 2023 Results

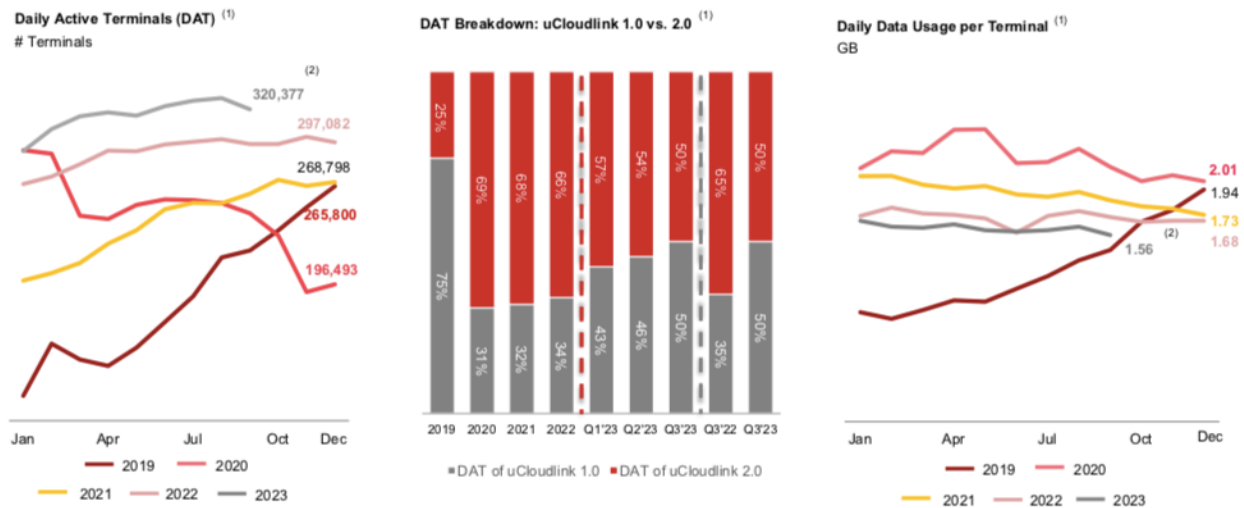
For the three months ending September 30, 2023, uCloudlink reported total revenues of \$23.9 million, up 31.0% from \$18.2 million in Q3 2022. Revenues from data connectivity services were \$13.8 million, an increase of 37.5% compared with \$10.1 million in the year-ago period, primarily due to higher international and local data connectivity services, which grew 42.7% YoY to \$11.4 million and 14.3% YoY to \$2.4 million, respectively, aided by the accelerated recovery of international travel and UCL’s continuous investment in its local data connectivity business. Revenues from PaaS and SaaS services were \$2.3 million, down 2.0% from \$2.4 million in the same period of 2022. Revenues from sales of products increased from \$5.6 million to \$7.3 million due to the increase in sales of terminals. In terms of geographic distribution, Japan as UCL’s largest market contributed 44.2% of total revenues, North America contributed 26.3%, while mainland China and other countries contributed 17.2% and the remaining 12.3%, respectively, compared to 35.1%, 41.5%, 2.4%, and 21.0%, respectively, in Q3 2022. Overall gross profit was \$12.2 million, or 51.2% in gross margin, compared to \$8.7 million, or 47.7% in gross margin in the same period last year, with improved gross margins on sales of products. Total operating expenses were \$9.2 million, compared to \$7.9 million in Q3 2022, a roughly 16.5% increase, as the company enhanced its sales force to promote newly launched products: R&D expenses increased by 8.4% YoY to \$1.6 million, primarily due to the increase in staff costs; S&M expenses increased to \$3.8 million, up 77.3% over the year, due to the increase in promotional fees and staff costs; and G&A expenses declined by 11.0% to \$3.8 million, primarily attributable to a decrease of \$1.2 million in bad debt provision, which was partially offset by an increase of \$0.6 million in staff costs. uCloudlink’s net income for Q3 2023 was \$3.5 million, or \$0.09 per basic and diluted ADS, compared to a net loss of \$4.6 million, or \$0.15 per basic and diluted ADS in the year-ago period. *We see UCL having the potential to continue this growth momentum, as the company generates further revenues from the resuming international data connectivity business and the launch of new products with expanded market shares.*

Variance Table (\$ in millions, except per share data)			
	Q3 2023E	Q3 2023A	Variance (Actual Versus Result)
Revenue	23.7	23.9	0.2
EPS	0.01	0.09	0.08

Source: Diamond Equity Research



Source: UCL Investor Presentation November 2023



Source: UCL Investor Presentation November 2023

Liquidity and Balance Sheet

As of September 30, 2023, uCloudlink’s cash and cash equivalents totaled \$20.3 million, compared to \$18.6 million as of June 30, 2023, primarily due to the net inflow of \$2.8 million from operations and net proceeds of \$0.7 million from bank borrowings, partially offset by a repayment of \$0.9 million for bank borrowings and a payment of \$0.8 million for capital expenditures. *The company has achieved positive operating cash flow sequentially since Q2 2022, demonstrating UCL’s ability to achieve financial sustainability to support its long-term operations and growth.* The company’s asset-light operating model and continuous positive operating cash flow strengthened its balance sheet.

Management Guidance

uCloudlink expects total revenues to be between \$22.0 and \$26.2 million for Q4 2023, representing an increase of 12.2% to 33.7% compared to the same period of 2022.

Investment Thesis

uCloudlink is targeting the large mobile data connectivity service market driven by the increasing adoption of mobile devices and internet penetration. This includes the local data connectivity market, the international roaming market as well as the global IoT market. In addition, the robust development of the entire IoT industry further drives the demand for the data usage and connectivity services as we approach 5G widespread adoption, where entirely new applications will be possible in various application scenarios such as mobile broadband (MBB) and fixed broadband (FBB), industrial automation, autonomous driving, AR/VR, internet of vehicles, cargo transportation and logistics and cloud computing, which may require new mobile data connectivity solution for users, hardware vendors and carriers with higher speed and more reliable connections. uCloudlink operates as an innovative mobile technology company that offers the world’s first and leading mobile data traffic sharing marketplace to billions of users globally, serving 2,539 business partners in 63 countries and regions, with aggregated mobile data allowances from 367 mobile network operators (MNOs) globally as of September 30, 2023. Leveraging its integral cloud SIM technology and architecture, which allows dynamic selection of network services based on signal coverage and cost, and intelligent distribution of data traffic in the SIM card pool to terminals that may support multiple end devices through its cloud SIM platform, the company provides mobile data connectivity services with reliable connections, high speeds and competitive pricing, allowing users to enjoy a smooth mobile connectivity experience without limitation to one particular MNO. Currently the company operates its business under what they refer to as uCloudlink 1.0 and uCloudlink 2.0 models, and plan to launch uCloudlink 3.0 model in the future. Under the UCL1.0, the company primarily offers pocket WIFI leasing, mobile WIFI retail, GMI mobile phone roaming, and other related services for international travelers that need mobile data connectivity services across different countries, although we note various products also are compatible in local markets. Products of UCL 2.0 stage includes home broadband, GMI mobile phone data service, IoT data service and other related services, and aim to provide mobile data connectivity services to local users across different MNOs in a single country. uCloudlink 3.0 is in trials, which is technologically ready. We note each segment has clear growth roadmaps and are targeting large market opportunities. uCloudlink is well positioned to capture growing mobile data connectivity service market segments by leveraging its sophisticated cloud SIM technology and architecture, distinct mobile data traffic sharing marketplace enabling a smooth mobile connectivity experience, and reasonable management team with years of operational experience in industry. We also note the recently launched HyperConn™-Enabled 5G Mobile WiFi Device, which uses AI to ensure users always have the best WiFi connection, opens new markets such as education, IoT, remote work, and surveillance. HyperConn™ products can also help MNOs develop data connectivity markets globally, including 5G markets. Additionally, HyperConn™ products will allow the company to target IoT opportunities in new industries. In the second half of year 2021, the company released the GlocalMe Numen (first HyperConn 5G mobile Wi-Fi device, MSRP \$599), GlocalMe Genie, a 4G pad device powered by HyperConn™ (unpriced), and Mini Turbo, portable Wi-Fi Hotspot equipped with HyperConn. As of September 30, 2023, UCL had 181 patents with 145 approved and 36 pending approval. The Company expects strong growth momentum to continue over the next couple of years given its aggressive marketing strategy, increasing mobile penetration, and the resumption of international travel. *Given uCloudlink’s growth potential and relatively inexpensive valuation, the company in our view offers investors a unique opportunity to invest in the growing data connectivity industry, as 5G adoption expands, which is likely to benefit from the institutional money flowing into the global mobile data connectivity service industry.*

uCloudlink is targeting the enormous mobile data connectivity service market driven by the increasing adoption of mobile devices and internet penetration, and the surging demand for optimal mobile data traffic solutions with high speed and reliable connections, as 5G adoption grows

We view uCloudlink as well positioned to capture market segments with its sophisticated cloud SIM technology and architecture, distinct mobile data traffic sharing marketplace enabling a smooth mobile connectivity experience, and seasoned management team with years of operational experience in the industry

Risk Factors

- uCloudlink's business has been and is likely to continue to be materially adversely affected by the outbreak of COVID-19. uCloudlink depends on network operators for their wireless networks, infrastructure, and data traffic. Any disruptions of or limitations on the company's use of such networks, infrastructure and data traffic may adversely affect its business and financial results
- The company's ability to grow its business and user base for its service may be limited unless it can continue to obtain data traffic at favorable rates
- Litigation at uCloudlink is still ongoing. The company is, and may in the future be, subject to intellectual property claims, which are costly to defend, could result in significant damage awards, disrupt its business operation, and could limit its ability to use certain technologies in the future
- Since the governments in countries and regions such as China and Japan have or will strengthen the enforcement of regulation over use of M2M cards and real-name registration for SIM card users, the development of its 2.0 business may be slowed down
- The company is highly regulated in all its areas of operations and could be impacted by regulatory changes
- If expansions into new businesses do not achieve the expected results, the company's future operations and growth prospects may be materially and adversely affected
- Trading range of ADSs are highly volatile, which could result in large losses for investors. The company's ADSs may be delisted under the Holding Foreign Companies Accountable Act if the PCAOB is unable to inspect auditors who are in China
- Founders hold substantial ownership of company; two founders own roughly 50% of outstanding shares and 92% of the aggregate voting power and their interests may not always be aligned with independent shareholders
- uCloudlink has limited liquidity and overall awareness, limiting its ability to obtain fair valuation
- uCloudlink is a small capitalization business and as such may struggle to attract sufficient sell-side coverage and exposure and will face specific executional risk factors because of its smaller size relative to large capitalization equities

These Risk Factors Are Not Comprehensive. For Full List of Risk Factors Please Read uCloudlink Group Inc.'s Latest Prospectus and/or 20F Filing Risk Factors

Income Statement

(\$ in M)	FY19A	FY20A	FY21A	FY22A	1Q23A	2Q23A	3Q23A	4Q23E	FY23E	FY24E	FY25E
REVENUES:											
Revenues from services	91.11	46.15	37.80	46.23	12.92	14.10	16.63	16.77	60.41	76.53	99.70
Sales of products	67.27	43.42	36.03	25.23	5.09	7.88	7.23	7.39	27.59	33.37	40.71
Total net revenues	158.38	89.57	73.83	71.46	18.01	21.98	23.86	24.16	88.00	109.90	140.41
Cost of services	(35.59)	(26.39)	(21.56)	(20.35)	(5.10)	(5.93)	(7.33)	(7.08)	(25.43)	(30.61)	(38.88)
Cost of products sold	(57.87)	(34.87)	(30.43)	(18.58)	(4.30)	(6.19)	(4.33)	(5.05)	(19.86)	(23.36)	(28.50)
Total cost of revenues	(93.46)	(61.26)	(51.99)	(38.93)	(9.41)	(12.11)	(11.66)	(12.13)	(45.30)	(53.97)	(67.38)
Gross (loss) profit	64.92	28.31	21.84	32.53	8.60	9.87	12.21	12.03	42.70	55.93	73.03
OPERATING EXPENSES:											
Sales and marketing expenses	(24.37)	(29.26)	(13.62)	(10.31)	(2.92)	(3.52)	(3.79)	(3.86)	(14.08)	(15.39)	(16.85)
Research and development expenses	(15.11)	(26.36)	(13.70)	(8.43)	(1.30)	(1.55)	(1.60)	(1.70)	(6.16)	(6.59)	(7.02)
General and administrative expenses	(20.22)	(43.22)	(28.55)	(18.73)	(3.44)	(3.87)	(3.82)	(3.84)	(14.96)	(16.49)	(16.85)
Other expense, net	0.29	7.55	(11.88)	(14.27)	1.12	(1.87)	0.32	(0.00)	(0.43)	(0.22)	(0.14)
Total operating expenses	(59.41)	(91.29)	(67.75)	(51.73)	(6.54)	(10.80)	(8.89)	(9.40)	(35.63)	(38.68)	(40.86)
EBIT	5.51	(62.98)	(45.91)	(19.19)	2.06	(0.94)	3.32	2.63	7.08	17.24	32.17
Interest income	0.19	0.04	0.01	0.02	0.01	0.02	0.01	0.01	0.04	0.01	0.01
Interest expenses	(0.44)	(0.29)	(0.19)	(0.44)	(0.05)	(0.03)	(0.03)	(0.03)	(0.13)	(0.15)	(0.20)
Amortization of beneficial conversion feature				(0.15)							
Income(loss) before income tax	5.26	(63.23)	(46.08)	(19.76)	2.02	(0.95)	3.31	2.61	6.99	17.09	31.98
Income tax expenses (benefits)	(0.06)	(0.19)	(0.24)	(0.16)	(0.01)	(0.03)	(0.02)	(0.02)	(0.08)	(4.27)	(7.99)
Share of profit in equity method investment, net of tax			0.29	0.07	0.07	0.06	0.20		0.33		
Adj. Net profit/(loss)	5.21	(63.42)	(46.04)	(19.85)	2.07	(0.92)	3.49	2.60	7.24	12.82	23.98
Accretion of Series A-2 ordinary shares and Series A Preferred Shares	(2.54)	(1.29)									
Allocation to Series A-2 ordinary shares											
Income allocation to participating preferred shareholders	(0.30)										
Net income/(loss) attributable to Company	2.37	(64.71)	(46.04)	(19.85)	2.07	(0.92)	3.49	2.60	7.24	12.82	23.98
Earnings per share											
Basic	0.01	(0.25)	(0.16)	(0.06)	0.01	(0.00)	0.01	0.01	0.02	0.03	0.06
Diluted	0.01	(0.25)	(0.16)	(0.06)	0.01	(0.00)	0.01	0.01	0.02	0.03	0.06
Earnings per ADS (10 Class A equal to 1 ADS)											
Basic	0.10	(2.49)	(1.61)	(0.64)	0.06	(0.02)	0.09	0.07	0.19	0.33	0.57
Diluted	0.10	(2.49)	(1.61)	(0.64)	0.06	(0.02)	0.09	0.07	0.19	0.33	0.57
Weighted Average no. of Shares outstanding (in M)											
Basic	232.18	259.85	285.98	312.49	369.44	370.59	372.33	374.33	371.67	391.67	421.67
Diluted	232.18	259.85	285.98	312.49	369.44	370.59	372.33	374.33	371.67	391.67	421.67

Source: Diamond Equity Research

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