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Q3 2018 Fanhua Inc Earnings Call

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CORPORATE PARTICIPANTS

Chunlin Wang *Fanhua Inc. - Chairman & CEO*
Oasis Qiu *Fanhua Inc. - IR Manager*

CONFERENCE CALL PARTICIPANTS

Arthur Hall
Dan Tian *China International Capital Corporation Limited, Research Division - Analyst*

PRESENTATION

Operator

Thank you for standing by for Fanhua's Third Quarter 2018 Earnings Conference Call. (Operator Instructions) For your information, this conference call is now being broadcasted live over the Internet. The webcast replay will be available within 3 hours after the conference is finished. Please visit Fanhua's IR website at ir.fanhua Holdings.com under the Events & Webcasts section. Today's conference is being recorded. If you have any objection, you may disconnect at this time.

I'd now like to turn the meeting over to your host for today's conference, Ms. Oasis Qiu, Fanhua's Investor Relations Manager.

Oasis Qiu *Fanhua Inc. - IR Manager*

Good morning. Welcome to our third quarter 2018 earnings conference call. The earnings results were released earlier today and are available on our IR website as well as on Newswire.

Before we continue, please note that the discussion today will contain forward-looking statements made under the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. The accuracy of these statements may be impacted by a number of business risks and uncertainties that could cause our actual results to differ materially from those projected or anticipated. Such risks and uncertainties include, but not limited to, those outlined in our filings with the SEC, including our Registration Statement on Form 20-F. We do not undertake any obligation to update these forward-looking information except as required under applicable law.

Joining us today are our Chief Executive Officer and Chairman, Mr. Chunlin Wang; Chief Financial Officer Mr. Peng Ge; and Board Secretary, [Lily Lee]. Mr. Wang will walk you through our financial results in the third quarter of 2018. He and Mr. Ge, Mrs. Li would then take your questions after the prepared remarks.

Now I will turn the call over to Mr. Wang.

Chunlin Wang *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu *Fanhua Inc. - IR Manager*

Thank you for joining us on today's conference call. Here with me, we have our Chief Financial Officer, Mr. Peng Ge; and our Board Secretary, [Mrs. Lily Lee]. We will begin today's call with a review of our third quarter 2018 financial results and the major progress that was made during the quarter followed by a brief discussion of our business outlook for the fourth quarter 2018. Then we will have a Q&A session after the report.

Chunlin Wang *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu *Fanhua Inc. - IR Manager*

To begin with, I would like to give a brief analysis of industry dynamics. Since early this year, government efforts to ratify the order in the financial markets are set to continue. Deleveraging, removal of implied guaranteed return, cracking down on illegal fund-raising are the main themes. Meanwhile, insurance regulator continue its emphasis on long-term protection of products, capping the guarantee returns on savings type of insurance products and restricting the fast return feature for those products, which formed stark contrast with the



aggressive wealth management product offered by the banks in the first half 2018. As a result, consumers were held back from making decisions to purchase savings products, which directly led to a decline in sales agents income and dampened their morale, thus resulting in obvious drop in sales agents; productivity and active ratio across the industry. And as a result, negative growth in first year premiums of regular personal life insurance business, which is the most variable insurance business, has seemed to become an inevitably reality across the industry for the full year 2018.

Chunlin Wang *Fanhua Inc.* - Chairman & CEO

(foreign language)

Oasis Qiu *Fanhua Inc.* - IR Manager

Against this backdrop, we continue to report strong profit for the third quarter 2018. Operating income was up 48.7% year-over-year to RMB 124.6 million, again beating our previous guidance. And net income increased by 73.9% year-over-year to RMB 195.2 million.

(foreign language) Now let's look at the performance of our 3 business segments, firstly the life insurance segment. Our total life insurance premiums hit RMB 1.5 billion in the third quarter 2018, up 10.6% year-over-year, of which new business in terms of annualized premiums equivalent was down 28.9% from a year ago to RMB 394.5 million, as we had previously expected, mainly caused by the high base in the same period last year and the change in our product structure. As a result of the notice No. 134, the sales of fast return-type annuity products exploded in September 2017. In the meantime, guarantee returns from annuity products declined after new rule took effect. As a result, annualized premiums equivalent from high-ticket annuity insurance products dropped significantly in the third quarter of 2018, accounting for 11% of our total new business, as compared to 49% same period last year. Health insurance business, however, despite the fact that the per policy amount of health insurance products is typically less than half of that annuity products, remained strong growth during the quarter, up 101.4% year-over-year in terms of annualized premiums equivalent, taking up 82% of our total life insurance new business as compared to 28% a year ago.

Chunlin Wang *Fanhua Inc.* - Chairman & CEO

(foreign language)

Oasis Qiu *Fanhua Inc.* - IR Manager

We are particularly encouraged by the performance of our renewal business. Due to the strong growth in new business of our life insurance segment in the same period last year and benefiting from our outstanding renewal business management. Renewal premiums grew 109.5% year-over-year, which is one of the key drivers behind the continued rapid growth in our operating profits during the quarter. Gross margin of our life insurance business improved significantly during the third quarter 2018, largely attributable to the increase in the contribution from renewal business, which represented 20.6% of our total net revenues in the third quarter 2018, as compared to 9.3% in the third quarter 2017.

(foreign language) While the performance of our life insurance new business was largely in line with our prior expectations, we anticipate annualized premiums equivalent of our life insurance business to achieve solid growth year-over-year in the fourth quarter of 2018. As such, we maintain our estimate of positive growth in new life insurance business in terms of annualized premiums equivalent for the full year 2018.

Chunlin Wang *Fanhua Inc.* - Chairman & CEO

(foreign language)

Oasis Qiu *Fanhua Inc.* - IR Manager

The P&C insurance business segment. Revenues from the P&C agency segment in the third quarter 2018 mainly represented RMB 8.9 million on the platform service fee and RMB 14 million commission income from Baoxian.com. The decline in net revenues in this segment was mainly due to the transition of our auto insurance business towards a platform fee-based business model and the Baoxian.com's termination of business cooperation with one of its major business partners, a third party online lending service provider since June 2018. Despite the decline in revenues, as the gross margin from platform service fee is 100%, the overall gross margin from our P&C insurance business improved from 13.7% to 34.3% in the third quarter of 2018.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

Thirdly, the claims adjusting segment. The claims adjusting segment reported a solid performance with 9.9% year-over-year increase in net revenues, with gross margin improving from 40.1% a year ago to 44.8% in the third quarter of 2018.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

In the second part I'd like to discuss, the progress that we made on expanding our sales network. Firstly, as of September 30, 2018, total number of registered sales agents exceeded 716,000, representing the growth of 73.1% year-over-year. While total number of agents who have sold life insurance policies during the third quarter reached 44,686.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

And secondly, we are happy to welcome over 10 industry veterans to join us during the third quarter, who will serve as the general managers or deputies of our provincial branches. With their prior work and experience in top 5 life insurance companies, we believe that their expertise will enable the company to further improve our business operations to become more professionalized.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

Thirdly, in the next part, I would like to give you an update of the solid progress that our online platforms have made during the quarter. Firstly, CNpad, as of the end of the third quarter 2018, total registered and activated users were over 496,000, representing an increase of 49% year-over-year. And RMB 419 million auto insurance premiums were transacted through CNpad during the quarter, representing 84.5% of our total auto insurance business.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

Secondly, Lan Zhanggui. As of the end of the third quarter 2018, registered users of Lan Zhanggui has exceeded 716,000 with RMB 418 million insurance premiums transacted through the platform during the third quarter, of which RMB 373 million were P&C -- sorry, RMB 37.3 million were P&C insurance premiums and RMB 450 million were first year premiums of life insurance products, accounting for 93.6% of our total first year premium.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

Thirdly, Baoxian.com. The number of its registered users exceeded 2 million, up 66.7% year-over-year. And its quarterly active users reached 140,000, up by 98.3% year-over-year. Insurance premiums transacted through the platform were over RMB 72.4 million. And the decline year-over-year was mainly due to the termination of corporation with a fintech company in June. But its regular businesses, on the other hand, still maintained rapid growth.



Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

Fourthly, eHuzhu. eHuzhu has reported in net increase of nearly 300,000 registered members each month. As of September 30, 2018, its registered members have hit over 3.8 million with its active paying members exceeding 2 million. In 4 years since its launch, it has helped more than 1,495 families with RMB 250 million fund raised through the platform. Yiqizhu, an online fundraising platform for those contracted with a serious disease under eHuzhu, has helped 844 families to raise a total of RMB 3.9 million funds.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

Next, I would like to share with you some recent major developments. Firstly, I would like to take this opportunity to congratulate CNfinance on its successful listing on New York Stock Exchange on November 7, 2018, under the ticker symbol of CNF. After its IPO, our shareholdings in CNfinance is diluted from 20.58% to 18.6%. But as we still have a seat on its board, the investment will still be accounted for under equity measures.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

And then secondly, as we previously announced, as part of Tianfu New Area's investment introduction project, Fanhua Lianxin Insurance Sales Company, our wholly owned subsidiary, which is the holding company of our life insurance operation, completed its -- the relocation and registration of its head office from Beijing to the Tianfu New Area of Sichuan Province on August 27, 2018.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

As a result of the relocation, on November 2, 2018, the company received a onetime reward of RMB 8 million from the local government. Fanhua Lianxin will also be eligible to enjoy certain favorable tax treatment and fiscal incentives in proportion to its contribution to the local economy.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

After the relocation, we have resumed collection of headquarters-to-headquarters commission receivables from our life insurance company partners, which have previously been suspended. We expect our operating cash flow will return to normal level afterwards.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

In addition, pursuant to its policy of attracting an investment to develop the local economy, in 2016, the Renshou County government in which the Tianfu New Area is situated, expressed its support for Fanhua to publicly bid for a parcel of land in the Tianfu New Area to establish a back-office center. As Fanhua had neither a license nor interest in real estate development, on July 16, 2016, Fanhua established a joint venture with an independent, third-party real estate developer, Sichuan Tianyi Real Estate Development Company for the sole purpose of developing the parcel of land. Under this arrangement, Sichuan Tianyi would be responsible for developing the land



and providing core funding for development, while Fanhua would not provide any loan guarantee or any other funding for the development. Upon completion of the real estate development, Sichuan Tianyi would keep all the profits from the sales of the development properties and Fanhua will have a right to purchase certain properties at a discount. As of date, the project is still under development.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

Looking ahead to the fourth quarter of 2018, we expect annualized premiums equivalent of our life insurance business to grow by no less than 35% to RMB 460 million from RMB 340 million in the same period last year. For full year 2018, annualized premiums equivalent of our life insurance business is expected to achieve positive growth and operating income to grow by no less than 50% year-over-year. We are optimistic about achieving these targets.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

Now the management will open the floor for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Dan Tian from CICC.

Dan Tian China International Capital Corporation Limited, Research Division - Analyst

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

The question from Tian, Dan, and he has 3 questions. Firstly, the company recorded strong growth year-over-year in a number of sales agents in the third quarter. He would like to know whether the company has kept a record of our active sales agents, the number of our active sales agents each month or what's the active ratio of our sales agents. And the second question, insurance company have started preparing for the year-opening sales in 2019. And as far as the information he has got, the situation seems a bit challenging and he wonders what preparations we have made for the year-opening sales in 2019 and what are our tactics for the year-opening sales and what's our expectation for the growth of our life insurance business next year. And the third question, recently, there's an officer from the CBIRC, who talked about a reform -- a possible reform on the sales agents organization model, what's our view on this potential reform?

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

Since we started our expansion to achieve the target of 1 million sales agents by 2019, the net increase per month of our sales agents is basically in line with our expectations, we have maintained a net increase of like 25,000 agents per month. And as I mentioned just now, we have also attracted a lot of senior managers from top life insurance companies to join us, which is a good demonstration of the acceleration of the trend of the division of labor and the division of the manufacturing from distribution. However, due to the restriction on the annuity products and life savings types of products, the active ratio of sales agents is somewhat affected. And -- but we think that this is a normal phenomenon in times of correction or in times of adjustments of the industry. And so for -- as for Fanhua, the active ratio of our agents is relatively stable. And right now, basically 50% of our registered sales agents are active agents in terms of selling all types of products, all kinds of sales activities, including for selling like auto insurance, P&C insurance, and the accidental insurance and life insurance or have recommended someone to join our eHuzhu platform. And for the monthly active agents for life insurance business, this is the key metric that we put more focus on, currently, the number of active life insurance agents is roughly 5% of the total registered



sales agents or 10% of the active agents. So in 2018, particularly in the third quarter, we do see a somewhat decline in the monthly active ratio of our life insurance agents mainly because of the adjustment in the products as well as the rapid increase in the number of our sales -- registered sales agents, but we would definitely put more focus on increasing the active ratio of our sales agents going forward.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

As for the year-opening sales in 2019, I think life insurance company kind of in awkward stations. On the one hand, they want to put more focus on achieving their full year operating targets in 2018. And at the same time, they need to set a target for the year-opening sales. So as for -- based on information that we have gathered so far each insurance company gives different -- have different tactics for the year-opening sales.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

And now our year opening sales pace remains consistent in the past years. And we have made full preparations for the year opening sales. Firstly, we have already completed the product and the contract arrangements with the insurance companies. And we expect that after 2019, there will be more -- better performance in the sales of savings type of products, participating type of products because we think that consumers will have better digested the change in the product designs and the saving type of products, and they will be more willing to buy the savings types of products, driving the sales of this type of products. And then on -- we will hold our annual meetings on December 10, which will last like 5 days. By that time, we will deploy the specific tasks for the next year, and we look forward to a good performance in the year-opening sales.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

And the third question regarding to the speech by the deputy director of the intermediary division of the CBIRC, firstly, I think that the comment, actually, is not really quite official because the comments were made in a speech in a forum, which is more like an academic communication rather than an official attitude by the regulator.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

We are fully convinced of 2 trends. Firstly, long-term, regular life insurance products will still be mainly sold through individual sales agents. And then secondly, we firmly believe of trends -- of accelerating trends of divisions of manufacturing from distribution.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

Thank you.

Operator

Our next question comes from the line of Arthur Hall from Hallco.



Arthur Hall

The only question I had was the top 3 insurance carriers for the quarter, has that changed at all? Who were the top 3 for the life insurance carriers? And what was their percentage? And how do you see that changing?

Oasis Qiu Fanhua Inc. - IR Manager

(foreign language)

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

We maintain normal and active cooperation with our business partners. And still, a lot of new insurance companies are trying to pursue cooperation with us. There are 3 criteria that we will look for when we select our business partners, i.e. their product offerings and the sales service as well as their technology support capability. And right now, more and more insurance companies fit into this criteria. As for the top 3 in the third quarter, Huaxia accounts for 31% of our total life insurance revenues, and Tian'an represents 21% and the Aegon takes up 26%. And other companies like Taikang and ICBC AXA are also has been quite active to pursue the cooperation.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

And we expect that the cooperation with Aegon, Greatwall and Evergrande will have more positive performance in 2019.

Chunlin Wang Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu Fanhua Inc. - IR Manager

Thank you.

Operator

(Operator Instructions) I will now hand back to management for any closing comments.

Oasis Qiu Fanhua Inc. - IR Manager

Thank you for joining us on today's call. If you have any further questions, please feel free to reach out to us. Thank you.

Operator

Thank you so much. Ladies and gentlemen, that does conclude the call for today. Thank you so much for your attendance. You may now disconnect.

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