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FANH - Q2 2018 Fanhua Inc Earnings Call

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AUGUST 21, 2018 / 1:00AM, FANH - Q2 2018 Fanhua Inc Earnings Call

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 Second Quarter and First Half 2018 Earnings Conference Call. (Operator Instructions) For your information, this conference call is now being broadcasted live over the Internet. Webcast replay will be available within 3 hours after the conference is finished. Please visit Fanhua's IR website at ir.fanhuaholdings.com under the Events and Webcast section. Today's conference is being recorded. If you have any objections, you may disconnect at this time. I would 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 second 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 United States Private Securities Litigation Reform Act of 1995. The accuracy of these statements maybe 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 this forward-looking information except as required under applicable law.

Joining us today are our Chief Executive Officer, 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 second quarter of 2018. And he, Mr. Ge and Ms. Lee will 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 second quarter 2018 financial results and the progress that was made during the quarter, followed by a brief discussion of our business outlook for the second half of 2018. Then we will have a Q&A session after the report.



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Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

In the second quarter of 2018, the central government increased efforts to deleverage and rectify market disorders so as to contain financial risk. In the meantime, insurance regulators continue its strive to steer the industry back to its primary goal of providing long-term protection to consumers. Amidst this backdrop, new policy sales for most life insurance companies dropped year-over-year, as the growth in the number of sales agents in the industry stagnated, while consumers were held back from buying on expectations for more meaningful improvement in product design of annuity and participating insurance products in the coming quarters.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

As far as Fanhua is concerned, in the second quarter of 2018, we continue to report strong results, with operating income growing by 77.2% year-over-year to RMB 127.6 million, beating our previous guidance of RMB 100 million, and net income attributable to shareholders growing by 22.4% year-over-year to RMB 171.8 million. The earnings per ADS grew by 20% year-over-year. The stellar growth of operating income was mainly due to the faster-than-expected growth in new policy sales for life insurance products and the increase in contribution from the new business, which generates higher gross margin than new business.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

Now let's look at our life insurance business segment. During the second quarter of 2018, our life insurance segment posted strong performance across all of the key operational metrics. Total life insurance premium grew by 69.8% year-over-year to RMB 1.5 billion, outpacing the overall industrial growth, among which first year premiums grew by 41.4% year-over-year to RMB 713 million. And with newer premiums increased by 109.1% year-over-year to RMB 763.9 million.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

Of particular note, our new business started to show more impressive value. In the second quarter of 2018, our renewal premiums have surpassed first year premiums. And the revenues contributed by renewal business as a percentage of total life insurance revenues have increased from 7.6% in the same period last year to 15.8% in the second quarter of 2018. Renewal business of long-term regular life insurance products is crucial to the sustainable and sound development of the company over the long run as it provides the company with stable and recurring revenues and profits for years to come.

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Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

In the meantime, the operation fundamentals of our life insurance segment remain quite strong as evidenced by the following aspects: firstly, our sales force continue to increase at a record pace, with a number of registered sales agents growing 92.2% year-over-year to 630,995, and the number of performing sales agents for life insurance growing 97% year-over-year to 66,654; and secondly, the number of insurance policies during the second quarter of 2018 grew 143.9% year-over-year, and for that reason, our first year premiums continue to grow by 41.4% year-over-year, even though the average per policy premium for health insurance products, which have become the main product for the company, is much lower than that of annuity and endowment insurance products; thirdly, annualized insurance premiums from the health insurance business were up 177.1% year-over-year, accounting for 79.4% of our total life insurance business as compared to 42.7% a year ago. And fourthly, 13 months persistency ratio outperformed the industry average and remained above 94%.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

Let's turn to P&C insurance business segment. In the second quarter of 2018, our P&C insurance segment recorded RMB 91.8 million in net revenues, which represent platform service fee contributed by CNpad, and commission income generated by Baoxian.com, with the former contributing RMB 5.8 million and the latter RMB 86.0 million. Our P&C revenues in the same period last year mainly represented commission income from our auto and non-auto P&C insurance business.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

And then in the second quarter 2018, revenues of our claims adjusting business segment remained flat year-over-year at around RMB 72.0 million.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

In the third part, I would like to share with you a few operational progress that we made during the second quarter.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

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Oasis Qiu - Fanhua Inc. - IR Manager

Firstly, our 521 Development Plan. We rolled out the 521 Development Plan on June 14, 2018, after assessing the current market trends in our overall growth strategies. The plan is a mid- to long-term initiative to facilitate the implementation of Fanhua model, with an aim to cultivate and retain key talent for the company. The plan is meant to motivate all Fanhua employees and sales agents to be more dedicated, professional and passionate in their work, and attract them to take root in Fanhua and serve for Fanhua as well as elevate a sense of responsibility, sense of entrepreneurship and sense of innovation. Since we made the announcement, the plan has not only received highly enthusiastic reaction from our employees and entrepreneurial team leaders but also attracted lots of attention from the industry. We are pleased with the effect it has achieved so far.

Chunlin Wang - Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu - Fanhua Inc. - IR Manager

Secondly, the progress in service network expansion, in the second quarter 2018, we continue to focus on enhancing our sales capability and further expanding our market presence in new regions. We added 39 new sub-branches, increasing the total number of our life insurance sales outlets up to 580.

Chunlin Wang - Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu - Fanhua Inc. - IR Manager

Thirdly, the development of our online platform, and firstly CNpad, our auto insurance platform business, which is built upon CNpad, has maintained steady growth. As of June 30, 2018, CNpad auto app has gathered an aggregate of over 464,000 registered users, up 57.8% year-over-year. Total insurance premiums transacted via CNpad auto app was approximately RMB 580 million, which was flattish quarter-over-quarter.

Chunlin Wang - Fanhua Inc. - Chairman & CEO

(foreign language)

Oasis Qiu - Fanhua Inc. - IR Manager

Secondly, Baowang. Baowang maintained strong growth in the second quarter of 2018. The number of its registered users exceeded 1.8 million, up 75.3% year-over-year and its active users reached 89,600, up by 96.8% year-over-year. Insurance premiums hit RMB 560 million, representing an increase of over 11x year-over-year, but a decrease on a quarter-over-quarter basis. The sequential decline was mainly due to the suspension of corporation with one of our partners in June, which is a third-party online lending platform, as the underwriter decided to cut back underwriting business for such kind of platforms in view of the recent tightened financial regulatory oversight. We do not have specific time line for resuming the corporation at this stage.



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Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

As for eHuzhu, it has been in operation for 4 years, gathering over 3 million effective paying members as of June 31, 2018. It has helped more than 1,000 families with RMB 115 million funding raised through the platform. On May 30, 2018, eHuzhu launched an online fund raising platform for those contracted with serious disease, named "Yiqizhu" (foreign language) allowing broader group of Chinese families access to alternative solutions. As of day, there were 106 cases which have sought help through the platform and raised over 1.9 million fund (inaudible) in total.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

Apart from the operational progress, I am proud to share with you the news that we have won a number of awards during the second quarter, which fully demonstrates our brand recognition and growing market influence.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

Firstly, Fanhua was listed again as one of the Top 20 Global Insurance Brokers by A. M. Best in July 2018, and it has been on the list for 4 consecutive years.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

In July 2018, Mr. Lichong Liu, President of Fanhua Insurance Sales Service Group Company Limited, our wholly owned operating entity in China, was presented the Insurance Master Golden Award in the Third International Insurance Festival and 2017 Insurance Master Award Ceremony.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

In June 2018, in recognition of its outstanding and steady performance, in 2017, Baoxian.com was awarded the Internet Insurance Platform of the Year 2017 at the Third China Internet Insurance Conference. Its President, Mrs. Dan Wei, was named The Person of the Year 2017 at the event.

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Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

Last but not least, dividend declarations. Based on the solid result of the second quarter 2018, our Board of Directors declare a quarterly dividend of USD 0.25 per ADS to shareholders of record on September 5, 2018, payable around September 19, 2018.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

In the last part, I would like to share with you our view on the business outlook in the second half 2018. As statistics show, the performance of the overall life insurance market in China was largely in line with our predictions made earlier this year. As we had expected, most life insurers have been actively adjusting their business structure with much higher proportion of protection-oriented products in their total business mix. The rising demand of the expanding middle-class in China for life insurance products has become and will continue to be a key catalyst to drive the sustainable growth of the life insurance market in China.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

As for Fanhua, despite the regulatory restrictions on short-term and fast return savings or rented life insurance products and the potential negative growth in the Chinese life insurance industry, we remain confident to achieve positive growth in annualized life insurance premiums in 2018. Now we believe the fast growth in renewal business will continue, which will become an increasingly more important source to our profit growth. And this allow us to raise our full year guidance for operating income from 40% to no less than 50% year-over-year.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

Looking ahead to the third quarter of 2018. In view of the extremely high base in the third quarter of 2017, owing to the swell of fast return annuity and endowment insurance products, our annualized life insurance premiums may decrease slightly year-over-year. However, we are still confident that we will be able to achieve no less than RMB 100 million in operating income in the third quarter of 2018, based on the expected positive growth in health insurance business and continue fast growth in renewal business during the quarter.



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Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

Thank you. Now the management will open the floor for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from the line of Arthur Hall from Arthur Incorporated.

Arthur Hall

Since health insurance is such an important part of your business, could you give more information on the type of insurance? Is there a death benefit in the insurance? What's the duration of the insurance and the renewal rates? And the approximate operating margin on the health insurance?

Oasis Qiu - *Fanhua Inc. - IR Manager*

(foreign language)

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

(foreign language)

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

The type of health insurance product that we sell are mainly critical illness products and the duration is mainly in the range of, like, mostly 20 years. And the gross margins for the first year commission is about 26%. And the gross margin for the renewals commission is about 60%. So the average, the combined average is about 30%.

Operator

Your next question comes from the line of Dan Tian CICC.

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

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

There are 2 questions from Dan Tian. And the first question is that our first year premiums and renewal premiums grew by 70% year-over-year, while the revenues for our life insurance products only grew by 37%. And the gross profits from life insurance business also only increased by 19%. He is wondering what's the reason that the revenues growth was outpaced by premium growth? And the second question is about the progress of our 521 Development Plan?

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

Our first year premiums for life insurance products grew by 41.4%, and the renewal premiums grew by 109%. So the combined total life insurance premiums increased by 69%, roughly 70%. And for the renewal business the commission rate is about 17% on average. And the commission rate for the first year products -- first year premiums is about 122%. So I think one of the reasons that our revenue growth was lower than the premium growth.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

And the reason that the gross margins growth was lower than the premium growth was because we recognized a performance bonus, head-quarter-to-head quarter performance bonus of RMB 30 million, which increased the gross profit for our life insurance business last year -- the same period last year.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

And the performance bonus was basically calculated on the combined sales volumes of our sales agents. And the payment of such kind of performance bonus was not in -- was based on fixed timing. So last year, the performance bonus was recognized in the second quarter, and for this year, it's possible that we may have similar kind of performance bonus in third quarter.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)



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Oasis Qiu - *Fanhua Inc. - IR Manager*

Since we announced the plan to the capital markets and all members of the company on June 14, we organized a meeting attended by all the head and deputies of our agency subsidiaries and branches to give full account of all the details about the 521 Development Plan and to kick start the subscription process. As of date, the number of applicants for participating in the plan has exceeded 2,300 persons. We expect the whole transaction to be completed by year-end.

Operator

(Operator Instructions) Your next question comes from the line of [Leon Liu] from (inaudible) Management.

Unidentified Analyst

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

There are 2 questions. The first question is regarding our next quarter guidance. While the guidance that we provided for the next quarter is slightly lower than the second quarter, he is wondering what's the reason? Is it because we expect the business growth will slow down? Or is it because there will be change in business mix? And the second question is about management's view -- what's the management's view about the growth outlook for next year?

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

So last year, actually, we have created a record high sales because of the product ban on the fast return type of annuity and universal products in October 2017. So based on this high base, we expect that this is possible that our first year premiums may decline year-over-year. And that is the base that we predict our profit guidance. And as for the business structure, we believe that it will remain more or less the same, whereas the health insurance still be the major product.

Unidentified Analyst

(foreign language)

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

It was because we do expect that the premium volume may also be lower than the second quarter.



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Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

We do expect that our business and profits will bounce back up in the fourth quarter. So basically the seasonality in this year will be quite a stark contrast to that in 2017.

Chunlin Wang - *Fanhua Inc. - Chairman & CEO*

(foreign language)

Oasis Qiu - *Fanhua Inc. - IR Manager*

As for the outlook for 2019. Firstly for 2018, as we had mentioned in the prepared remarks that we are confident to achieve positive growth in first year premiums and increase our operating profit guidance from 40% to 50%. But for the industry, we do think that it will be a year of correction, a year of adjustment, for the industry in 2018. And -- however, after the adjustment in 2018, we think that the industry will resume rapid growth in 2019 and after. We remain confident about the growth outlook for 2019.

Operator

There are no further questions at this time. Presenters, please continue.

Oasis Qiu - *Fanhua Inc. - IR Manager*

Thank you for participating in our conference call. If you have any further questions, please feel free to contact us. Thank you.

Operator

Ladies and gentlemen, this concludes our conference for today. Thank you for participating. You may all disconnect.

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