Fanhua Q4 2018 Earnings Conference Call Script

Operator:

Thank you for standing by for Fanhua's Fourth Quarter and Fiscal Year 2018 earnings conference call. At this time, all participants are in listen-only mode. All lines have been placed on mute to prevent background noise. After the management's prepared remarks, there will be a question-and-answer session. Please follow the instructions given at that time if you would like to ask a question. For your information, this conference call is now being broadcasted live over the internet. Webcast replay will be available within three hours after the conference is finished. Please visit Fanhua's IR website at ir.fanhuaholdings.com under the "Events & Webcasts" 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 officer.

Oasis Qiu: Good Morning. Welcome to our Fourth Quarter and Fiscal Year 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 US 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 are not limited to those outlined in our filings with the Securities and Exchange Commission, 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 Li. Mr. Wang will provide a review of our financial and operational highlights in the fourth quarter and fiscal year 2018. He, Mr. Ge and Ms. Li will take your questions after the prepared remarks. Now I will turn the call over to Mr. Wang.

CEO Wang Chunlin (Translated): 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 Ms. Lily Li. We will begin today's call by reviewing our fourth quarter and fiscal year 2018 financial results. Then I will share some of the operational highlights in 2018, followed by a brief discussion of our business outlook for 2019. There will be a Q&A session after the report.

1. Review of Fourth Quarter and Fiscal Year 2018 Financial and Operational Results

As the Circular No. 134 issued by the CIRC in 2017 continued to exert its impact in 2018, and against the backdrop of tightened regulation focusing on steering the China's life insurance industry back to its fundamental function of providing protection to the society, we report a solid set of key operating metrics which beat our prior expectations.

Our annualized insurance premiums ("APE") on regular life insurance products reached RMB1.9 billion in 2018, up 3.8% from a year ago while renewal insurance premiums registered a growth of 119.3% year-over-year to RMB3.7 billion, leading to a total of RMB6.2 billion life insurance premiums, representing a growth of 46.2% year-over-year.

Our operating income grew 55.9% year-over-year to RMB425.7 million in 2018, with net income growing 35.8% year-over-year to RMB609.9 million and earnings per American Depositary Shares ("ADS") up 34.8% year-over-year to US$1.43. We distributed cash dividend of US$1.00 per ADS in 2018, representing a dividend payout ratio of 69.9%.

In the fourth quarter of 2018, we had stellar growth of 80.9% year-over-year in total insurance premiums to RMB 1.7 billion, of which annualized premiums equivalent on regular life insurance products grew by 37.7% to RMB467.9 million and renewal insurance premiums were RMB1.1 billion, up 100.4% year-over-year.

We wrapped up the year with strong note in the fourth quarter of 2018, with an operating income increasing by 34.3% from a year ago to RMB83.4 million.

2. Key operational highlights in 2018

Fanhua made steady progress on expanding our sales force to one million while many insurance companies face increasing difficulty to recruit and retain agents. As of December 31, 2018, we added over 300,000 sales agents from a year ago and the total number of our sales agents hit over 800,000. It shows that separation of product design and distribution is an inevitable trend and Fanhua is the best choice embrace such trend. We firmly believe that we will be able to reach our target of one million sales agents by 2019.

In 2018, all of our provincial subsidiaries or branches which have been operating for more than a year have become profitable. In addition, except for eHuzhu which is essential a public charity platform, all of our other online platforms have also achieved profitability.

In 2018, of all of our provincial branches or subsidiaries, there are five which can each generate more than RMB100 million annual annualized life insurance premiums, ten which can each generate more than RMB50 million annualized life insurance premiums and all of them can each generate more than RMB10 million annualized life insurance premiums equivalent. These are strong testaments of the robust operation and development of our subsidiaries and branches.

2018, we made some solid achievements in sales network development. As of December 31, 2018, we added 180 new sales outlets to a total of 682.

Baoxian.com generated RMB1.3 billion insurance premiums, up 80% from a year ago, with approximately RMB10.0 million operating profit. It has become a leading internet insurance service provider in China.

In 2018, eHuzhu continued to pursue steady and healthy development. As of December 31, 2018, it has added 800,000 new registered members and the number of effective members reached 3.4 million. Since its inception, it has raised RMB314 million funds and helped more than 1,840 families. It has won wide recognition from its members and become a good tool to promote Fanhua's brand image.

In 2018, Lan Zhanggui has gathered more than 807,000 registered users including approximately 150,000 users who have sold at least one life insurance policy through the platform during the year, generating a total of RMB2.3 billion new life insurance premiums. Meanwhile, we continued to improve the digital tool's user experience by adding and optimizing its key industry-leading features, especially the features related to agent recruitment, insurance proposal, tracking and notification, online training and training courses development, honor system building and event announcement etc.

In 2018, Fanhua has welcomed more than 20 new managers and 35 senior executives in the group and our operating subsidiaries/branches who are the backbones that help significantly strengthen the Company's management and operation capabilities during the year.

Our achievements have won the recognition of the media, our clients and the general public. Fanhua and our subsidiaries were honored with several awards during 2018, including Outstanding Brand of the Year 2017 awarded to Fanhua Inc., China Leadership and Outstanding Insurance Intermediary of Year 2018 and The Best Insurance Intermediary Brand of the Year 2018 in the 13th China Insurance Innovation Awards granted to our wholly subsidiary Fanhua Insurance Sales and Services Group Limited, the Internet Insurance Platform of the Year 2017 won by Baoxian.com, and Internet Enterprise Social Responsibility Award won by eHuzhu.

In addition, one case handled by our subsidiary Fanhua Insurance Claims & Loss Adjustors Co., Ltd related to loss assessment for a catastrophic flood-stricken aluminum manufacturer was named among the Top Ten Leading Examples of Risk Management in China in 2017.

We are also honored to rank 46th among Fortunes' Top 100 Fastest Growing Companies and were included in MSCI China Small Cap Index. We were ranked among the top 20 global insurance brokers in 2017, according to A.M. Best. We been in the list for four consecutive years.

3. Outlook in the first quarter and fiscal year 2019

Looking ahead to 2019, as the complex international geopolitical landscape adds to uncertainty in macroeconomic environment in China and abroad, the China Banking and Insurance Regulatory Commission will inevitably focus on the theme of strict regulatory supervision and risk control in 2019. However, we are convinced that we are on track towards a continued growth, benefiting from a rapidly expanding middle class in China and accelerated trend of division of manufacturing from distribution, and based on Fanhua's scalable platform, rapidly expanding sales force, nationwide footprint and large customer base built over the past 21 years.

As such, we expect our APE on regular life insurance products to increase by 30% year-over-year and operating income by 40% year-over-year in the first quarter of 2019.

For 2019, we expect APE on life insurance products to increase by 30% year-over-year to RMB2.5 billion, renewal insurance premiums to grow by 50% year-over-year to RMB5.6 billion, and operating income to grow by 40% to RMB600 million.

Non-operating income and share of income of affiliate may decline in 2019, primarily because : 1) investment income is expected to drop mainly due to a decrease in cash reserve as a result of the Company's increasing spending on share buyback and dividends and the loans related to the Company's 521 development plan; 2) the interests derived from the loans related to the Company's 521 development plan won't be recognized as interest income in the Company's income statements and instead will be recorded as additional paid-in capital when received according to relevant rules under the US GAPP; and 3) CNFinance Holdings Ltd, in which Fanhua owns 18.5% equity interests, intends to upgrade its business model from heavy-asset model to light-asset platform model which may impact its profit in 2019.

As a result of the aforementioned factors, we expect a slight increase in net income attributable to shareholders in 2019 on a year-on-year basis. However, as the shares related to the 521 development plan will be treated as treasury shares which won't be included in the shares used for calculating basic earnings per share, according to relevant rules under the US GAPP, we anticipate the growth of our basic earnings per share will be no less than 10%.

At the board meeting held on March 8, 2019 at the Company's headquarter, our Board of directors passed the below resolutions:

Firstly, the board approved to increase the Company's annual dividend by 20% from US$1.0 per ADS in 2018 to US$1.2 per ADS in 2019, which will be paid on a quarterly basis. Management believe that

1) Our strong cash reserve of RMB2.3 billion as of year-end of 2018 should be sufficient to support our need for future business development since we currently primarily rely on organic growth to expand our business;
2) The long term regular life insurance business that Fanhua focuses on has high embedded value and cash value, which will provide a strong base for sustainable cash generation in the long run.
3) Our cash dividend is determined based on the Company's operating cash flow to make sure that dividend distribution won't eat into the Company's existing cash reserve.

Secondly, the Board approved a share repurchase program, authorizing the management to execute the repurchase of up to US$200 million of the Company's ADSs by December 31, 2019, in any form that the management may think appropriate.

To our dearest shareholders and all of our friends who are concerned about us, I would like to take this opportunity to solemnly announce that:

The era of separation of production and distribution in the China's life insurance industry has arrived, which will present a once-in-a-lifetime golden opportunity to Fanhua and Fanhua' employees and sales teams!

Fanhua Model is the right direction in which all Fanhua employees and sales teams should forge ahead as one! Fanhua's 521 development plan will be the core engine to drive us make big stride by leaps and bounds!

We believe that with snowballing profit growth and continued increase in dividends, the Company will be able to build trust and win support from our shareholders.

I firmly belive that the aspiration to become a company that can generate hundreds of billions of insurance premiums won't be just a dream!

To achieve these targets, we Fanhua people are dedicated to fulfilling our mission and sparing no efforts to pursuit continued development! With all of our sales force under my command, whatever may come, being a difficulty or a challenge, we are not afraid and we will work as one to tackle all of the obstacles to achieve our goals!

I love Fanhua!

Thank you.

Q&A:

1. CICC: Fanhua announced a big increase in annual dividend from US$1.0 per ADS in 2018 to US$1.2 per ADS in 2019. Given that the paid-out ratio was already quite high in 2018, will the increase in dividend in 2019 put any pressure on the Company's operating cashflow and adversely impact the Company's operation?

   Chunlin Wang: Our dividend payout ratio was approximately 69% of the Company's net income attributable to shareholders in 2018. After deducting the impact of 521 development plan (dividends payable to 521 development participants will be used to payback interests related to the loans), even though we increase annual dividends by 20% in 2019, we expect the cash outflow related to dividend payments will be similar to that in 2018.

   We expect our operating income to grow by 40% year-over-year in 2019 which will be strong base to support our dividend distribution. Secondly, we had RMB2.3 billion cash and cash equivalents and short term investments. As we have no major M&A plan in the near term and we currently primarily rely on organic growth to expand our business. We believe our current cash reserve should be sufficient to drive our long term business development. Separately, the long term life insurance business that we are specialized at and focus on has high embedded value and high cash value which will enable us to generate sustainable cash flow, and therefore our dividend policy won't eat into the Company's cash reserve.

2. CICC: The Company expect to grow APE (annualized premiums equivalent) by 30% in 2019. What are the drivers behind the growth? Is it because the no. of agents will continue to increase or Company expect to establish partnership with more insurance companies? And how is the Company's year-opening sales so far?

We started distributing life insurance products in 2005. Since then, we have put a lot of focuses on strengthening business quality, improving our technologic capabilities and service quality as well as accumulating talents. That is why when the life insurance industry took off in 2015, we were able to grow faster than the industry and the independent insurance intermediary sector.

Therefore, despite the tightening regulation in the China's life insurance industry in the past two years, we are able to benefit from the expanding middle class in China and accelerated trend of the separation of manufacturing and distribution in the life insurance market in China. We believe we are well positioned to achieve positive growth amid challenging market environment and achieve rapid growth that outpaced the industry when the industry picks up growth momentum.

3. Hallco: Congratulations on a very good quarter and your statement of your vision. My question is related to your underwriters. Can you list your top 3-4 major insurance underwriters and what percentage do you expect them to do in 2019?

We have maintained very good relationship with all of our insurance company partners. But of course we will adjust priority in terms of the cooperation with different insurance underwriters depending on their product offerings, service capability and terms related to commissions. Currently, our top three insurance underwriters are Huaxia, Tian'an and Aeon. Our insurance company partners structure is getting more diversified and broad. We have also maintained active partnership with more than 10 other insurance companies. In 2019, we expect more and more insurance companies, especially small and medium size companies, will have more strong political will to partner with independent insurance intermediaries and as a result we do expect the shares of Huaxia and Tian'an to come down as a total percentage of our life insurance business mix.