

NOAH HOLDINGS 3Q 2018 EARNINGS CALL EDITED TRANSCRIPT

Nov 19, 2018, 8:00 PM (US EST)

OPERATOR

Good day, ladies and gentlemen. Welcome to Noah Holdings Limited Third Quarter 2018 Financial Results Conference Call. At this time all participants are in listen-only mode. Following management's prepared remarks, there will be a Q&A session. During the Q&A session we ask that you please limit yourselves to two questions and one follow-up. If you would like to ask additional questions, you may re-enter the queue to do so. As a reminder, this conference is being recorded. After the close of the US market on Monday, Noah issued a press release announcing its Third Quarter 2018 Financial Results which is available on the company's IR website at <http://ir.noahgroup.com>. This call is also being webcast live and will be available for replay purposes on the company's website.

I would like to call your attention to the Safe Harbor statements in connection with today's call. The company will make forward-looking statements including those with respect to expected future operating results and expansion of its business. Please refer to the risk factors inherent in the company's business and that have been filed with the SEC. Actual results may be materially different from any forward-looking statements the company makes today. Noah Holdings Limited does not undertake any obligation to update any forward-looking statement as a result of new information, future events or otherwise except as required under the applicable law. The results announced today are unaudited and subject to adjustments in connection with the completion of the company's audit. Additionally, certain non-GAAP measures will be used in our financial discussion. A reconciliation of GAAP and non-GAAP financial results can be found in the earnings press release posted on the company's website.

With that, I would now like to hand the call over to Kenny Lam, Noah's Group President.

[Kenny Lam – Noah Holdings Limited Group President]

Thank you, Operator. I want to welcome all our investor and analyst friends to our earnings conference call today. In addition to myself, Ms. Wang Jingbo, Chairlady and CEO of Noah, our CFO Shang, will also be participating in our call.

For today's agenda, I will first briefly summarize Noah's overall performance for the first three quarters of 2018 as well as the development of our core wealth management and asset management businesses. Chairlady Wang will then provide her current views on the overall market, regulatory environment, and company product strategies. Our CFO Shang will then follow with a detailed discussion of Noah's third quarter financial performance. We will conclude the call with questions and answer session.

As we entered into the second half of 2018, market sentiments remained volatile. Amidst trade disputes, stringent financial regulatory reforms and deleveraging, investment appetite has been substantially reduced. Despite some clear policy signals including tax cuts, encouragement of private enterprise development, and continued open-door policies, market confidence is still very fragile.

During this transitional period, many Chinese companies are undergoing brutal tests of the market. This is true also for China's wealth and asset management industries. As a leading firm, Noah continues to focus on providing high-quality services and creating value for our clients, while improving our risk management and other core competencies, maintaining sustainable growth and preparing for challenges we might face.

In the first three quarters of 2018, the Company's business grew steadily and performed well across the board. In the third quarter, Non-GAAP net income to our shareholders was up 41% year over year to RMB294 million and up 19% year over year to RMB802 million for the first three quarters of 2018. The Group's net revenues for the first three quarters was RMB2.5 billion, up 17% year over year. In the wealth management segment, we raised RMB84.9 billion in financial products, while the transaction value for the third quarter was up 19% year over year. AUM of our asset management business at the end of the third quarter reached RMB164.1 billion, showing a growth of 15% year over year. We are very pleased to have achieved such financial performance in a challenging environment.

In the wealth management business, demand for professional wealth management services in China is still strong. Recruiting suitable talents and fostering steady development are particularly important during this period. As of the end of the third quarter 2018, our frontline team covered 83 cities across the country, and the number of relationship managers increased 21% year over year to 1,559. In order to grow with our clients, and further enhance our ability to provide comprehensive services to them, Noah continues to host in-depth investor education events in 2018.

Since the beginning of this year, we have held hundreds of events such as Noah company visit, small investment sessions, and in-depth one-on-one client meetings. For ultra-high-net-worth clients, we provide more customized services and activities such as closed sessions with senior management, tailor-made trust planning services, and private events for our "black card" clients. Through detailed analysis of client profiles and our relationship with "black card" clients could truly be driven by comprehensive services rather than pure financial product sales.

For existing clients, we have focused heavily on the improvement of our post-investment services. Periodic fund performance reports have been comprehensively systemized and templated, and are now more concise and easier for clients to read and retrieve online. Fund updates and other information can now be communicated with clients via voice through our APP for relationship managers, adding an enhanced human touch.

We further integrated our client service resources into a new client operation center in 2018. In addition to the existing customer service hotline, we added AI-supported client service assistants, and also actively reached out to existing clients to better understand their needs. During the past five months, the client operation center has hosted 59 LP conferences for both Gopher and externally-managed funds. We believe that these initiatives will help our relationship managers provide more professional post-investment services to their clients in a planned and organized

manner.

Furthermore, the research work of the revamped Noah Research Team has become a lot more systematic and professional. In the first three quarters, our Research Team have provided 165 training sessions for our frontline professionals, covering 42 fund managers in different asset classes. They have also published 422 internal and external research reports, and conducted 83 interviews with domestic and international media. A substantial number of media and online platforms have cited our research results, and the brand reputation and market influence of Noah Research have been firmly established. Active users of the Noah Research on-line channel has increased by more than 5-fold in the last 6 months.

Our asset management business is also growing healthily in 2018. As of the end of the third quarter, Gopher's total assets under management reached RMB164.1 billion, increasing 15% year over year. Breaking down by asset classes, the AUM of our private equity investments increased by 19% year over year to reach RMB96.9 billion, accounting for 59% of the total assets under management. The AUM of our credit, real estate, secondary market equity, and discretionary investments respectively accounted for 25%, 10%, 3% and 3% of our total assets under management.

With the demands of China's high-net-worth clients becoming more specialized and institutionalized, Gopher continued to enhance its investment capabilities, both in breadth and depth. The demand from institutional investors has also been rising along with the development of China's asset management industry. Gopher recently won the bid as the manager of an RMB1 billion angel fund invested by the government of Xiangjiang New District of Hunan province. It is an important recognition of our fund management experience.

As a leading alternative asset manager in the industry, Gopher has established a standardized process for online operations, covering the entire process of "fundraising – investing – management – redemption." Gopher has comprehensively sorted and integrated its investment management system. Through a visualized display interface, the system can display panoramic views of our historical investment database, including dozens of our funds-of-funds, hundreds of invested-funds, and thousands of portfolio companies. We are also striving to fully exploit the value of data resources. These initiatives to further integrate resources of capital, technology, operation, and back-office support will provide a stronger foundation for Gopher's growth.

For our overseas business, in 2018, as high-net-worth clients become more active in global asset allocation, Noah's globalization strategy continues to move forward steadily. Our offices in Hong Kong, the U.S, Canada, Australia, and Singapore are providing more diversified product and service for clients. As of the end of the third quarter, Gopher's overseas assets under management reached RMB23.7 billion, increasing 20% on a yearly basis.

As we continue to expand our global business, we are also attracting overseas investors who are interested in China. At the end of October, the "China-Australia Family Office Alliance", was created. In the alliance, Noah joins hands with six of Australia's top family offices to open up investment channels for family offices in the two countries and brings more cooperation opportunities and experience sharing in wealth management and estate planning.

Lastly, I would like to share some of our Group's progress in technology and operations. Recently, our intelligent customer service robots have been launched on our official website,

WeChat public account, and Noah online APP. Questions and issues in eight major categories including the Group's introduction, products and services, and daily conversations can all be resolved by AI. As of the end of September, intelligent robots have answered nearly 6,000 customer questions.

Our one-stop Noah account system has been continuously improved. Audio and visual recording of client order information, contract signing, and product status updates have all been launched online, and product information can now be delivered to customers more timely and accurately. We believe that embracing technology will further help Noah's client service capability.

2018 is a year of change, and it puts higher demands on our company's operations management and risk control. But this is not the first time Noah has faced harsh market conditions. We believe that the short-term market fluctuations caused by external sentiments actually give rise to more opportunities and long-term returns. We will continue to adhere to our strategy of building our core competencies, maintaining compliant and sustainable management, and focusing on our own growth in an uncertain market environment.

With that, I will now turn the call to Noah's Chairlady and CEO, Wang Jingbo. She will speak in Chinese, and her remarks will be followed by English interpretation.

[Jingbo Wang – Noah Holdings Co-founder, Chairlady & CEO]

Jingbo Wang: (Speaking Chinese).

(Translated). Thank you, Kenny. (Speaking Chinese).

(Translated). In the third quarter of 2018, from a macro perspective, the market sentiment in China reached a low point. The impact of domestic deleveraging exceeded expectations; the downward pressure on China's economy increased; and A-shares index continued to sink. Moreover, the Sino-US trade war was in a stalemate, and the market generally believed that we would need to prepare for the long haul.

That being said, from a micro perspective on the enterprise operations, Noah's senior management team has already completed the adjustments to both business strategy and our own mentality. We believe that macro pressure is a reality of the market that we must face and tackle. It is at the micro level of operations where we can take actions and make a difference. Thanks to the experience gained through our past track record with conservative approach, coupled with our respect for industry common sense, such a critical point in 2018 is not daunting to us. We believe as long as Noah can maintain our strategic strengths, the opportunities actually outweigh challenges.

We still strongly believe that both wealth management and asset management are emerging industries in China. The implementation of the New Asset Management Regulations and the recent exposures of risks will clear out the lower-quality participants in the market and provide real-life education for investors. The correct concepts of long-term investing and asset allocation are being accepted by more and more clients. All these are beneficial to the long-term development of the industry.

From our growth data in the third quarter, we can see that increased comprehensive services coupled with global asset allocation for high-net-worth clients, as well as the combination of wealth management and asset management in business model has reduced the impact of industry cycle volatility, and allow our company to develop in a healthier and steadier manner.

Jingbo Wang: (Speaking Chinese).

(Translated). Next, I would like to share with you a detailed overview of the major service and product categories of Noah and Gopher.

With the current risk exposures in the market, the demand from clients for asset allocation services has increased significantly. For our ultra-high-net-worth clients, the demand for comprehensive services is even more prominent. Insurance products, trust planning, and other low-correlation assets were strong in demand, and Noah's revenues from such products and services increased by 197% year-over-year in the third quarter.

Noah's core strategy this year is to continuously upgrade our core customer service system, providing high-quality services to black card and family office clients. As of the end of the third quarter, we had more than 700 black card clients, whose total assets with Noah have exceeded RMB60 billion.

Gopher's family office services have also been recognized by many ultra-high-net-worth clients. In the first three quarters of 2018, the AUM of Gopher's discretionary and family office investments grew by 50% from the end of last year. We believe that this sector will become a new driver for Noah's future growth; Of course it will also put higher pressure and demand for our comprehensive service capabilities.

During the third quarter of 2018, in the primary market, the fundraising side remained sluggish, while the investment side gradually improved. Bubbles and risk levels have been reduced both in terms of valuation and company quality. Some projects that Gopher had co-invested in during the past few years have begun to seek overseas listings, and we are confident that this will help us to provide increasing performance-based income to our clients and shareholders in the future.

Although the scale of PE fundraising for Noah kept declining in the third quarter, Gopher's assets under management in private equity still maintained a year-over-year growth of nearly 20% to reach RMB96.9 billion, accounting for 59% of the total AUM. We have learned from past experience that often during periods when fundraising is difficult, it is the best time to invest. Our strategy remains to work closely with leading fund managers to keep the number of funds offered stable, and to take small but consistent steps to continue moving forward.

In the third quarter, we raised capital for and invested in the newest funds from Shunwei, Innovation Works, Jingwei and several other top fund managers in China. At the same time, we strengthened cooperation in co-investments and direct investments with leading fund managers. Gopher's direct investment capabilities and its team construction have always been a major direction of our efforts. The strategy of secondary fund is also a main focus of us, as the demand from institutional clients has been obviously increasing.

Jingbo Wang: (Speaking Chinese).

(Translated). In terms of real estate funds, we have optimized our investment strategy and risk

management process. Strategy-wise, we continue to promote preferred shares portfolio funds and core & value-added acquisition funds, focusing on equity investment and cooperating with core real estate developers. At the end of the third quarter of 2018, the AUM of Gopher's real estate investments had increased by 43% year-over-year to RMB16.6 billion. At the same time, several new real estate funds have finished filing, and are either being or will be launched.

Gopher's real estate asset acquisition team has also been actively working, with the goal to acquire core properties in core cities during the economic downturn; Our real estate operations team has been gaining valuable experience in terms of property operations.

It is also worth mentioning that the U.S. real estate fund managed by Gopher's New York real estate team has also been officially launched and completed the investment in its first project. As of the end of the third quarter, most of the real estate funds managed by Gopher were equity investment funds and property-holding funds.

On the secondary market products front, affected by the market downturn, the scale of funds raised in the third quarter decreased significantly to around RMB1.5 billion. That being said, we believe that the current market valuation is in a reasonable investment range; Increasing allocation in outperforming fund manager should be the core strategy now. Recently, we have launched a value investment fund with a three-year lock-up period, and it has already garnered recognition from high-net-worth clients.

In terms of Gopher's secondary market funds performance, Gopher's quantitative strategy and market-neutral strategy fund-of-funds' performance is eye-catching in this market, both generating more than 5% in positive returns since the beginning of the year. Gopher's flagship FOF and MOM funds have also significantly outperformed the CSI 300 Index by 12 and 7 percentage points respectively in the first three quarters.

We are well aware that fixed-income funds and interest-bearing assets remain in high demand from high-net-worth clients. Since 2015, Noah has actively promoted portfolio investment and net-asset-value management for our fixed-income funds. We have adhered to the diversification of underlying assets and selective engagement with quality counterparties, only market-leading licensees, and enhancement of risk management with our proprietary risk control system. These measures together with other long-term inputs have enabled us to maintain a sound level of asset quality and risk control amid a somewhat chaotic 2018 for the greater market. In the third quarter, the fundraising volume of Noah's fixed-income products reached RMB22.8 billion, accounting for 81% of our transaction value.

Jingbo Wang: (Speaking Chinese).

(Translated). Lastly, I would like to briefly talk about our view on recent regulatory actions and on macro-economy. The New Asset Management Regulations is navigating the domestic industry development to correct supervisory deficiencies, manage market irregularities, and prevent systemic risks. High leverage is indeed the Sword of Damocles hanging over the Chinese economy, and deleveraging is very much necessary.

However, the deleveraging process needs to be carried out gradually and strategically, to prevent further harm to the Chinese economy in the future. Clearing out lower-quality industry participants and establishing a new market order is necessary for the long-term healthy development of the

asset management industry as well as for the country as a whole.

Although current economic conditions are weak, for enterprises, it is not necessarily a bad thing. This could also be a rare opportunity for us to re-examine our strategy, talent pool and resources, as well as to cut unnecessary costs, optimize our business model, and grow into a healthier enterprise. Now we are indeed facing such an opportunity, as the market demands us to build new capabilities to continuously improve and to convert the growing pains into the driving force for further development.

As Kazuo Inamori once said, the growth of bamboo can be used as a metaphor for the development of a corporate enterprise: when the economy is booming, the enterprise, just like a bamboo, often grows rapidly without forming nodes, thus eventually becoming weak and fragile. Bamboo only forms nodes that give it structural strength during times of less favorable conditions. Likewise, it is only when an enterprise experiences and overcomes various difficulties that it develops the foundational strength of its structure to enhance its overall corporate competitiveness and resilience. We believe this also applies to our industry and the country as a whole.

Noah Wealth Management was formed in 2003 and Noah Holdings was publicly listed in 2010. Today we stand as an enterprise with a 15-year operating history. Over the past 15 years, we have experienced four economic cycles and suffered from various risks such as investment fraud, industry cycle judgment errors, and credit defaults. This year, we have also witnessed some of the most accomplished, successful entrepreneurs being closed out the position of stock pledge and losing all their shares in the company. This has left an indelible impression on us.

For Noah, our senior management team has always been absolutely transparent in all communications, and facing both ourselves and the market honestly. Although we strive to “understand risks without experiencing them”, we believe that every mistake we made, if we learn from it, can make us stronger and wiser over time. With the passage of time and our own growing maturity, our fear, awe, and appreciation of common sense and respect for the power of the market are all only getting stronger. We strive to become a friend of time. That is our expectation.

Jingbo Wang: (Speaking Chinese).

(Translated). Thank you all. Now I will turn the call over to our CFO Shang, to review our financial results.

[Shang Chuang – CFO of Noah]

Thank you Chairlady and hello everyone.

As Kenny and Chairlady Wang both noted, we are satisfied with our financial results for the third quarter of 2018 and we are on track to deliver a solid result for the full year amidst the volatile environment this year.

Net revenues for the third quarter of 2018 were RMB839.0 million, an increase of 22.6% year-over-year, and Non-GAAP attributable net income in the same period was RMB293.9 million, up 40.5% year-over-year.

By revenue contribution, we achieved one-time commissions in the amount of RMB232.6 million, compared with RMB213.1 million in the same quarter last year, up 9.2% year-over-year as we continue to engage with our clients through diversified product and service offerings. Total transaction value of financial products we distributed during the quarter was RMB28.0 billion, an increase of 18.9% from a year ago. Our effective one-time commission rate for the third quarter was slightly increased from 0.81% to 0.83% quarter-over-quarter, down year over year due to changes in product mix.

Recurring service fees in the third quarter of 2018 were RMB478.6 million, up 39.0% from the same period last year, contributing to 56.7% of revenues. The growth of our accumulated distributed products and the high quality of our assets under management continue to provide strong revenue streams.

Total performance-based income for the third quarter of 2018 was RMB33.6 million compared to RMB74.8 million for the same period last year. We have realized performance-based income for 17 consecutive quarters, reflecting our ability to deliver investment returns to our clients through market cycles. It demonstrates our efforts to build a leading multi-strategy asset management platform with strong investment capabilities.

By segment, net revenues from the wealth management business contribute over 68% of total net revenues with RMB576.9 million and grew 18% year over year. Net revenues from the asset management business amounted to RMB198.5 million, up 20.7% year-over-year. Our other financial services segment continue to grow and achieved net revenues of RMB63.6 million, doubled year over year. We are especially pleased that our other financial service business breakeven point this quarter.

In the third quarter, operating income was RMB271.1 million, a 69.1% increase year-over-year. And the margin increased to 32.3% from 23.4% a year ago and 27.7% in 2Q2018, mainly thanks to our focus on cost management. In this quarter, our selling expenses was RMB81.2 million, slightly higher by 5.5% year over year and down 32.6% quarter to quarter as we completed most of our brand campaign in the first half of the year. General and administrative expenses was RMB60.0 million, flat year over year and decreased 12.4% quarter over quarter.

Non-GAAP net income for the third quarter was RMB293.9 million, a strong increase of 40.5% year-over-year. This quarter we adjusted for RMB35.7 million of share based compensation, RMB20.7 million of losses from unrealized fair value changes of equity securities and RMB29.9 million of gains from realized fair value changes of equity securities.

On the balance sheet side, as of September 30, 2018, the Company had RMB2.4 billion in cash and cash equivalents, improved from RMB2.1 billion in the previous quarter. The cash inflow of RMB449.8 million from operating activities in the third quarter was mainly due to the strong cash generation in our core business.

Finally, I would like to highlight that our performance year-to-date reflects strong fundamentals and steady profitability in our businesses. We remain confident in achieving our full year 2018 non-GAAP attributable net income guidance of RMB1.0 to RMB1.05 billion.

With that, let's open up the call for questions. Operator?

Questions and Answers

[Operator]

Thank you. We will now begin the question-and-answer session. (Operator Instructions).
Katherine Lei with JPMorgan.

[Katherine Lei – JPMorgan]

So when I look at the results, I think on the profit line, it is better than expected. However, I think [there are] two key points that we want to ask. Our first question is on WMP sales, because actually in the third quarter, sales volume continued to contract and mainly on the PE products and secondary market products, as well as the insurance [products]. So can I get a clarity on management guidance that where do you think the sales trends will be?

And also, I would like to ask, because PE product has been a flagship product of Noah; then going forward, do you think the trend will continue or you are developing some other brand-name products as well? So this is the first question.

The second question is actually also related to volume. It's on Gopher's AUM. Gopher's AUM only up 2% QOQ in the 3Q. So this one, what do you think will be the growth rate? And what do you think the mix of the AUM would be in the coming year? Okay. Thank you.

[Shang Chuang – CFO of Noah]

Katherine, on the second question, so Gopher's AUM mix, right?

[Katherine Lei – JPMorgan]

Yes, I think both questions actually, at end of the day, tied to the same theme, that investors believe that Noah has been very good at doing PE, no matter it's on the Gopher side or on the WMP side. However, people are thinking that maybe PE industry as a whole, its growth has plateaued at the stage.

Then for Noah, then what are you going to sell going forward, and what kind of products you're going to develop into the flagship product? That's something that people -- because now, when clients think about PE products, it's likely that the first name came to their mind would be Noah, but I think you may not be able to say the same thing for other products. So how are Noah going to face this challenge?

[Shang Chuang – CFO of Noah]

Yes, Katherine, I will take a crack at answering both of your questions, and will ask if Madam Wang and Kenny have anything to add further. So as Madam Wang mentioned earlier, since inception, we have actually been through four whole economic cycles in China. And our strategy and business model have always been to continue to strengthen our diversified product and service offering.

So since IPO actually, I recall back in 2012, 2013 period, actually the economic environment was also quite challenging, and the investment appetite for equity products as a whole, including

private equity and A-share market was quite weak. But we continue to engage with our clients through other products such as fixed income. And so the recent downturns in the investor appetite were not particularly worrying in the long term, because we still continue to see very robust wealth creation. And we think the demand for different large asset classes comes and goes.

So this year is likely to be a weaker year for private equity and a bit for public A-shares, but as the cycle continues to develop, it is most likely we're going to see a reverse in investor appetite, and then equity products will become more in favor.

So the important thing for us is that we continue to strengthen our product and investment capability across the large asset classes, and we feel quite satisfied both in terms of private equity, A-shares, real estate, fixed income, even for insurance. And now [in] a lot of complementary services such as trust planning, we have really cemented our expertise. And so that's on the wealth management side.

On the asset management side, you can see that in terms of our product mix, nearly 60% of our AUM comes from private equity. And so that really solidifies our leading position in private equity industry in China. These are very long-term products and the fact that we have been able to accumulate nearly 100 billion of AUM [in Private Equity] now shows that we have a very strong position going forward. And we continue not only to invest in leading funds such as those mentioned by Madam Wang such as Matrix, Shunwei, but we have also been, in the most recent year, adding our co-investment and direct investment capabilities.

[Kenny Lam – Group President of Noah]

Shang -- I'll add to what Shang said. Katherine, thanks for the questions. This is Kenny here. I think in the market indeed, Noah is known for private equity. But as you can see in this quarter's results, we've proved that clients are also coming to Noah platform for other things. So if you look at the release of the results, the value of the products distributed this quarter was actually up 18.9% year-over-year.

And if you look at the mix, as Shang said, it fluctuates between four different types. It fluctuates between fixed income, private equity, secondary market and other products. So I think it shows that our platform, while not perfect, is now beginning to attract clients for things other than private equity, and we're able to withstand the cyclical demand that may change from product to product. That's point number one.

Point number two, I think you mentioned insurance. I think we disclosed in our speeches that other services, which includes insurance, actually went up by 197% year-over-year. And so actually, demand for insurance products through our insurance brokerage platform has increased substantially. So again, it showed our efforts in recent years to be a lot more diversified in our revenue base and in our product base.

Okay. With that, I guess we'll go on to the next question.

[Operator]

Yuan Xue with CICC.

[Yuan Xue - CICC]

(Speaking Chinese).

[Kenny Lam – Group President of Noah]

Wait, wait -- Much better.

[Yuan Xue - CICC]

(Speaking Chinese).

[Kenny Lam – Group President of Noah]

So maybe I'll try to translate -- and then you can point out. So the two questions are similar to the first one. [The first question is] on the mix of the products we distributed, there is a much higher percentage in fixed income, and the question is what we expect going forward. The second question is on the other financial services segment, it is the first quarter of breaking even or actually [being] slightly profitable. So how does that come from? Shang, you want to --

[Shang Chuang – CFO of Noah]

Yes, sure. So on the growth in terms of the other financial services, most of the growth we saw this quarter came from our lending business. So we make loans to our registered clients, and the majority of these loans are backed by high-quality assets. Some of them are our financial products. And we continue to see short-term borrowing needs from our clients, and we continue to provide comprehensive product and service offerings to our clients and this is one example.

[Operator]

Edward Du with Deutsche Bank.

[Edward Du – Deutsche Bank]

Two questions -- my first question is that recently, we've seen many supporting policies in private sector financing, especially for the SMEs. And the regulator also mentioned that they encourage the private funds to participate in the funding support on the equity side or debt side, like bond or something. My question is about that. Do you see any further business opportunity in the SME financing in terms of Noah's position, or any benefit we can enjoy from the encouraging policies like the tax benefit or something else? This is my first question.

And my second question is for your micro-financing company -- you just mentioned it. May I know more about its current capital position, leverage, and do you have any further capital injection plan? And can you share more views on the business development for Rongyitong and any outlook for its loan balance and volume this year and next year? And above are my two questions.

[Shang Chuang – CFO of Noah]

Thank you, Edward. I'll provide a little bit more background on our lending services business. The

business was set up several -- a couple of years ago, and it was mainly targeting our registered clients. Currently, it has registered share capital of roughly around RMB350 million, and the business model is that it would securitize its loan receivables. And the basic process is forming quality assets and then through securitization, make a net fee and help service de-securitization.

We see loan -- we expect loan volume this year to double that of last year. It's going to probably reach somewhere around RMB10 billion this year, and most of the -- the average duration is less than one year. I mentioned earlier most of it would have high-quality collateral.

Going forward, we continue to see growth opportunities. And as part of our budgeting process for 2019, we are considering how best to allocate our resources across the various business lines. But I think we will look into increasing the capital base for our lending business to help further expand its business. But [for] exactly how much, I don't think we have a conclusion yet. I think it will be in line and on pace with the base of the business, as well as other capital needs of our other business lines.

And for your first question, I will -- Madam Wang would like to provide an answers to it.

[Jingbo Wang – Chairlady and CEO of Noah]

(Speaking Chinese).

(Translated). Okay. So two points that Madam Wang wanted to provide in terms of the first question regarding the latest regulatory policies. So most recently, we're seeing some improvement of operating environment from latest policy announcements. For our business in particular, we're seeing that registration of private funds improve. In the middle of this year, it was quite delayed, but we're seeing improvement in terms of the speed of registration.

Particularly -- the second point is in terms of providing new liquidity or financing to private enterprises where we are closely observing this development. But as of now, we expect that most of the capital to come from state-owned enterprises and large institutions. Possibly this is an opportunity for us if we can be the manager to this capital, and help them structure and allocate to mezzanine types of investments. But this is quite new, and we're closely monitoring and following up on potential business opportunities.

[Edward Du – Deutsche Bank]

Thank you.

[Operator]

Daphne Poon with Citi.

[Daphne Poon – Citi]

So my first question would be for the fixed income product sales. So we see the transaction volume has increased strongly this quarter. But then if we look at Gopher's fixed income AUM, it was down QOQ. So I'm just wondering what would be the mix of those fixed income product sales. Is it mainly driven by credit products or what would be the underlying asset mix?

And I guess second is just on the regulatory environment. So we see recently there has been lots of relaxation on different policies, including the new asset management rule or the registration of products. So for example, we are seeing relaxation on the bank WMPs side. So I would just like to hear your view. Do you think it's possible the government pull back on asset management tightening earlier this year? And do you see a potential loosening in the longer term? Just would like to hear your view on this. Thank you.

[Shang Chuang – CFO of Noah]

Just hold on for one second; we're translating the question. [For] your two questions, I will answer the first one. Madam Wang will answer the question regarding the regulatory developments and our expectation going forward.

In terms of the fixed income product that we distributed in the third quarter, most of it is still shorter-duration product. As in the third quarter, there was still quite a bit of volatility in the capital market, and so clients will continue to be nervous about making new investments on long-term decisions. But as we mentioned in the second quarter, we think that in a situation like that, it's still quite important to engage our client and maintain their capital with us. So we're quite nimble in terms of rolling out shorter-duration product which met clients' needs.

As these [products] are much shorter in duration, so it didn't help Gopher's credit AUM growth too much in the third quarter. But I think it's really a balance of trying to meet the clients' needs and our views on the overall long-term investment decisions of our clients, but I think we need to balance both.

In terms of the second question, I will ask Madam Wang to provide her thoughts on regulatory development.

[Jingbo Wang – Chairlady and CEO of Noah]

(Speaking Chinese).

(Translated). Yes, in terms of the regulation, I think earlier this year, what we saw with regulation was very stringent and tight. It almost felt like it was a complete pendulum swing to the other side, to the opposite side. Several years ago, there was little or lack of regulation in terms of new forms of financial services. And we saw, starting late last year and early this year, there was a lot of new regulations that came into play. But some of the regulation perhaps didn't cater to how the market was operating.

And so we're seeing some adjustments to the regulation to make sure that private enterprises who previously got financing are not completely cut off. So we're also seeing improvement in registering a private fund. So we see the recent month to be fine-tuning, rather than a reversal of regulation objectives. But we certainly feel that regulatory environment is slowly but surely getting better and better.

[Kenny Lam – Group President of Noah]

It's Kenny here. I want to emphasize two points. One is, I echo Chairlady Wang's and Shang's point that the core principles that were laid out in the new regulations on the asset management are not going to change. I think those core principles are very much assimilating to a global

standard that we like in this market.

The second point is regulator is actually learning to strike a balance in terms of its regulatory push. And so we're seeing that the balance is actually better struck in the last half or so. And that actually makes a player like us to understand that the regulators are actually improving. And we believe that it will still be relatively volatile in the months ahead, but is actually going in the right direction.

[Operator]

Analyst with JL Warren Capital.

[Analyst – JL Warren Capital]

I have two questions. The first question is about the lending business, about how do you recognize your interest income. What is your average interest rate, and are you lending to your existing high-net-worth clients or the corporate?

The second question about the selling expense. In the third quarter, your selling expense was recorded as 81 million in RMB, down from RMB120 million in the second quarter and RMB106 million in the first quarter. So what is the implication in the longer term? Thanks.

[Shang Chuang – CFO of Noah]

Thank you for the question and the translation. So I will answer both of the questions. On the first question regarding our lending business, as I mentioned earlier, we're providing short-term lending to our registered clients. That would include individuals as well as companies. The average interest rate is in the low-teens, and this reflects the high quality in terms of the borrower, as well as the high-quality collateral that we obtain when we make these loans.

In terms of the revenue recognition policy, the majority of the revenue is basically accrual of interest fee payable, or the net fees we're making when we're servicing those loans receivable that we have securitized out.

In terms of your second question on selling expenses, in the third quarter of this year, we had selling expenses of roughly about -- one second. We had selling expenses roughly about RMB80 million, which is flat year-over-year and down 32% from the second quarter. It was down from the second quarter because for the first half of the year, primarily in the second quarter, we spent most on our brand campaign. For the full year, we have budgeted roughly about RMB60 million to RMB80 to spend on strengthening our brand campaign and most of it was booked in the second quarter.

So that was the main reason why third quarter selling expenses came down, but we continue to be very focused on cost management. So versus a year ago, selling expense is flat. We don't expect any major brand campaign initiatives, at least for the next 12 months. But as I mentioned, we are in the process of doing our budgets for 2019. If there is any major investments or spending, we will keep the market updated in our next call.

[Operator]

George Cai with JPMorgan.

[George Cai – JPMorgan]

I have a few questions. The first one is on WMP transaction value. So do we have a guidance, a year-over-year growth guidance, for 2019 in terms of the WMP transaction value? So this is my first question.

My second question is on fee rate. So we continue to see the recurring fee rate improved in the third quarter. So we guess this is mainly due to the product mix, due to more sales of fixed income products. So besides that, are there any other reasons for the recurring -- or for the firm fee rate increase as well as the recurring fee? So this is my second question.

The third question is on Rongyitong. So we can see from the balance sheet that there's some receivable net balance around RMB680 million. Then just wanted to clarify -- you probably mentioned that loan [volume] could double to reach RMB10 billion this year. So just want to double-check with this number. And then we want to ask about the provision level and any potential default of the business. So this is my third question.

My last question is on the updates of Huishan.

[Shang Chuang – CFO of Noah]

Okay. Thank you, George, for your multiple questions. If you could give us a minute, we'll translate it to the management; one second.

Okay. So we will answer your questions in order I guess. So in terms of the transaction value for 2019 and going forward, I think we continue to want to improve the market share. I think we have been saying that for several years now. As you look at various industry reports, I think we're still seeing wealth management, asset management businesses growing at double-digits. So I think that will definitely be a goal of ours [in the] medium to long term, but the growth will not be linear growth, because obviously, we need to deal with the macro environment.

I would like to highlight that from the financial result we saw for the first three quarters of this year, I think our revenue growth is no longer just correlated to overall volume growth because we have been strengthening our investment capability, which helps us improve the revenue quality from our AUM.

So that taps into your second question. We have been very actively and strategically adding our investment capabilities around co-investment and [direct] investments, and they are able to help us in terms of effective fee rate. So if you do the math in terms of the recurring service fee rate over our AUM, it has been steadily improving over the last few quarters, and we continue to see opportunities and room for that to grow further.

In terms of the one-time commission effective fee, that is more related to the transaction value mix for that particular quarter. I mentioned earlier on my prepared remarks that it was around 83 basis point for the third quarter, slightly up versus the second quarter and down versus the third quarter of 2017. I think we are generally comfortable when our effective one-time commission fee

rate is around 80 to 120 basis points and quarter-to-quarter variance really depends on the transaction value product mix.

And now moving on to --

[Kenny Lam – Group President of Noah]

Can I mention one point about the recurring fee? I think the group here should understand that it has been a long-term strategy of Noah to try to move away its reliance on the single quarter volume sales, and actually moving more towards recurring revenue, because we believe that it actually is a much stronger basis for our revenue.

And so you see that it is a strategy that has been in place for the last 4 or 5 years where we're building up our asset management capabilities; we're building up diversified revenue sources that goes beyond the volume for the particular quarter. So I think that Shang's mentioned how we should not only focus on volume for that particular quarter, but actually look at how we have built a broader way of generating revenue is actually quite important.

[Shang Chuang – CFO of Noah]

Yes. Now, in terms of your third question on our lending business, our lending service business, so as of the end of September 30, 2018, we had a loan receivable roughly about RMB700 million. So that is the loan receivable that we have yet securitized. I mentioned the business model for our lending business is to form high-quality loan receivables and then securitize them out. From all the loans that were originated and eventually will be securitized, we expect this year we're going to probably reach somewhere around RMB10 billion, which would be -- if we achieve that, that would double what we did last year.

We have currently a provision of 1% for those loans that are on our balance sheet, but that's a temporary position as we will eventually securitize our loan receivables. But as of now, for the last two, three years that we have been operating this business, we have not had any defaults. The main reason is because of the fact that we focus primarily on high-quality borrowers and the fact that we have high-quality collateral.

On your fourth question on Huishan, I will pass it to Madam Wang.

[Jingbo Wang – Chairlady and CEO of Noah]

(Speaking Chinese).

(Translated). So a couple of points on the Huishan products that we have been helping our clients to undergo restructuring. So overall, we continue to see progress in terms of the restructuring of the Huishan investment. We're still currently in an official bankruptcy process, so I think that is a good sign. In terms of the operations of Huishan, we have now seen and observed several consecutive months of positive cash flow.

From the government policy perspective, the State Council has, in multiple occasions, highlighted that the dairy industry is a really important strategic industry for China. And the latest regulatory policies in terms of helping private enterprises access financing, encouraging a lot of debt to be converted to equity, I think this may also be beneficial to the restructuring of Huishan.

And lastly, the Huishan management is very focused on repaying, including our fund investment. And as of now, I think we will probably get more clarity on a repayment plan sometime next year.

[Operator]

Craig Cao with UBS.

[Craig Cao – UBS]

Speaking Chinese.

[Shang Chuang – CFO of Noah]

Okay. Thank you. For the benefit of the audience, I will translate the two questions from the analyst from UBS. So first question is that I noted for fixed income transaction value for the third quarter increased meaningfully. At the same time, we also saw operating margin improve in this quarter. Can you explain the reason for the margin improvement, given the strong fixed income product distribution?

The second question is in terms of the overall regulatory tightening that we saw for most of this year, Noah was still able to achieve relationship manager growth. So relationship manager grew roughly around 20% over the same period last year.

I noted for other financial services companies, such as insurance company, it actually has been difficult for them to increase the number of salespeople or frontline employees. So if management can share with us how Noah was able to increase relationship managers, and what is the plan in terms of relationship manager growth going forward? So those are the two questions.

I will answer the first question and Kenny will answer the second question. So you're right, so for the third quarter, we saw fixed income product transaction value increase meaningfully, primarily because we were able to engage with our clients despite volatility in capital markets with shorter-duration credit products. Shorter-duration credit products have lower one-time commission rate, but we still feel that it's important to maintain that engagement with clients.

The improvement in margin for the third quarter primarily is because of two reasons. One on the top line side, we saw very robust recurring revenue growth. This is because of the continued growth in AUM, as well as improvement in fee rate of the AUM that we manage.

The second reason is on the cost side. Given the volatility we saw in the first half, we were very focused on tightening costs and improving cost management for -- starting in the third quarter. And we felt that we did a fairly good job. And so across the board, cost has been quite managed in the third quarter, and particularly, we didn't spend any large amount of brand campaign dollars this quarter; most of it was in the second quarter. So we were able to, on a net basis, improve operating margin on a year-over-year as well as quarter-over-quarter basis to [above] 30%.

So I think on a full year basis, it will be good if we end up with an operating margin of somewhere near 30%. Medium to long-term basis, I feel that there is [room for] margin improvement as we continue to focus on productivity gains, but in the short term on a quarter-to-quarter basis, I think it really depends on what type of spending and investment we're making for that particular quarter.

[Kenny Lam – Group President of Noah]

And it's Kenny here. I'll answer the question about the relationship managers. I actually think that our relationship manager career development and training program has been the key attraction for the new talent. You can see that the way we manage our RM salesforce is actually not a very short-term focus. So we look at each RM and believe that it would take at least 2, 3 years before he or she becomes productive; he or she becomes a client-trusted advisor.

And therefore, if you see the way we develop the program, we focus a lot more on how we help the RMs build their skills. We invest a lot in training. We actually invest [a large] amount in their career development. So that's why we attract, in this actually down market, a lot of relationship managers to the platform.

The second point I want to make is if you look at the churn rate of our high-performing relationship managers, it's actually probably the best in the industry. We're below 3% in terms of churn rate for the high-performing relationship managers. And the tenure of our relationship managers are usually over 3 to 4 years.

And so just to summarize, we think that if you look at the front line, it is the key interface to our clients, and the key to loyalty. And therefore, we spend a lot of time thinking through how we invest in terms of training and how we invest in terms of career development.

[Operator]

Connie Shen with JP Morgan

[Connie Shen – JPMorgan AM]

(Speaking Chinese).

[Shang Chuang – CFO of Noah]

Thanks for calling. I guess for the benefit of the audience, I'll translate the questions into English first. So Connie from JP Morgan had a question regarding the relationship manager and the strategy on several metrics. So she notes that for registered clients, this particular metric has more than doubled over the last few years, while active client number has only increased in double-digits in the same period. In addition, the number of relationship managers increased roughly about 50% over the last two years. So given these three metrics, can management share with us what is the strategy on clients going forward? Is it to focus more on deepening client wallet share of existing clients, or is trying to get more registered clients become active?

[Jingbo Wang – Chairlady and CEO of Noah]

(Speaking Chinese).

[Shang Chuang – CFO of Noah]

A couple of points from Madam Wang regarding Connie's question. So we're actually quite excited about the medium to long-term growth aspect of our industry. And so we have been continuously recruiting high-quality relationship managers as well as employees because we

think these will be the basis for supporting our growth going forward.

In terms of the registered clients, I think over the last few years, we have been very focused on getting our brand out there to the potential clients, and getting them to become our registered clients. So you can see it as enlarging the funnel and getting access to high-net-worth individuals, both in terms of offline through our relationship managers who are now in more than 83 cities, also in last two, three years, I have also seen that we have done quite well in terms of our online efforts.

So if you download our App, you can see that you are able to get some -- our views on the market through our Apps, and you can get a better understanding of Noah. And so this is really to help enlarge our breadth in terms of being able to get in touch with high-net-worth individuals. But in this particular year, we actually have focused on larger clients because when the market is quite volatile, we actually think it's better to serve large clients because they would understand the volatility more rationally and more sophisticatedly.

For smaller clients, I think it's harder to serve them in a volatile market because they can be quite anxious, but we will service these newer registered clients, or these smaller clients, through other related services. For example, we have an education subsidiary that really focused on getting Chinese investor to be more updated on how the capital market is and what is a more proper way to invest their money long term. For example, we have more market low-correlation products such as insurance.

So I think going forward, we're really focusing on getting in touch with more clients, but being able to deliver and offer not just financial products, but also financial services offerings.

Now so whether we are going to focus on deepening wallet share of existing clients or trying to convert more registered clients to active clients, I think that strategy, particularly in such a dynamic market such as China, we need to remain flexible. In years where it's challenging in terms of the investment environment, we probably will focus more on deepening client wallet share. In an environment where the investment is not so difficult, we'll probably want to do more conversion of registered clients. So we will adjust it according to our view of the market.

Now, on our leading position on VC and private equity, I would also like -- Madam would also like to add that fundraising this year is lower than that of last year. But actually, we continue to make a lot of effort in strengthening our position in this particular segment. We have invested in very top-tier funds and our investment is more valuable because even for the leading GPs in China, in an environment like this, it's very difficult for them to raise new funds.

Actually, if you follow the industry statistics, I think new fundraising for venture capital, and private equity this year is down 80%. So the fact that we're still able to raise new money and make new deployments, makes us a very active participant. And this will cement and further solidify our positioning for this particular business.

Okay. I guess with that, if we don't have any further questions, we will end the call today.

[Kenny Lam – Group President of Noah]

Yes, any more questions, Operator?

[Operator]

There are no more questions at this time.

[Kenny Lam – Group President of Noah]

Okay. Well, thank you all for today's call.

[Shang Chuang – CFO of Noah]

Thank you. Bye.

[Operator]

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.