Noah Holdings Limited [Noah]
Q2 2023 Results Conference Call
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Company Representatives
Jingbo Wang, Co-Founder, Chief Executive Officer
Grant Pan, Chief Financial Officer
Melo Xi, Director of Investor Relations

Analysts
Yoyo Fan, CICC
Chiyao Huang, Morgan Stanley
Peter Zhang, JPMorgan

Presentation

Operator: Good day, and welcome to the Noah Holdings Second Quarter 2023 Earnings Conference Call. (Operator Instructions). After today's presentation, there will be an opportunity to ask questions. (Operator Instructions). Please note this event is being recorded.

I would now like to turn the conference over to Melo Xi, Director of Investor Relations. Please go ahead.

Melo Xi: Thank you, operator. Good morning and welcome to Noah's 2023 second quarter earnings call. I'm Melo Xi, Director of Investor Relations at Noah Group. The presenters joining us today are Ms. Wang Jingbo, our Co-founder, Chairlady and CEO, and Mr. Grant Pan, our CFO.

Before we start, we would like to kindly remind you that during today's call, we may make forward-looking statements based on our current expectations of the business. Please keep in mind that these statements are subjected to risks and uncertainties that may cause Noah's actual results to differ from these statements. We do not undertake any duty to update these statements. For a discussion of some of the key risks that could affect results, please see the Safe Harbor statement section of our 6-K filing.

We'll also refer to certain non-GAAP measures and you'll find reconciliations in our 6-K report made available on the Financial Reports section of Noah's Investor Relations website.

Also please note that nothing on this call constitutes an offer to sell, or a solicitation of an offer to purchase an interest in any Noah or Noah-affiliated products. This call is copyrighted material of Noah and may not be duplicated without consent.

Please also be aware that the link to a live webcast with presentation materials is available on our Investor Relations website.

With that, I would like to welcome our Chairlady and CEO, Ms. Wang Jingbo. Chairlady, handing to you now. Thanks.

Jingbo Wang: Thank you. (Speaking foreign language).

Melo Xi: Thank you, Chairlady.

(Translated). For the agenda of today's conference call, I would like to start with my thoughts on the macro economy and the wealth management industry, Noah's progress in global expansion plan; and then report on the overall performance of the first half of the year and the development of our business units. Then, Mr. Grant Pan, our group CFO, will present the financial information, followed by a Q&A session.

In the second quarter of 2023, we observed that the geopolitical conflicts and global economic slowdown has replaced inflation as the top concerns for Chinese high-net-worth investors, and they are taking accounts of these considerations when actively adjusting their asset allocation strategies. At the same time, due to the innovations and breakthroughs in AI technology driven by ChatGPT, high-net-worth clients who are familiar with primary market investments, such as venture capital, are also hoping to take part in this new round of technology advancement cycle and the investment opportunities that comes along the way.

A diversified asset allocation strategy in terms of geography and asset classes becomes increasingly important amid heightened level of macro-economic uncertainties. We recommend that Noah's high-net-worth clients to review their portfolios, starting with a running through a checklist across all aspect of their investments, ensuring sufficient allocation in the safety-net portion, coupled with multi-strategy investments to capture cross-cycle growth opportunities, achieving an anti-fragile strategic and tactical asset allocation.

We are also aware of the recent payment default by certain wealth management companies and trust product platforms on their non-standardized private credit products. I would like to point out that Noah, since its establishment in 2003, has been sticking to our founding principles and common practices of the financial services industry for 20 years.

From the inception of our company, we have insisted on the segregation of clients' capital, maintaining separate custodian accounts for our asset management products, no leveraged funding for clients, no products with maturity mismatches, and no cross-border fund movement transactions. Together with our continued devotion to investing in research capabilities, such principles not only establish us as a pioneer in terms of compliance and vision, but also bolster our capacity to navigate economic headwinds and shield our clients' hard-earned capital through professional asset allocation advisories.

Thanks to our continued devotion to strengthen our investment research capabilities, coupled with our management's forward-looking macroeconomic judgment, in 2016, we started to wind down our exposure in residential property assets. We have fully exited this asset class and among the clients who invested in this type of products, 98.7% were profitable. After the CX incident in

2019, we also started to wind down and fully exited non-standardized private credit exposure, or so-called trust products. During this exit process, although we experienced short-term hardships and lost some of our clients and employees along the way, we had successfully completed the standardization transformation in 2021 nevertheless, which was proven to have effectively safeguarded our clients' wealth amidst recent challenges faced by this asset class.

In terms of financial performance, the Company recorded overall net revenues of RMB1.7 billion in the first half of 2023, up 13.8% year-on-year. Domestic business contributed RMB1.0 billion, accounting for 59.2%, down 13.4% year-on-year. With our continued investment in distribution, products selection and comprehensive services, overseas business contributed RMB714.9 million, up 104.1% year-on-year, and increased its share of the group's revenue to 40.8% from 22.6% last year.

By segment, wealth management segment contributed RMB1.3 billion, up 22.5% year-on-year. The domestic portion contributed RMB769.9 million, down slightly by 4.3% year-on-year, while due to the expansion of overseas product offerings and comprehensive services income, overseas portion contributed RMB566.8 million, up 96.4% year-on-year.

Asset management segment contributed RMB389.9 million, down 5.4% year-on-year. Domestic portion contributed RMB241.9 million, down 31.2% year-on-year, while overseas portion contributed RMB148.1 million, up 140.3% year-on-year, mainly due to the increase in overseas AUM.

In terms of comprehensive services, wealth preservation and inheritance remain the most concerned wealth management needs among high-net-worth clients and families. In the first half of this year, revenues contributed by domestic insurance brokerage business grew 54.6% year-on-year. Overseas insurance, family trust and other comprehensive services grew by 380.8% year-on-year, with the number of active clients in this segment increasing over 6x, thanks to the growth of our operations in Hong Kong and Singapore offices.

For the first half, we achieved operating profits of RMB628.3 million with an operating margin of 36.0%.

For our domestic wealth management business, with the migration of domestic high-net-worth clients to Tier 1 and central hub cities, as well as more supply of talent, we continued our strategy to focus on and expand our presence in China's Tier 1 and central hub cities by increasing the recruitment of top-tier talent, enhancing the asset allocation capabilities and service quality of our relationship managers, strengthening investment and research capabilities and providing customized asset allocation solutions to our clients with the help of CCI model.

By the end of the quarter, the number of domestic RMs stood at 1,319, up 5.1% year-on-year and 1.5% quarter-on-quarter.

In terms of domestic online wealth management, through continuous investments in technology infrastructure, we have effectively integrated our clients' portfolio report with CCI allocation tools, which provides recommendations for clients' four types of wallets, namely liquidity management, growth investments, protection inheritance and safety-net portfolio.

During the first half, transaction value of mutual funds exceeded RMB 22 billion, up 14% year-on-year, while the transaction value of private secondary products exceeded RMB 8.5 billion, up 33.6% year-on-year.

In terms of corporate and institutional clients, the Smile Treasury platform, which was launched in 2022, has successfully attracted nearly 6,000 clients on board. During the first half, active clients increased by 73.7% year-on-year, with an average client AUA of nearly RMB600,000.

On the international wealth management side, we continued to implement our private banker recruitment program in Hong Kong and Singapore. By the end of the quarter, we had 56 relationship managers in Hong Kong and Singapore, up 100% quarter-on-quarter. We are also in the process of setting up client service stations in Los Angeles and Dubai, which should be completed in the second half of 2023, to better serve the global wealth management needs of Chinese clients around the world.

As of the second quarter of 2023, Noah International had more than 13,600 international clients, with the number of clients in Hong Kong and Singapore grew by 12.8% and 185.2% year-on-year respectively. Clients' AUM with Noah on a discretionary investment basis reached USD262 million, up 20.4% quarter-on-quarter, and the cumulative number of clients reached 471, up 44% quarter-on-quarter.

In terms of international Online Wealth Management, we successfully launched our iNoah One Account platform, an integrated account solution that provides multi-domain and multi-class asset allocation for Noah's overseas clients. We have also successfully connected nine systemically important banks globally through our nominee account, effectively reducing the time and cost of opening and managing separate bank accounts for our global clients.

Active clients for overseas mutual funds reached 1,956 people, a significant increase of 465.3% year-on-year; transaction value reached USD609 million, an increase of more than 700% year-on-year.

International smile treasury business, also began to show significant progress, and so far has successfully attracted more than 170 overseas corporate and institutional clients. The transaction value of the first half reached over USD73 million, an increase of 193.5%.

On the asset management side, Gopher's total AUM was RMB156.9 billion, up 0.9% year-on-year. Meanwhile, Gopher has established three strategic client groups based in Shanghai, Hong Kong and Singapore, with team members coming from diverse backgrounds including investment banking, consulting, buy-side and sell-side investment research and family offices. This not only enables Gopher to cooperate with domestic and international wealth management teams to provide exclusive, diversified and customized asset allocation services for strategic-level clients, but also to actively explore opportunities in expanding overseas institutional and family office clients by leveraging Gopher's diversified actively managed products at home and abroad.

In the first half of 2023, Gopher's actively managed target strategy product team dynamically deployed high-volatility strategies to enhance portfolio returns while balancing pullback and volatilities to maximize long-term returns. During the first half, its active investment product achieved 4% annualized return, annualized volatility of 6.3%, and Sharpe ratio of 0.4; its balanced investment product achieved a 8% annualized return, 5.6% annualized volatility, and Sharpe ratio of 1.2. Lastly, its stable investment product achieved a 9% annualized return, 2.1% annualized volatility, and Sharpe ratio of 3.6.

Overseas AUM of Gopher International's actively managed products, reached USD4.7 billion, equivalent to RMB34.3 billion, up 15.8% year-on-year, and its proportion of the group’s total AUM also increased to 21.8%. In 2023, we strengthened the screening, coverage and launching of top-tier global hedge fund managers, as well as the introduction of USD structured products, effectively completed our overseas product matrix.

In terms of ESG, we continued to promote the integration of investment products with ESG concepts. Since the end of 2022, Gopher has launched an ESG public market product in cooperation with Rayliant Asset Management, which integrates ESG evaluation framework into fundamental quantitative strategy, maximizing long-term investment returns amid the state’s efforts to promote the development of various segments of key ESG initiatives such as carbon neutrality.

As of July, we have cumulatively raised nearly RMB100 million for this product, with a cumulative return of over 14%, outperforming the CSI 300 benchmark Index over the same period.

In summary, Noah's long-term success as an independent wealth management firm lies in its adherence to our core strategy of client-centric, survival as the bottom line, as well as respecting the common senses of the financial services industry. Our three complementary business segments, including wealth management, asset management and comprehensive services, not only enable us to fully meet the needs of a diverse range of clients, including individuals, institutions and family offices, but also bring a greater degree of inherent stability and balance to our business.

Next, I would like to ask CFO Grant Pan, to present the financial performances in detail. Thank you all.

Grant Pan: Thanks, Melo. Thank you, Chairlady, and hello, investors and analysts. With the lifting of travel restrictions, the second quarter saw a steady recovery on track, and the contribution of contact-related activities to economic growth also expanded, as evidenced by a 5.5% year-over-year increase in GDP in the first half of the year. Despite more active domestic economic activities, the recovery is still at an early stage, and being confronted with uncertainties due to a slowing global economy and rising geopolitical concerns. The investment sentiment of high-net-worth individuals still remains at the conservative side as they continue to seek out safe havens and wealth preservation.

Our dedicated focus on client-focused strategy has paid off, with strong financial numbers showing that we are aligning clients' best interests with our wealth management advices provided. For the 6 months ended June 30, 2023, our net revenues increased by 13.8% year-over-year to RMB1.7 billion, of which 30.2% came from insurance income, as we have executed our CIO house view on wealth preservation and bottom-line-focused asset allocation strategy.

Together with our continued investment in talent capital, global research capabilities and broadened coverage network of top-tier global asset managers, net revenues from overseas business experienced a rise by 104.1% year-over-year, accounting for 41% of the Group's total net revenue.

In the meantime, we are committed to demonstrating the progress in building client channels, resulting in an 13.1% increase in the number of core diamond and black card clients. Within active clients, overseas active clients reached almost 2,000, an increase of 140% year-over-year.

Top-line wise, it is encouraging to witness a rather solid recovery in net revenues, mainly driven by expanding distribution of protection-oriented products and the growth in our international business. We increased the distribution share of insurance products both onshore and offshore, as evidenced by the quarterly one-time commission fees increased by 95% year-over-year and 130% quarter-over-quarter to RMB400 million, the highest-single quarter since 2022. In the first half of the year, one-time commission fees amounted to RMB580 million, up 87.8% year-over-year.

We expect a gradual recovery in investor sentiment in the second half of the year, which may lead to a rebound in growth-oriented investment for products. In addition, we have a robust pipeline of client events in overseas markets, which will lead to increased opportunities to the distribution of offshore investment and insurance products to overseas Chinese high-net-worth individual clients.

The stabilizing income stream, recurring service fees, was RMB921 million in the first half of the year, largely stable compared to the first half of last year. Performance-based income was RMB111 million, down 44% year-over-year due to the relatively muted exit environment. Other service fee income in the first half of the year was RMB133 million, up 62.8% year-over-year, resulting from more value-added services provided to our clients.

Benefiting from our effective cost efficiency strategy implemented in G&A and selling expenses, the first half of 2023 achieved an operating profit of RMB628 million and a healthy operating margin of 36%, down 1.4% and 5.5% respectively from the corresponding period of last year. This was mainly due to the low base of 2022 under strict restrictions on travelling and client activities, as well as higher government subsidies during Covid. Our strategy is to be cautious on overhead expenses, while still able to invest our resources into client interfaces and international talent acquisitions and operations.

The transaction value in the second quarter was RMB18.4 billion, up almost 10% year-over-year, an aggregate transaction value of RMB35.2 billion as of the 6 months ended. In tandem with the expansion of global footprint, overseas transaction value reached USD1.5 billion for the 6 months ended, equivalent to RMB10.5 billion, up 162.5% year-over-year, primarily owing to the introduction of discretionary investment and cash management products that have successfully increased our acquisition of overseas clients' wallet share. The contribution from overseas private secondary products significantly increased 764.5% year-over-year to nearly USD4.8 billion, equivalent to RMB34.8 billion.

In terms of transaction value in RMB products, our continuous efforts to expand our client base, including both individual and institutional clients, resulted in a 32.2% quarter-over-quarter increase in the transaction value, including both individual and institutional clients, resulting in a 32.2% quarter-over-quarter increase in the transaction value of mutual funds, while we maintained a cautious approach of fundraising and investment allocation in other investment products, especially in private equity.

That being said, we will continue to closely monitor the space for attractive opportunities, especially in the technology sector, as China's economic recovery continues.

From the perspective of segmented results in the first half of 2023, net revenues from wealth management were RMB1.3 billion, accounting for 76.3% of total net revenues. Asset management net revenues were RMB0.4 billion, accounting for 22.3% of total net revenues.

Internationally, we were able to effectively assist our clients in safeguarding their wealth in volatile capital markets, thanks to our forward-looking assessment on the macro-economy and advice to clients on wealth preservation in this environment. Dedication to global expansion helped fuel growth in overseas AUM with a 15.8% year-over-year increase to USD4.7 billion as of June 30, 2023, primarily attributable to our expanded array of offerings including structured products, mutual fund distribution, and private secondary products.

Turning to the balance sheet, we have maintained a healthy liquidity position with our current ratio at 3.2x. The gearing ratio is 19.8% and we have RMB4.7 billion in cash to further execute our globalization plan.

At the end of June, we voluntarily requested S&P Global to withdraw its credit rating coverage, which stood at BBB- with a stable outlook according to S&P, given our current capital structure and no need to raise debt financing in the foreseeable future.

In addition, the Board has approved a 1-to-10 share split proposal for our Hong Kong traded shares, in order to lower the investment barrier and increase the trading liquidity of the subdivided Hong Kong shares. Our ADS price traded on the New York Stock Exchange will not be affected. And the conversion rate between Hong Kong shares and ADS will be 5:1 after the subdivision takes effect. This plan will be subject to shareholder approval through an extraordinary general meeting, which is expected to take place on October 26, 2023 Hong Kong time.

In conclusion, our performance in the first half of the year has delivered steady growth in revenues, and positive progress for our international expansion strategy.

Looking ahead to the second half of 2023, we are optimistic that China will continue to produce growth opportunities, and are confident that investor sentiment, consumer confidence, and consumption will gradually but steadily improve. Against this backdrop, we are confident that we can better assist our domestic clients optimize their asset allocation strategy and provide more advanced client experiences.

Overseas, as geopolitical conflicts and the financial environment become more unstable, tightening conditions are still seen as top concerns for high-net-worth individuals across the globe. Not only is their demand for global asset allocation services increasing, but their need to enter global markets as some entrepreneurs is also on the rise, resulting in a faster wealth accumulation effect for our high-net-worth clients in the coming years.

We have always evolved our strategic structure and footprint to adapt to changing trends. With more offices and international talent recruitment, we believe this innovation will enable us to attract high-net-worths around the world [and equip us to meet the needs of global Mandarin-speaking clients].

Once again, we thank all our shareholders for their trust and support. And we remain committed to creating diversified offerings and long-term value for our clients and shareholders.

Thank you for your time. And we will now open the floor for questions.

Questions and Answers

Operator: We will now begin the question-and-answer session. (Operator Instructions). Yoyo Fan with CICC.

Yoyo Fan: (Speaking foreign language). I have two questions. The first one is regarding the recent risk event faced by the wealth management companies. So what's the impact on how industry and also on our Noah?

The second question is about our coverage network. As we can see the cities we covered decreased in this calendar year. So what's our future plans for the domestic cities layout? That's my questions.

Grant Pan: (Speaking foreign language).

Jingbo Wang: (Speaking foreign language).

Grant Pan: I think I give a translation and also supplement from me. Chairlady said it's actually expected matter, it's probably a matter of time in terms of how the asset is consisted of mostly real property exposure, as well as some the ST, or low-price A-stocks, that in the history, we've never had any cooperation with these companies. And I believe it's also a very, I guess, historical moment in terms of investor education for this industry, as Warren Buffet said that bad things are not going to last; it's going to disappear, it's just a matter of time.

So our strategy has always been evolving around the whereabouts of our clients. So as we first started in this industry, obviously, many of them entrepreneurs in probably 4-5 tier cities, 20 years ago. But I guess as of now, 2023, most of them already moved into first-tier cities, and we believe actually have better talent supplies, and probably closer in terms of physical distance to our clients. And that's why we're focusing our resources in the top cities in China, and that way, we're able to be more efficient and also consolidate our resources in these top cities.

Yoyo Fan: (Speaking foreign language). Thank you very much.

Operator: [Chiyao Huang], Morgan Stanley.

Jian Huang: (Speaking foreign language). My first question is regarding the management's outlook on PE/VC investment and exit condition in China. What's the outlook for the PE/VC fundraising and other sales in the future, considering the IPO environment domestically and offshore?

And second question is on the plan for the cash balance that Noah have, which is quite sizeable. And is there any investment plan or any plan to further enhance shareholder returns?

Grant Pan: Okay. I will have Chairlady answer the first question and I'll take the second question in terms of the balance sheet capital.

Jingbo Wang: (Speaking foreign language).

(Translated). So as you know that if you're familiar with Noah, obviously, we have been in this industry PE/VC actually rather early stage. And the peak actually distribution and placement of PE/VC came in the year 2017. So I guess we're still pretty confident in terms of how the portfolio companies are performing. Obviously, people need a better -- a longer patience in terms of exiting. As long as you're holding on to the good companies, we believe things will get on the brighter side in terms of exiting conditions.

Another thing is we actually have done a batch of exiting in the year spent between 2020 and 2021, when the market conditions were performing relatively well, and realized carry income for both the company as well as the clients. We did a quick survey, historical statistics, if you will, for the past historical investments for clients. As we mentioned on the call, that the products relating to real properties, actually 98% investors' claims have benefit, have made profits on the exit. In terms of PE/VC existing clients, also over 90% are at profitable in terms of their investment cost.

So we're optimistic, although prudently optimistic, about the future of the PE/VC industry. We will continue to probably move a little earlier stage in terms of PE/VC and focusing on technology-based companies. So that's for the PE/VC question.

And in terms of the cash on the balance sheet, obviously, we plan and cautiously maintain a very strong liquidity position. Although the balance sheet under accounting principles show 4.7 billion, we actually do have another round 300 million to 400 million in short term investments. So the total capital liquidity position is around 5 billion cash. I think one plan, one part of the plan, is obviously to continue to support our international expansion, which obviously, has a pretty high demand on capital; and the second time also, debating to continue to increase dividend distributions in the future, as we want to make sure that we bring better returns to our shareholders.

Chiyao Huang: Thank you very much.

Jingbo Wang: (Speaking foreign language).

(Translated). I think another interesting fact to supplement is that we do put together a dedicated team to work on exiting the portfolio companies. And we're noticing an interesting trend where probably in the past, the founders of these portfolio companies are not a little bit reluctant to give cash back to the shareholders as they continue to grow. But we believe that noticing a trend, that more and more of them are willing to actually distribute cash and capital back to the shareholders if the IPO is -- the timing the IPO is uncertain -- they're willing to give a little bit more capital back to the shareholders, just like what Noah is doing.

Chiyao Huang: (Inaudible).

Operator: Peter Zhang with JPMorgan.

Peter Zhang: (Speaking foreign language). My first question is regarding the mutual fund management fee cut. We notice that major mutual fund in China has been cutting their management fee since July. We wish to understand what's the potential impact to Noah?

My second question is regarding the second half outlook. We notice that in second quarter, insurance business contribute a large proportion of the revenue. And we notice that a major insurer in China has been stop selling the 3.5% guarantee in the quarter. We wish to understand what will be the trend in second half for insurance-related business for your revenue trend?

Grant Pan: Okay. Thank you, Peter. I'll take the first question. Mutual fund is actually a very important tool for us to first attract new capital from clients, or maintain their wallet share between products. So although obviously, we're seeing this trend of downward pressure on mutual fund fee, but the actual contribution of revenue from mutual funds to our group net revenue is actually at a pretty small percentage.

The total distribution fee plus the management fee to the contribution of the net revenue actually is less than 5%. So the impact of our 2023 net revenue of the fee downgrading is not going to be more than 3 million RMB. Even we annualize that, it will be less than 10 million. So I guess the direct financial impact on gross net revenue is rather limited, but we continue to use mutual fund and continue to expand the strategic distribution placement as a good way to attract new capital and also, I guess, maintenance of the existing capital of clients.

Jingbo Wang: (Speaking foreign language).

(Translated). We also think it's probably going to be helpful for high-net-worth individuals to attract new orders because some of the mega-internet platforms for mutual funds probably has reached its peak in terms of distribution and maintenance of mutual funds. And many platforms actually, clients may have concentrated portfolio that probably will experience some significant or at least some major losses because of the concentration. But now with IC model in terms of mutual fund placements.

And also, we believe that high-net-worth individuals are getting more and more sensitive to the fees associated with mutual funds, so IC model as well as lower transaction costs and infrastructure costs will help them to actually put more investments -- or transferring more investments from traditional private hedge funds or private equity into more standard and lower-cost mutual funds.

In terms of the future, I guess for the second half of the year, we know that insurance products from domestic contributed quite a bit of revenue, honestly to the entire industry for the first half. But I guess for the second half of the year, we'll continue to advise our clients based on our CIO lead, probably still on a pretty conservative side, and overseas insurance product [audio gap] insurance also diversified investment product portfolios will continue to consist of a large part of the transaction value of second half.

(Speaking foreign language).

Jingbo Wang: (Speaking foreign language).

(Translated). Insurance distribution probably is very helpful supplement in total solution to our clients. But mostly in the past, it's either product-driven or campaign-driven, like I just mentioned, 3.5% domestic insurance. But we have been building or putting together a lot of infrastructure and platform around insurance as a total solution to our clients; and also, diversified the client type from purely individual base to probably more enterprise base.

And we'll continue to build that into one of our primary solutions to our clients, and I guess the way we actually conduct our insurance business is a little different from purely agency-based insurance type of institutions, as we do put insurance product strategy as part of the total solution to our clients.

Peter Zhang: That's very clear, thank you. (Speaking foreign language).

Operator: As we have no further questions, this concludes the question-and-answer session. And the conference has also now concluded. Thank you for attending today's presentation. You may all now disconnect.