Noah Holdings Limited [Noah]

Q1 2023 Earnings Release Conference Call

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Company Representatives

Ms. Jingbo Wang, Co-Founder, Chief Executive Officer

Mr. Grant Pan, Group Chief Financial Officer

Mr. Melo Xi, Director of IR

Analysts

Helen Li, UBS

Chi Yao Huang, Morgan Stanley

Mr. Xi

Good morning and welcome to Noah's 2023 first 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. I'd like to inform you that we are currently live from our new headquarters Noah Wealth Center, located in Hongqiao, Shanghai.

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 discussion of some of the 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 the our 6-K report made available on the financial reports section of Noah's investor relations website.

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

Ms. Wang speaking in Mandarin (as translated)

For the agenda of today's conference call, I would like to first talk about the macro economic environment, Noah's global expansion progress, and then report the overall performance of the first quarter as well as our various business segments. Then, Grant Pan, our group CFO, will present the financial information for the quarter, and lastly, we will end with a Q&A session.

After an extremely complex macro environment in 2022, the macro challenges still persist in 2023. Heightened interest rate levels and a tight credit environment in the U.S. not only limited the recovery in economic activities, but also significantly impacted the stability of the European and US financial systems. The loss of depositor confidence in small and medium-sized banks and regional banks spiraled into an accelerated withdrawal of savings and bank runs, also causing shareholders of these banks suffering significant losses. While U.S. regulators provided timely protection for clients' deposits in these banks, the restoration of investor confidence in the capital markets was inevitably delayed again.

In the Chinese market, after 3 years of pandemic control, we believe the Chinese economy will get back on trajectory for growth, as COVID restrictions were lifted and borders opened. However, it will take time for the economy to recover, and we see that while consumption in sectors such as tourism and restaurants are picking up, sales of big-ticket items such as real estate, automobiles and home appliances are still weak, which indirectly reflects the cautious attitude of consumers towards future income growth expectations. We believe that China's wealth management and asset management industry, which is dominated by capital market products, will encounter great challenges as the bank deposit portion of consumers' financial assets may be held longer, and China's wealth management industry will shift back to bank dominance; on the bright side, we believe the rising savings rate also provides growth opportunities for diverse investment products in the future, benefiting distinguished independent wealth managers like us; As overseas inflation and U.S. dollar interest rates remain high, we have seen a substantial increase in overseas Chinese's demand for global asset allocation. As an independent wealth manager, Noah's overseas offices in Hong Kong, Singapore and the U.S. have become substantially more attractive to overseas Chinese HNW clients as they can offer a more diversified range of global wealth management products.

From 2019 to 2022, after three years of organizational reforms, Noah has internally formed three established product business units, namely, Gopher Asset Management, Fund Smile and Noah Glory which provides insurance, family trust and other value add services. Each of these product BUs has relatively independent domestic and international operations. Starting in 2022, Noah has also begun to actively build overseas direct sales capabilities, and online client service interfaces to better service global Chinese investors.

During the first quarter of 2023, the Company recorded overall net revenues of RMB 803 million, up 1.0% YoY and down 8.9% QoQ. The domestic business contributed RMB 488 million, accounting for 60.3%, down 20.2% YoY and 19.0% QoQ, while the overseas business contributed RMB 321 million, up 68.4% YoY and 13.0% QoQ, and increased to 39.7% of total revenue from 23.8% from the comparable period last year. With the gradual improvement of Noah's overseas setup, we hope that the contribution of overseas revenue can reach more than 50% of the whole group in the next 3-5 years.

Thanks to better cost management, the operating margin for the first quarter was 34.7% and operating profit was RMB 279 million, an increase of 26.9% QoQ.

By segment, the wealth management segment contributed RMB 589 million, up 1.5% YoY and down 9.4% QoQ. The domestic portion contributed RMB 351 million, down 17.5% YoY and 20.7% QoQ, while the overseas portion contributed RMB 238 million, up 52.7% YoY and 14.8% QoQ, thanks to the growth of overseas product transaction value and insurance distributions.

The asset management segment contributed RMB 206 million, up 2.3% YoY and down 8.1% QoQ. The domestic portion contributed RMB 123 million, down 26.3% and 16.6% YoY and QoQ, respectively, while the overseas portion contributed RMB 83 million, up 138.8% YoY and 8.2% QoQ; this was mainly due to the growth in the scale of overseas AUM and the increase in carry income from overseas private equity exits in the first quarter.

On the protection and preservation side, the demand for insurance product allocation from HNW individuals remained high. During the first quarter, the domestic insurance brokerage business generated 241.0% YoY growth in revenue and the number of active clients increased more than 6 times YoY.

For our overseas insurance brokerage business and overseas family trust services, during the first quarter, overseas insurance revenue increased 179.8% YoY and 2.9% QoQ, and the number of active clients increased 234.1% YoY and 31.7% QoQ. Our overseas family trust team has provided trust services to a total of 473 overseas Chinese families as of the end of the quarter, an 8.2% increase compared to the end of 2022. Evidently, in an environment where capital market volatility continues and uncertainty in the macro environment has yet to subside, there is still a lot of unmet demand for asset allocation security from Chinese clients around the world.

For our domestic wealth management business, our core strategy is to focus on upsizing and strengthening central hub cities. Tier 1 cities have more talent resources and better innovation environments, as well as better education options for children. As domestic HNWI migrate to Tier 1 cities, Noah is also reducing the number of satellite cities to further reduce costs and increase efficiency, while increasing investments in Tier 1 cities. As of the first quarter, the number of domestic relationship managers was 1,299, a 3.2% increase from the previous quarter.

In terms of domestic online channel, we focused on strengthening the empowerment of technology systems and upgrading client experience. By providing a wider array of online product shelf, CCI asset allocation tools and investment strategy reports, as well a more interactive and informative portfolio interface, transaction value for mutual funds reached RMB 10 billion, an increase of 40.3% year-on-year;
In terms of corporate and institutional clients, the Smile Treasury platform launched in 2022 successfully attracted nearly 5,000 corporate and institutional clients. During the first quarter, the number of active clients of Smile Treasury increased by 325.5% YoY, and the overall AUA with us reached RMB 2 billion.

On the international wealth management side, we further expanded the number and quality of our branch offices and private bankers. As of the end of the first quarter, Noah's Hong Kong and Singapore wealth management teams had 28 relationship managers, with the goal of reaching 100 private bankers in Hong Kong and 20 private bankers in Singapore by the end of 2023.

As of the first quarter of 2023, the number of clients in Hong Kong and Singapore achieved 13.1% and 77.6% YoY growth, respectively. Clients' AUM with Noah on a discretionary investment basis reached USD 230 million, up 33.2% YoY, and the cumulative number of clients reached 327, up 79.7% YoY. Noah's international client grew 13.2% YoY to 13,427, and the number of active overseas clients reached 1,763 in the quarter, up 35.3% YoY.

In terms of international Online Wealth Management, in 2023, we will mainly focus on helping overseas private bankers to be able to fully execute their clients' transactions, and provide portfolio advice and services to their clients online more efficiently.

The number of active clients of overseas mutual funds reached 1,409 in the first quarter, a significant increase of 537.5% YoY; transaction value reached USD 340 million, a 10.4% increase QoQ on top of a more significant YoY increase; the overall overseas mutual fund AUA reached USD 970 million, an increase of 588.7% YoY.
International smile treasury business, also began to show significant progress, and so far has successfully attracted more than 140 overseas corporate and institutional clients, the transaction value of the first quarter reached 35 million U.S. dollars, an increase of 13.4 times.

On the asset management side, Gopher's total AUM was RMB 157.6 billion, up 0.9% YoY. Among which, Gopher's actively managed target strategy products, executed disciplined risk management and limited pull-backs. During this quarter, the investment team made timely investment judgments and its active investment product achieved 12.3% annualized return, annualized volatility of 6.3%, and Sharpe ratio of 1.7; its balanced investment product achieved a 14.9% annualized return, 5.2% annualized volatility, and Sharpe ratio of 2.6; lastly, its stable investment product achieved a 7.8% annualized return, 1.9% annualized volatility, and Sharpe ratio of 3.3.

Overseas AUM of Gopher International's actively managed products, achieved a 14.9% YoY increase to USD 4.9 billion and accounting for 21.2% of the total AUM. In the current interest rate and economic cycle, we see excellent entry opportunities and investment thesis in private credit, private equity buyout, special opportunities and PE Secondary funds, as well as early stage technology VC investments. Gopher's overseas PE AUM also achieved a 7.5% YoY increase to USD 3.9 billion in the first quarter. We plan to continue to improve our global coverage of top managers and expand our partner network, as well as upgrade our KYP technology system, to better provide overseas alternative investment product solutions to our global Chinese clients.

In terms of ESG, 2023 is the 9th year for us to publish sustainability reports, to showcase the new developments and achievements of Noah towards ESG every year. In the past 3 years, Noah started to track ESG awareness among Diamond and Black card clients and saw the willingness of investing in ESG increase from 35% to 87%. Noah's continuous ESG advocacy and investor education has also played a non-negligible role in the process of clients' greater recognition of ESG concepts.

In addition to the environmental and sustainability aspects, we have made continuous improvements at the corporate governance level. We have built collective leadership by establishing five major committees at group level, including the Strategy Committee, Talent Committee, Reform Committee, Operations Committee and Technology Committee. We have established the AT + ST framework in each business unit (BU) and region, which is responsible for building and motivating talent, as well as making and managing key business objectives, thus completing the transformation from "individual leadership" to "organizational capability". In this process, although the management awareness and decision-making efficiency seem to be slower, the quality of decision-making has been greatly improved.

Finally, we have officially opened our brand new headquarter on May 18 this year. Noah Wealth Center is located in the core area of Hongqiao transportation hub, located in the central axis of Shanghai, the whole complex has a total area of about 72,000 square meters. With the geographical advantage of Hongqiao transportation Hub, Noah can serve its clients from Delta triangle, as well as the whole country and even the world more conveniently. We have made a stand-alone building of the new headquarters a client-centric experience center for Noah's global clients, making Noah a truly private bank with a unique client interface.

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

Mr. Pan

Thank you Chairlady, and hello investors and analysts. As mentioned by the chairlady, the first quarter of 2023 entails a moderate economic recovery in China, indicated by a 4.5% YoY growth in its GDP. Market sentiments started to slightly lean away from savings, turning to a mild increase in the demand for investment, evidenced by a 2.2% QoQ rate of rebound in the issuance value of mutual fund products. Although investors activities became more active and transaction values in the markets have gone up, sentiments towards relatively higher risk-profile products, like PE products, still remained prudent.

In the meanwhile, from an international perspective, the US Federal Reserves has been sticking to a hawkish monetary policy throughout the quarter, accumulatively raising the federal interest rate twice from 4.5% to 5%, which largely indicated a continuation of the theme from 2022. In addition, the sudden collapse of SVB in March caused US banking sector in crisis and even had spillover effect on global financial industry, which brought concerns to investors about market volatilities on top of hiking rates and tightening credit conditions.

Staying true to our client-centric strategies, we dedicate to transform these uncertainties into opportunities to generate cross-cycle preservation and growth for our clients' wealth, coupled with our constant improvement in domestic capabilities and ongoing expansion in the international market. In turn, our client engagement and financial performance weren't hindered by the concurrent complex macro environment. Noah's quarterly transaction value increased 12.0% YoY to RMB 16.8 billion, 31.5% of which contributed by overseas products. Reflecting on financials, revenues from overseas business for this quarter increased 68.4% YoY and 13.0% QoQ to RMB 321 million, taking up 40% of the group's total revenue. Combined with the cost efficiency strategy, Noah achieved a 26.9% QoQ increase in operating income to RMB 279 million, implying an operating margin of 34.7%. As a result, non-GAAP net income was RMB 240 million, up 60.6% QoQ with the net margin standing at 29.8%.

Now, please let me walk you through the detailed financial results of the first quarter.

We recorded quarterly net revenues of RMB 803 million, up 1.0% YoY but down 8.9% QoQ. Notably, our one-time commission fees were up 72.5% YoY to RMB 176 million, indicating a quick recovery in investor sentiments regarding products with lower risk profiles such as insurance products. As our global expansion strategy progresses, the distribution of offshore insurance products took up an increasing share of revenue this quarter, and we believe the expansion of offshore products' distribution to Chinese investors residing abroad will have ample room to grow.

The stabilizing revenue stream, recurring service fees, was RMB 474 million in the first quarter of 2023, which takes up 58.8% of total revenues and remains relatively steady from last quarter. Performance-based income was RMB 83 million, flat from the previous quarter but went down 52% YoY due to weaker market performances on security-type products.

Quarterly operating income was RMB 279 million, down 11.1% YoY but up 26.9% QoQ, implying an increase of 9.8% QoQ in operating margin due to a 20.8% QoQ decrease in total operating cost and expenses, which is resulted from our precise cost efficiency strategy in G&A and selling expenses. Interest income in this quarter was RMB 34 million, up 172.1% YoY and 141.3% QoQ mainly as a result of USD deposits. Consequently, non-GAAP net income was RMB 240 million, down 23.6% YoY but up 60.6% QoQ, indicating a non-GAAP net margin of 29.8%, which increased 12.9% QoQ while decreased 9.6% YoY due to the change of our revenue structure in carry.

Transaction value was RMB 16.8 billion for the quarter, up 12.0% YoY but down 6.7% from the previous quarter. Notably, the transaction value of private secondary products increased 6.5% YoY and 27.5% QoQ to RMB 4.3 billion. The transaction value of mutual fund products decreased 18.1% QoQ to RMB 10.0 billion, but it increased 40.3% YoY thanks to our continuous efforts to enlarge our client base including both individual and institutional clients onshore and offshore. Besides, the transaction value of private equity products was RMB 1.3 billion, mainly from USD PE products which went up 3% QoQ, thanks to the continuous fundraising of our New York real estate investment team and Silicon Valley venture capital investment team as well as an enlarged coverage and selection of global top tier products.

Since the loosen-up of COVID restrictions and domestic and international traveling. We have been investing heavily to bring back Noah's famous investment seminar to our clients. The client summit we held in Hangzhou during the first quarter of 2023 attracted more than 1200 HNWIs clients and dozens of reputational fund managers in the industry, who are invited to provide their latest views on the economy and investment strategies. Additionally, overseas client activities, like the investment summit we held in Hong Kong, also underpinned a promising progress for Noah's global expansion plan with over 600 clients in attendance. The portion of overseas transaction value reached 31.5%, up 15.5% YoY and 3.2% QoQ; overseas AUM also increased 14.9% YoY and 2.8% QoQ to RMB 33.4 billion, taking up 21.2% of total AUM. Moreover, overseas active clients went up 35.3% YoY and 1.3% QoQ, demonstrating the progress in the establishment of client channels in our overseas wealth management business.

As for our segmented results, net revenues from wealth management were RMB 587 million, taking up 73% of total net revenues, Net revenues from asset management net revenues was RMB 205.2 million taking up 25.5% of total revenues,.

Total AUM increased by RMB 445 million from last quarter, sitting at RMB 157.6 billion, primarily due to the increase of AUM in public securities products thanks to our

USD cash management offerings. Overseas AUM increased by RMB 919 million this quarter, making up 21.2% of total AUM.

Moving onto balance sheet, we remain in a healthy position in terms of liquidity as our current ratio stands at 3.2 times. The debt to asset ratio was 20.2%. Currently, we have RMB 4.7 billion in cash and we are preparing the dividend payouts as well as executing our globalization plan.

In addition, as mentioned in the previous quarter, Noah will declare a final dividend of RMB 5.5 per share, equivalent to US$0.4 per ADS or HK$6.2 per share, subject to the final approval of the upcoming AGM on June 12, 2023. We look forward to providing stable and sustainable returns to the shareholders with the growth of our business.

Wrapping up, our first quarter performance delivered a stable set of underlying results with a positive outlook on our domestic-international Dual Circulation Strategy. We believe that Noah will be able to tread through the uncertainties and seize the opportunities to expand in the coming years. Again we sincerely appreciate all shareholders for your ongoing trust and support, and strive to create diversified portfolio and long-term value for clients and shareholders.
Thank you for listening, I will now open the floor for questions.

Questions and Answers

Helen Li: This is Helen from UBS two questions if I may. The first is on RM expansion plan in the first quarter: the number of onshore RM saw a sequential increase of 40%. I remembered your previous guidance was no increase or slight increase in onshore RM, so is there any change of plans; and for the 40% increase in onshore RM how many were new joiners and how many RMs have left the firm. The second questions is on revenue contribution from Hong Kong business, what proportion of the revenue can be attributable to newly acquired local clients rather than onshore client referrals. Thank you

Ms. Wang (as translated) and Mr. Pan: Thanks Helen, basically the change in the domestic RMs are in compliance actually with our strategy domestically, we do have a program called 311 basically the 14 cities the 3 major city is Shanghai, Beijing, Shengzhen and also 11 or 12 other first-tier city that we believe are very, very important for the future market expansion. So for these cities we actually do have a goal for the average business that is over 10 billion each year within 3 to 5 years, so for these city we are still expanding and also recruiting actively. As a result on these smaller cities probably in the 3rd, 4th tier networks, the branch offices you know some of the RMs that are not operating or performing to the standard of the 311 cities obviously we let go, or they choose to leave. But we don't' have exact data to track the turnover rate but if you want it, we will be very happy to provide it. But basically is the strategy surrounding the domestic market is to continuously to heavily invest into the 311 cities. We actually as a matter of fact, I just want to supplement. You know, from the budget standpoint, we do set aside a strategic budget to support the hiring, especially the higher talents that probably doesn't fit in the current compensation schemes who actually do have a strategic budget to supplement the cities so they're able to attract the relatively higher tier talents. So we'll see a number in the in the number of RM and also contributed partially to the Plan Big Tree That's basically we're trying to attract relatively younger blood into the team. so basically the ones with less than five years' experience but with great academic background, and to supplement the RM team so that will actually have a team of younger talent, that'll be able to grow into larger and better RMs in the future years. So Helen to your second question, basically we don't typically characterize that as referral a local business. So basically, all the oversea business that arising from the class demand are 100% viewed as locally developed. So basically, the domestic RMs, when they do realize or they, their clients actually express to them that they do have oversea assets and they need some help on the allocation, I won't see assets, the domestic RM will actually team up with RMs in Hong Kong and Singapore to continually to focus on figuring out what exactly the allocation is, but I think one factor is for sure, that domestic RM is not aware of and they will not be able to know what exactly they placing orders on or what kind of allocation advice is provided to them. So that's, I would say 100% as being served locally on the oversea market and these clients assets already, you know, overseas, and they're probably already being served by the oversea private bank or other institutions. So basically that piece of business will be built, purely as the oversea allocation

Helen Li speaking in Mandarin (as translated): One more question, since Hong Kong and Singapore have a 120 RMs recruitment guidance, I was wondering if there is any recruitment guidance in mainland.

Mr. Pan speaking in Mandarin (as translated): There is no exact guidance in the mainland China, however, the RM recruitment plan is still focusing on 311 cities under 5+2 compensation model that each team has 5 ARs plus 2 FRs along with suitable SRs, by which each city is able to acquire reasonable compensation based on their performance. Thus, there is no limit or guidance of RM hiring as long as it delivers ideally.

Chi Yao Huang: The first question is on the asset allocation of high net worth individuals their preference and the preference products. What's the latest trend the managements are seeing right now. And the second question is on the revenue and profit outlook and especially what party is more certain we think will be the most important drivers this year and what the other parts are more uncertain this year. Thank you.

Ms. Wang (as translated) and Mr. Pan: So what basically we still are looking at rather uncertain macro outlook. So majority of the clients actually take a pretty defensive stance in terms of the investment strategy or you will say bear market minded or balanced minded type of strategy. I think it's one interesting fact to note that the age structure of majority of the high net worth individuals are first generation entrepreneurs or business owners. So in the first half of their life, you know, obviously very aggressive and probably in the attack mode, if you will, in the investment strategy, but now they're getting, you know, especially the baby boomers that was born between 1962 to 1972. They're looking at the second half their life so that taking much more defensive strategy and mindset towards investment and asset allocation strategy. If you think about it, that a majority of the wealth and asset and investment probably are very heavily pro-China in the past, and now they're probably looking at an erupting globalization as allocation strategy to diversify the geographic risks. So we're seeing a very clear trend of increasing allocation probably to the preservation strategy in terms of assets structure, in terms of insurance products, even trust and some of the family planning, to actually not only support investment as allocation but also the lifestyle on the Global Citizen type of style. Not yet seeing a quick recovery, a strong recovery, investment type of assets. We believe that they're still assessing the situation, but I guess the action and also the mindset currently is still I would say very conservative. So that's the answer to your first question Chi Yao. To your second question, in terms of revenue and profit for the rest of the year, obviously, since we're getting primary listed on Hong Kong stock exchange, we cannot give a revenue or profit guidance. But I think one thing is for sure that from the expense and cost strategy, even if we're heavily investing on the globalization, we're still actually trying to maintain a relatively consistent profit margin to the past years. So basically, we're seeing more cost efficiencies, especially from domestic operations. For example, we're actually heavily concentrated in larger cities but closing down some of the smaller cities. Also, you know, letting go some of the low performing RMs and also using more the NWC which is the new headquarter as the marketing scenario, instead of, you know, paying millions on the hotel rooms, you know, especially for Shanghai and JiangZheHu provinces. So we'll maintain a relatively steady profit margin, especially from human capital expenses standpoint. And two, we believe that the continuing strive for, as you see in the first quarter, we actually have a very strong recovery in one-time commission, which means that we're still growing the new revenue from larger wallet share on newer clients. That's what we're maintaining. So hopefully, now obviously, even during a recovery year that China has a goal for the GDP recovery increase, So we obviously from the annual budget standpoint, are still very growth minded. We're obviously you know, growing the new territory in the global and oversea business, but at the same time, we have been installing quite ambitious targets I would say for wealth management, as well as other three business units that we have just mentioned. So we'll be hopefully seeing larger growth on the top line at the same time maintain a relatively healthy profit margin.

Mr. Xi

Thank you Peter, we have no further questions from the audience. So with that, we would like to conclude this quarter and year end's earnings call for our most updated financial reports. Please refer to the financial statements section within our investor relation website. So thank you all for listening.