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CISG - Q2 2013 CNinsure Inc Earnings Conference Call

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by for CNinsure's second quarter and first half of 2013 earnings conference call. At this time all participants are in a listen-only mode. After management's prepared remarks, there will be a question-and-answer session. Please follow the instructions given at that time if you would wish to ask a question. Please be advised, this conference call is now being broadcasted live over the Internet, and a webcast replay will be available within three hours after the conference has ended. Please visit CNinsure's IR website at ir.cninsure.net, under the events and webcasts section. Today's conference is being recorded. If there are any objections, please disconnect at this time. I would now like to turn the meeting over to your host for today's conference, Ms. Oasis Qiu, CNinsure's Investor Relations Officer.

Oasis Qiu - CNinsure Inc. - IR Officer

Good morning, everyone. Welcome to our second-quarter and first-half 2013 earnings conference call. The earnings results were released earlier today and are available on our IR website, as well as on the newswire.

Before we continue, please know that the discussion today will contain forward-looking statements made under the Safe Harbor provisions of the US Private Securities Litigation Reform Act of 1995. The accuracy of these statements may be impacted by a number of business risks and uncertainties that could cause our actual results to differ materially from those projected or anticipated. Such risks and uncertainties include but are not limited to those outlined in our filings with the SEC, including our registration statement on Form 20-F. We do not undertake any obligation to update this forward-looking information, except as required under applicable law.

Joining us today is our Chief Executive Officer, Mr. Chunlin Wang, and Chief Financial Officer, Mr. Peng Ge. They will walk you through our financial and operating performance in the second quarter and first half 2013 and take your questions after the prepared remarks.

Now I will turn the call over to Mr. Wang.

Chunlin Wang - CNinsure Inc. - CEO

(Interpreted). Hello, everyone. Thank you for joining us on the call. On today's agenda, our CFO, Mr. Peng Ge, and I will discuss the operational and financial highlights for the second quarter 2013 and share with you our business outlook for the rest of the year. We will take your questions after this.



China insurance industry grew 11.5% year over year in total gross premiums for the first half of the year, while property and casualty insurance premiums maintained a year-on-year growth of 16.6%, mainly driven by a modest increase in car sales. Fierce price competition in the sector continued into the second quarter, further squeezing the underwriting process of many P&C insurance companies.

In the life insurance sector, [high] sales of short-term investment-linked policies boosted life insurance premium growth during the second quarter, driving an 8.9% year-on-year growth in the first half of the year. While such common policies offer limited support to long-term embedded value, new business value in the life insurance sector remained in weak growth territory.

When faced with the market dynamics, we believe that we must keep abreast of the market changes in order to stay on the top. Over the past six months we have devoted a lot of effort through the use of technology and strengthened our capacity to better serve our clients with comprehensive financial services and products. We are pleased with the progress that we've made on executing the strategy.

During the second quarter, our mobile business support system has been put into operation in Guangdong, Sichuan and Hebei provinces. And an internal testing has been extended to Liaoning and Henan provinces. The aggregate number of CNpad, the workstation of the mobile business support system that was sold, exceeded 480 units as of June 30, 2013. And those units contributed over CNY15m in premiums during the first half of 2013. Besides, we were pleased to see premium contributions occurred [back] to CNpad, which CNY36,900 per month, slightly higher than we previously expected.

While there are still a lot of challenges ahead, we believe that to use the mobile technology in insurance sales is a trend of our time, in alliance with the direction of the insurance industry's transition. We are proud that we are the first one to adopt mobile technology at [non-insurance] intermediaries in China, and are able to balance that from the first mover advantage.

We are strongly committed to implementing our e-commerce strategy, with mobile support system a top priority, while exploring opportunities to grow B2C and B2B2C business.

Looking ahead to the second half 2013, we will accelerate sales of CNpads in more regions, strive for extending the operation of the mobile sales support system in all of our P&C subsidiaries in major cities by the end of October, and achieve the annual sales target of 5,000 units for 2013.

On system development front, we will focus on improving user experience by simplifying data input process and enhancing backend processing capacity, including improving quotation accuracy. In the meantime, we will start working on developing modules to enable broader range of products available through CNpad, including non-auto P&C products, life insurance and wealth management products.

Apart from that, we also plan to moderately allocate resources to [refine] our B2C website. We expect to complete a system upgrade by the end of the year. In the meantime, we expect to broaden our product offerings on the website and launch product-specific promotional activities in a small scale in order to improve staff, agents, and direct customers' awareness of the website. And meanwhile, we are also preparing to open a flagship store on China's largest retail e-commerce website, taobao.com, by the end of the year.

Since early 2012, when we began offering wealth management products to our clients, we have seen a rapid growth in customers and sales volume, while extending our [marketing spend]. As of the end of the second quarter 2013, we had established financial planning studios in key cities of six provinces, boosted the number of wealth management customers, increasing by 530 to over 1,800, and the value of wealth management products we distributed exceeding CNY240m during the second quarter of 2013.

While we offer wealth management products to meet customers' need for asset accumulation, during the second quarter we shifted our focus for life insurance products back to protection products to address our customers' specific demand for protection. Under this framework we have been proactively exploring new product opportunities by selling healthcare fund in Beijing and Shanghai, promoting retirement programs and cooperating with insurance companies and brokers on product design, such as cancer insurance and short-term consumption-type protection and products, etc.

In order to support our strategy to build comprehensive financial service platform and promote the adoption of e-commerce technology, as well as improve operational efficiency and cut operational costs, we've decided to push forward in organizational integration, which ends at integrating our various business units into one unified platform.

First of all, three of our business units, namely P&C insurance business unit, Life Insurance business unit and E-commerce business unit will be restructured into three product line divisions under the CNinsure insurance sales service group.

Secondly, the [partly] functional departments of this business unit, such as administration, human resources, finance, business management and operational management departments will be merged and centrally managed at the headquarter.

Thirdly, subsidiaries that were actively engaged in P&C insurance and life insurance distribution will then be -- will be merged together to establish one unified operational and management platform in order to reduce the operational cost of this subsidiary and enhance the efficiency.

Fourthly, we will provide both P&C and life insurance sales agents [same] access to a wide range of product offerings, including life insurance, P&C products and technology support so as to help them earn more money in a more cost-effective and productive way. We believe all these moves are imperative to the rollout of our strategy to develop comprehensive financial services and promote the adoption of technology in the future.

All these initiatives will reflect our commitment to continuously enhance our core competence, which we believe will prepare us well for a strong rebound and long-term sustainable growth.

With that, I will turn the call over to our CFO. Thank you.

Peng Ge - CNinsure Inc. - CFO

(Interpreted). Thank you. Hello, everyone. I'm pleased to report our financial results for the second quarter of 2013.

Our total net revenue for the second quarter 2013 recorded a growth of 2.8% year over year. The slowdown in growth rate was primarily due to a drop of 30.5% year on year in net revenue from life insurance business, primarily as the result of a decline in new business premiums. The drop in new business premium was mainly because we adjusted our sales focus from participating policies to traditional policies -- to traditional protection policies, which generally generate lower per-policy premiums.

While number of new policies sold during the quarter was flattish as compared to a year-ago quarter, reflecting a stable sales capability of life insurance sales team, there were other delays on customers' expectations after pricing deregulation for traditional life insurance products as it is believed that premium will drop once the pricing is liberalized.

The growth of recurring premiums remained at strong momentum, with over 31% growth year over year, partially attributable to a high 13-month persistency ratio of over 80%. As a whole, the total life insurance premium in the second quarter recorded a slight increase as compared to the corresponding period of 2012.

Total net revenues of our P&C insurance segment grew 10.9% from the year-ago quarter. And our claims adjustment business maintained a healthy growth, with net revenue for second quarter up 14.6% year over year, mainly attributable to the robust growth of the auto-related business.

Total operating cost and expenses for the second quarter 2013 was up 7.4%.

Commissions and fees expenses for the second quarter 2013 was up 17.6% from the year-ago quarter, primarily reflecting rising labor cost and rising auto commission rate that we pay to our sales agents as a result of the increased market competition.

Selling expenses for the second quarter 2013 was up 16.1% from the year-ago quarter. The increase was primarily due to increases in office, gasoline and vehicle expenses incurred by the claims adjusting segment.



General and administrative expenses for the second quarter 2013 were down 20.2% from the year-ago quarter, primarily due to decreases in share-based compensation expenses related to certain options granted on March 12, 2012, which are required to be recognized on an accelerated basis. And such expenses are expected to decrease each year, since the [grant].

Interest income for the second quarter 2013 was down 9.5% from the year-ago quarter. The decrease in interest income was primarily due to a decrease in bank interest rates from the corresponding period in 2012 and a decrease in the bank deposits. As we increase short-term investments, the aggregate value of the third party products that we invested in was approximately CNY233m.

Income tax expenses for the second quarter 2013 was down 59.7% from the year-ago quarter.

As a result of the foregoing factors, net income attributable to the Company's shareholders for the second quarter 2013 was down 36.3% from the year-ago quarter.

As of June 30, 2013, the Company has CNY2.3m in cash and cash -- CNY2.3b in cash and cash equivalents.

CNinsure expects its total net revenue to grow by approximately 5% for the third quarter of 2013 compared to the corresponding period in 2012. This forecast reflects CNinsure's current view, which is subject to change.

Thank you.

Oasis Qiu - *CNinsure Inc. - IR Officer*

Now our CEO, Mr. Wang, and our CFO, Mr. Ge, will open the floor for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). And your first question comes from the line of Richard Safranek of Wafra Investment. Please ask your question.

Richard Safranek - *Wafra Investment - Analyst*

Hi. Thank you for the call. My question was just regarding the share buyback that was initiated last November, the \$30m share buyback. How much of that \$30m share buyback was actually executed?

Peng Ge - *CNinsure Inc. - CFO*

(Interpreted). We were authorized by the Board to buy back a maximum amount of 30m shares in open market. And we have tried buying shares during the window period. And we bought a total of -- ADS with a total value of \$1.5m. And so far we haven't continued buying back shares because -- due to the low liquidity of our stocks and also because the restriction by the SEC on insider trading. It's very difficult for us to buy as much shares as we want.

Richard Safranek - *Wafra Investment - Analyst*

Have you thought of other ways of returning capital to shareholders?



Chunlin Wang - *CNinsure Inc. - CEO*

(Interpreted). We will consider from both long-term and short-term perspective. From long-term perspective we think that it's important to return the cash to our shareholders and to actually return a long-term value to them. And the organization integration and also our strategy to develop financial business and also to bring more technology into our business is actually the initiative that we would like -- want to prepare for, to bring CNinsure back to a long-term strong growth, and which we think actually is [predictable] within the next couple of years. And this is a better way to return to our shareholders a long-term value.

And then secondly, from a short-term perspective, we will balance our capital requirements for business growth, as well as the interest of the shareholders. And of course, we will also need to submit this observation to our Board for consideration to make a reasonable way to return to our shareholders.

Richard Safranek - *Wafra Investment - Analyst*

Well, yes. Unless you're going to make an acquisition, it seems to me that your net cash balance is so large that it's more than capable of supporting whatever growth initiatives you have, as well as returning a significant amount of that capital to shareholders. You highlight your significant net cash position in your press release. But it's just sitting there.

And if your numbers are to be believed, it's sizeable, and it should be supportive of your growth initiatives as well as returning a significant amount to shareholders, whether it's through a special one-time dividend or a more meaningful and genuine share buyback than what was previously executed. It just really sort of beggars belief that you need to sit there with that much cash. That's all I have to say. Thank you.

Peng Ge - *CNinsure Inc. - CFO*

(Interpreted). As Mr. Wang mentioned just now, our strategy is to develop a comprehensive financial services business as well as to develop our e-commerce business. And as everybody knows, e-commerce development requires a huge investment, as we have seen in many other peers.

And as for the comprehensive financial services, it is actually a golden time for companies like our size to explore in this sector. And we would like to keep looking for new opportunities, and there have been actually a lot of business opportunities. And we would either look for new targets or seeking opportunities to increase our shareholdings in those companies that we already own minority interest.

And also we are seeing the government is holding a more open-minded attitude towards opening the market further and they might loosen up the license issuance a little bit. So we would need to evaluate how much capital we will need to invest in this area to explore these new opportunities.

As for share buyback, it is true that we want to have more meaningful share buyback. However, due to the SEC's restriction on our daily trading volume and also on the bidding price, it is very difficult for us to buy as much as we wanted that I mentioned just now. So it is not how much money we would like to commit to, it is the actual restriction that we are subjected to. So we would like to see how much we can buy and how exactly this share buyback can boost our stock price performance. But having said that, we will submit that consideration to our Board for their consideration.

Richard Safranek - *Wafra Investment - Analyst*

Okay. Thank you. I guess my last question is, again, just closing this perceived valuation discount, have you considered maybe getting a dual listing in Hong Kong? You're kind of an orphan stock here. You don't have a lot of credibility and you aren't followed too widely by the analyst community. Maybe you're misunderstood by the investment community here in the US and you might be better served by getting a listing in Hong Kong, if you can get a listing in Hong Kong. Have you considered a dual listing structure?

Chunlin Wang - *CNinsure Inc. - CEO*

(Interpreted). We will strictly follow and keep compliance with the SEC requirements and regulations on disclosure. If we ever have such kind of plans or decision, we will disclose to the market.

Richard Safranek - *Wafra Investment - Analyst*

Okay. Great. Thanks.

Oasis Qiu - *CNinsure Inc. - IR Officer*

Thanks.

Operator

And your next question comes from the line of [Arthur Ho] of [Halco]. Please ask your question.

Arthur Ho - *Halco - Analyst*

Thank you. Two questions. In the fourth quarter last year you indicated that the P&C business margins were bottoming and would start to improve. That hasn't happened in the first two quarters. Would you expect that to happen in the remainder of the year and into next year? Your margins are currently at a level of about 26% versus about 50% several years ago.

Second question. What is the difference in the interest income between your cash holdings and the increased holdings of short-term investments? Thank you.

Peng Ge - *CNinsure Inc. - CFO*

(Interpreted). First of all, for this quarter our P&C gross margin was about 25.7% as compared to over [30%] last year quarter. But if we compare it sequentially, compare with the first quarter and the fourth quarter of last year, the gross margin for P&C was flattish. And remember the gross margin for first quarter was also 25 something, so basically in line with expectation.

Chunlin Wang - *CNinsure Inc. - CEO*

(Interpreted). But an additional comment from our CEO, Mr. Wang, is that we had originally expected the gross margins should be bottomed out in November. However, the development market evolved a little bit differently from what we anticipated and it's mainly due to the competition in the P&C market getting more exacerbated. As we can see from the performance of a lot of insurance -- P&C insurance companies, and they have suffered from underwriting loss. 70% of this company has suffered underwriting loss in the first half this year.

So in this environment -- under this environment we are still able to maintain a relatively stable gross margin, so that is [thankful] to the fundamental work that we have done last year. And we expect that our gross margins should be able to see a slight increase by the fourth quarter or early next year.

Peng Ge - *CNinsure Inc. - CFO*

(Interpreted). And Mr. Ge would like to answer your second question as to the different trend in interest income and short term investment. Previously most of our cash are put into the bank as [CD] with the annual returns of 2.5%. However, we are expecting that a further decrease of



interest rate will be the trend in the future. And there are a lot of wealth management products available with a relatively high return, so we invested some of our cash into the short-term wealth management products. But our investment policy is very conservative and those products are [comparatively] low risk and with a return of about 6% to 8% annual [use].

And on accounting front, we will recognize the return, the use of those -- on those investment products as it happens and rather than accrue the returns on a quarterly basis. So that's why you have seen a decrease in our interest income. But when the -- when we get the [use], you will see the interest income to increase.

Thank you.

Arthur Ho - *Halco - Analyst*

Thank you.

Operator

And your next question comes from the line of Patricia Cheng of CLSA. Please ask your question.

Patricia Cheng - *CLSA - Analyst*

(Interpreted). This is Patricia Cheng from CLSA and she has two questions regarding to our business. And this question is with regards to the gross margin, as we mentioned that our P&C gross margin will have a rebound, probably in the fourth quarter or next year, and Patricia is asking what will be the drivers. Is it due to a decrease in the commission that we pay to our sales agents or an increase of the commission that we receive from insurance companies? So to -- or to simply put, is it because we are able to negotiate with the insurance companies for better terms?

And then the second question is with regarding our expectation of revenue growth for the third quarter, which is 5% growth, what will be the drivers for the growth?

Chunlin Wang - *CNinsure Inc. - CEO*

(Interpreted). As mentioned just now, over 70% of P&C insurance companies have been suffering from underwriting loss. And this is not tolerated by the CIRC as well as the shareholders of this insurance company. And according to the message that I have got from the regulator and the insurance company, we believe that the competition -- the price competition in the P&C market will ease up gradually and the market will be more rationalized. And we believe that we can actually benefit more from this more regulated and better -- more rationalized market.

And over the past decade we have actually seen that the P&C market has kind of a cycle which comes from -- which begins from an underwriting loss and then the market becomes more rationalized, and then the insurance company become more profitable and then it begins competing for market shares again and initiate price competition, which results in another underwriting loss. And then the market becomes rationalized again.

So we believe that the market will probably follow that cycle again. And at this time and point we believe that the price competition has come to a point that neither the regulator and insurance company can tolerate anymore. So I am quite -- this is why I feel confident about the prospect in the P&C market.

And then secondly, we believe that the organization integration that we would like to push forward will help slow down the cost increase or even stabilize our cost increase. And then also, with the integrations, our P&C agents and life agents will have more opportunities to cross sell products and which will help them to boost their revenues as well as our revenue.



Peng Ge - *CNinsure Inc. - CFO*

(Interpreted). And then to come to your second question, our 5% net revenue gross expectation, and we believe that this target should be achievable based on our expectation that life insurance -- there is very limited room for our life insurance new business to go down further. And for this quarter our new business -- new life insurance business decreased by 30%. And I believe for the third quarter the new life business should be -- the decrease should be no higher than 15%.

Oasis Qiu - *CNinsure Inc. - IR Officer*

Thank you, Patricia.

Operator

And your next question comes from the line of Andy Nahas of Prospect Fund. Please ask your question.

Andy Nahas - *The Prospect Fund - Analyst*

Yes. Thank you. You were talking earlier about using the cash on the balance sheet to grow the business, and that is the best way to use the cash is to grow the Company in the future. I wanted to know how many times bigger or how big in annual revenue do you think CNinsure will become in the very long run without acquisitions and why?

Chunlin Wang - *CNinsure Inc. - CEO*

(Interpreted). We expect our annual revenue should be growing by double digits in 2014.

Andy Nahas - *The Prospect Fund - Analyst*

Okay. I guess I'm thinking more longer term than that. How big an annual revenue do you think this Company will become in the long run, and without acquisitions, and why do you think that?

Chunlin Wang - *CNinsure Inc. - CEO*

(Interpreted). I think it's foreseeable that we will be able to maintain a double-digit growth for at least five years, starting from 2014.

Andy Nahas - *The Prospect Fund - Analyst*

Okay. And then the other question I had is you have a website and you have sales agents, and what I'm wondering is how important is the website for generating revenues for the Company? What is the purpose of the website, or is it really the sales agents generating the revenues?

Chunlin Wang - *CNinsure Inc. - CEO*

(Interpreted). To be honest, this is the website -- the contribution from this website is still limited as e-commerce development requires huge investment in marketing and advertising. However, we are -- we believe that the timing for the B2C markets are still not ready, so that's why we are putting the marketing and advertising and so before we actually see the opportunities coming.



Right now, at this stage, we're maintaining the website operations and keep looking for opportunities. And the entry point for us to explore the e-commerce opportunities is the mobile technology, based on the fact that right now the mobile technology is the trend of our time and also based on the advantage that we already have, which is a large number of sales force. So we are using this mobile technology to help our agents to increase their productivity, their efficiency and allow them to sell more products to through their CNpads.

Right now, we are still perfecting the technology of the system. And we believe that the contributions -- we will see more meaningful contribution from this area in the next years.

And I would like to share with you to highlight when we promote the use of our CNpad among our sales agent. First of all is the per-unit productivity. As we originally expected, the annual per-unit productivity should be around 300,000. However, based on the results in the second quarter, so far we have sold over 480 units of CNpad. And a per-unit productivity has actually -- getting close to 500,000, so which is much higher than we originally anticipated.

And then secondly, based on the feedback from the sales agents who has been using CNpad, and they feel that CNpads do help them a lot and they feel -- more rely on CNpad to conduct their business.

Right now we are still controlling the pace of sales of CNpads while we are working on perfecting the technology and broaden -- continue to broaden the product offerings available to CNpad to make sure that our agents have better using experience.

Andy Nahas - *The Prospect Fund - Analyst*

Okay. And one last question. Over the next five years, what area will be the biggest growth driver for you? Will it be property casualty? Will it be life insurance or wealth management, do you think?

Chunlin Wang - *CNinsure Inc. - CEO*

(Interpreted). I think we can summarize our drivers for the next five years in three words. First, through phases. First is the comprehensive financial services, which consist of a wide range of products including life insurance, P&C insurance, wealth management products. And we describe those comprehensive financial services as a nuclear weapon.

And then the second driver is the e-commerce business, and we regarded as kind of a missile weapon for us.

And then thirdly, the organizational integration which enables us to integrate our various business units which used to be operated separately into a unified platform. And we regard this as a kind of an aircraft carrier for us. So these will be the three drivers.

Andy Nahas - *The Prospect Fund - Analyst*

Okay. Thank you.

Oasis Qiu - *CNinsure Inc. - IR Officer*

Thanks.

Operator

Thank you. Ladies and gentlemen, as there are no further questions, that does conclude our conference for today. Thanks for participating. You may all disconnect.



Editor

Portions of this transcript that are marked (interpreted) were spoken by an interpreter present on the live call. The interpreter was provided by the Company sponsoring this Event.

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