CNFinance Holdings Limited
Q4 and FY2020 Financial Results Conference Call
Tuesday, March 16, 2021 08:00 AM ET.

Executives:
Jane Jenn, Investor Relations
Bin Zhai, Chairman and Chief Executive Officer
Li Ning, Executive Director and Chief Financial Officer

Analysts:
William Gregozeski, Greenridge Global
Neil Gagnon, Gagnon Securities.

Presentation

Operator: Good day and welcome to the CNFinance Report for the Fourth Quarter and Fiscal Year of 2020 Financial Results Conference Call. All participants will be in listen-only mode. [Operator Instructions]. After today's presentation, there will be an opportunity to ask questions. Please note that this event is being recorded.

I would now like to turn the conference over to [Jane Jenn]. Please go ahead.

Jane Jenn: Good morning and good evening. And welcome to the CNFinance fourth quarter and fiscal year 2020 financial results conference call. In today's call, our CEO, Mr. Zhai, will walk us through the operating results, followed by the financial results from our CFO, Mr. Li. After that, we will have a Q&A session.

Before we start, I would like to remind you that this conference call contains forward-looking statements within the meaning of Section 21E of the Securities and Exchange Act of 1934 as amended, and as defined in the U.S. Private Securities Litigation Reform Act of 1995. These forward-looking statements can be identified by terminology such as will, expects, anticipates, future, intends, plans, believes, estimates, target, going forward, outlook and similar statements.

Such statements are based upon management's current expectations and current market and operating conditions, and relate to events that involve known or unknown risks, uncertainties, and other factors, all of which are difficult to predict and many of which are beyond the company's control, which may cause the company's actual results, performance or achievements to differ materially from those in the forward-looking statements.

Further information regarding these and other risks, uncertainties or factors is included in the company's filings with the U.S. Securities and Exchange Commission. The company does not undertake any obligation to update any forward-looking statements as a result of new information, future events or otherwise, except as required under law.

Now, please welcome our CEO, Mr. Zhai.

Bin Zhai: (Speaking foreign language).

(Translated). Thank you all for joining our call today. We would like to report on the business operation, business development and financial results in the fourth quarter and fiscal year of 2020. During the year, the outbreak of COVID-19 presented both challenges and opportunities to our business. However, CNFinance was able to maintain operation, and continued to create value to our shareholders while ensuring the health and safety of our employees, partners and clients. Later, we will answer your questions.

During the fourth quarter, we facilitated loans amounting RMB2.7 billion, representing an increase of 35% from the same period of 2019. The revenue and net income were RMB420 million and RMB105 million respectively during the quarter. For the fiscal year of 2020, we facilitated loans amounting RMB8.8 billion, representing an increase of 40% as compared to 2019.

We recorded revenue of RMB1.84 billion and a net income of RMB115 million. These results are strong proof of the effectiveness and efficiency of the Collaboration Model, and they also further increased our confidence in growing this model in the future.

2020 was a special year. It was the second year of our transformation to the Collaboration model. Since 2019, we had started a smooth transition from the old model to the current Collaboration Model. In 2020, we refined the Collaboration Model, which proved its capability to overcome obstacles brought up by the changing environment of business.

At the beginning of 2020, COVID-19 spread throughout China and later, the entire globe. China's national production and business operation during February and March was halted. As a result, we hardly facilitated any loans during that 2 months. Our delinquency ratio also increased drastically in the first quarter. At that moment, we endured the pressure. We were also fortunate to benefit from the advantages of our collaboration model implemented in 2019.

Under the pressure, we quickly responded and initiated communications with sales partners, as well as trust company partners, to develop action plans. We implemented modifications to improve product terms, loan approval process and post-loan management, all in an effort to provide financing services to meet MSE owners' most urgent needs.

After a whole year of adjustment into the collaboration model in 2019, we were able to cut down fixed cost drastically. The collaboration model also made us resilient when facing unexpected difficulties, since we share profit and bear risks with our sales partners. We were able to keep a 100% recovery rate when we experienced the rise of delinquency and NPLs.

In the second half of 2020, the government ordered the financial institutions to lower financing cost to the economy. Subsequently, our industry took another hit from the new order of the Supreme People's Court on interest rates. As we collaborate with licensed trust companies, we are not subject to this new court order. However, we proactively communicated with our funding partners and sales partners and reduced the interest rate of our loan products to follow the court order.

This decision presented us with both challenges and opportunities. The reduced interest rate impacted our interest income. It also created problems in deposing NPLs. In response to these issues, we started negotiations with trust company partners and sales partners in order to assure profit margins for all 3 parties and were still obliged to the court order.

Even the adjusted profit margin became lower for all parties. The increasing demand for our loan products helped boost the origination volume in third and fourth quarter of the year. The loan origination volume doubled in the second half of the year as compared to the first half, and was 57% higher than the same period in 2019. In 2021, we believe that the interest rate on our products will gradually recover to a higher rate, but still comply to the regulations.

In November, the government rolled out regulations to limit the scale of non-standard products issued by the trust companies. In order to satisfy the massive demand of prospective borrowers, we proactively started collaboration with new financial institutions such as Hu Nan Trusts and Lan Hai Bank. These new collaborations not only provided us sufficient funds, but also strengthened the trust between the sales partners and our platform with sufficient funding. Our financing service continued to meet the most urgent needs of MSE owners.

During 2020, we have overcome many challenges and facilitated loans amounting RMB88 billion, representing 40% increase from the year before. Our Collaboration Model and new loan products were also approved by the market. Also, in 2020, the number of contracted sales partners grew to 1,700 from 1,300, representing an increase of 31%.

From our experience in 2020, the Collaboration Model has proved its efficiency and effectiveness. CNF is more confident to further build our business under this model.

Report on the Work of the Government in 2021 has addressed on the continuity in providing financial solutions to MSEs, and this decision is exactly what CNF has been dedicated to. In 2021, in order to better service our customers and sales partners, and reach our set goal of exceeding RMB10 billion in outstanding loans under the Collaboration Model, we will invest more on technology and focus on refining our operation.

Our plans are: First, we will roll out diversified products. Based on the borrowers' credit reports, we will match them with financial institutions with different risk preferences. Other than our current trust loan products, we plan to introduce new trust loan products with interest rates ranging from 20% to 22% for class C customers, implying they have poorer credits compared with class A and B applicants. We also plan to cooperate with large banks to design loan products with interest rate of no more than 10% for class A customers.

Second, we will provide tailor-made terms with our sales partners based on the volume and quality of assets they introduced to our business. These new adjustments will incentivize them to achieve even higher efficiencies in our model. CNF also expects to capture a bigger market share in our industry.

Third, we will refine the platform operation. We will empower our business through technology, including a smarter and faster approval procedure, data integration, process visualization and other technological means in order to provide timely service in every business process. We will also improve the service quality and efficiency of the document signing and the post-loan management.

We believe that after striving through the challenging 2020, the company will continue to improve itself and seize every opportunity to create higher value for shareholders in 2021.

Now I would like to hand the call over to our CFO, Mr. Li Ning, who will walk you through the financial results of fourth quarter and fiscal year of 2020. Thank you.

Li Ning: Thanks, Mr. Zhai, and thanks again to everyone for joining us today. I will walk you through our fourth quarter of 2020 financials, followed by that of fiscal year of 2020. We believe year-over-year comparison is the best way to review our performance. Unless otherwise stated, all percentage changes I'm going to give will be on that basis. Also, unless otherwise stated, all numbers I'm going to give will be in RMB.

Total outstanding loan principal was RMB9.7 billion as of December 31, 2020, as compared to RMB11.3 billion as of December 31, 2019.

Total loan origination volume was 2.7 billion during the fourth quarter of 2020, representing an increase of 35% from 2 billion.

Interest and financing service fees on loans decreased by 29.5% to RMB417.1 million for the fourth quarter of 2020 as compared to RMB591.8 million, primarily due to the combined effect of, first, the decrease in the balance of average daily outstanding loan principal, and second, the lowered interest rate on loans facilitated in an effort to comply with recent rules and regulations issued by relevant PRC regulatory authorities, including the Decisions of the Supreme People's Court to Amend the Provisions on Several Issues concerning the Application of Law in the Trial of Private Lending Cases issued in August 2020.

Interest and fees expenses decreased by 32.7% to RMB159.3 million for the fourth quarter of 2020 as compared to RMB236.8 million, primarily due to the decrease in the principal of the borrowings under agreements to repurchase and other borrowings.

Collaboration cost for sales partners, representing sales incentives paid to sales partners, increased to RMB104.4 million for the fourth quarter of 2020 as compared to RMB75.8 million, primarily due to the increase in average daily outstanding loan principal under the collaboration model since December 2018.

Provision for credit losses decreased by 171.6% and recorded a reversal of RMB28.5 million for the fourth quarter of 2020 as compared to the provision of RMB39.8 million for the same period of 2019. The decrease was mainly attributable to the combined effect of, first, the decrease in loan balance; and second, the increase in outstanding loan principal under the collaboration model that was guaranteed by Credit Risk Mitigation Position put up by the sales partners; and third, the current expected credit loss model adopted since 2020 took into account the containment of COVID-19 pandemic, which led to positive overlook of economy growth in China as compared to the same period of 2019.

Total operating expenses decreased by 31% to RMB112.6 million for the fourth quarter of 2020, compared with RMB163.1 million.

Income tax expenses increased by 4.8% to RMB24.2 million for the fourth quarter of 2020 as compared to RMB23.1 million, primarily due to the increase in taxable income for the fourth quarter of 2020.

Net income increased by 72.6% to RMB105.3 million for the fourth quarter of 2020 as compared to RMB61 million.

Now let’s move on to the financials of 2020 as a whole. Total loan origination volume was 8.8 billion during the fiscal year of 2020, representing an increase of 39.7% from 6.3 billion in 2019.

Interest and financing service fees on loans decreased by 38.1% to RMB1,828.7 million for the fiscal year of 2020 as compared to RMB2,953.5 million for the same period of 2019, primarily due to the combined effect of, first, the decrease in the balance of average daily outstanding loan principal, and second, the lowered interest rate on loans facilitated in an effort to comply with recent rules and regulations issued by relevant PRC regulatory authorities, including the Decisions of the Supreme People’s Court to Amend the Provisions on Several Issues concerning the Application of Law in the Trial of Private Lending Cases issued in August 2020.

Interest and fees expenses decreased by 44.2% to RMB731.3 million for the fiscal year of 2020 as compared to RMB1,309.8 million for the same period of 2019, primarily due to the decrease in the principal of the borrowings under agreements to repurchase and other borrowings.

Collaboration cost for sales partners representing sales incentives paid to sales partners increased to RMB415.1 million for the fiscal year of 2020 as compared to RMB174 million for the same period of 2019, primarily due to the increase in average daily outstanding loan principal under the collaboration model as compared to the same period of 2019.

Provision for credit losses decreased by 22.8% to RMB280 million for the fiscal year of 2020 as compared to RMB362.8 million for the same period of 2019. The decrease was mainly attributable to the combined effect of, first, the decrease in loan balance; second, the increase in outstanding loan principal under the collaboration model that was guaranteed by Credit Risk Mitigation Position put up by the sales partners; and third, the current expected credit loss model adopted since 2020 took into account the overlook of the economy growth in China impacted by the COVID-19 pandemic.

Total operating expenses decreased by 16.1% to RMB445.3 million for the fiscal year of 2020 as compared to RMB531 million for the same period of 2019.

Income tax expenses decreased by 74.4% to RMB47.8 million for the fiscal year of 2020 as compared to RMB186.4 million for the same period of 2019, primarily due to the decrease in the amount of taxable income.

Net income decreased by 78.5% to RMB114.9 million for the fiscal year of 2020 as compared to RMB534.6 million for the same period of 2019.

As of December 31, 2020, the Company held cash and cash equivalents of RMB2.0 billion, compared with RMB1.7 billion as of December 31, 2019.

The aggregate delinquency rate for loans originated by the Company, which is calculated by dividing the total balance of outstanding loan principal for which any installment payment is past-due for one or more days as of a particular date, by the aggregate total amount of loans we originated since 2014, increased from 5.4% as of December 31, 2019 to 5.7% as of December 31, 2020.

The actual delinquency rate for loans originated by the Company increased from 17.1% as of December 31, 2019 to 22.6% as of December 31, 2020.

With that, I would like to open the Q&A session. Please go on.

Questions and Answers

Operator: We will now begin the question-and-answer session. [Operator Instructions]. William Gregozeski from Greenridge Global.

William Gregozeski: A couple of questions. You mentioned the new products for Class A, B and C applicants. Do you have an estimate of what kind of split each of those 3 categories are going to make going forward?

Bin Zhai: (Speaking foreign language).

(Translated). The products we have right now are more singular to those so-called Class B products. In the foreseeable future, say, 2021, I think the current products are still going to be our name products. As we still cooperate with trust companies to build out the products for Class B customers, I think that's going to be easier to roll out. And we are hoping to roll that out in the second quarter in 2021.

Also, since those products for Class B customers I mentioned before also the involve the problems with cooperating with sales partners, we will have to say if the sales partners are willing to accept those kind of new products. So as long as we're concerning the 2021, I think we're still going to use the products for Class B customers as the main product, and product for Class C customers as supplement.

Not really going to push out any product for Class A customers in the near future as 2021, since the product for Class A customers is going to be a brand-new product, the target customer group is going to be a little different from what we're having right now. So it's brand-new to the company, it's going to be a new journey. We are starting the negotiation process with the banks in the second quarter, and with the hope to start to roll out the product for Class A customers in about [half a year] with scale.

As I mentioned earlier, because the target customer groups are different, so we don’t really think it's going to make up a large percentage of our products in 2021. It's more like to build a solid foundation for our future development. That's my answer to your question.

William Gregozeski: Okay. All right, great. Do you think the global interest for the sales partners will increase with the -- you mentioned a tiered offering. Do you think that will make the existing sales partners more active, and possibly bring in new sales partners onto the platform?

Bin Zhai: (Speaking foreign language).

(Translated). My answer is simple -- yes. I will illustrate the following aspects. First, as I mentioned, as we are pushing out products to satisfy different classes of customers, it gives the sales partners more choices. Second, as we are refining our platform, I think we're going to be able to provide them with better services. And as we are refining our services, I think it will be possible also to transform, say, a customer from Class B to Class A. And I think that's going to expand our customer base as well. And I hope that answers your question.

William Gregozeski: Okay. And the last question is, it seems like the average loan size has been going up over the course of 2020. Do you think that will continue on into 2021?

Bin Zhai: (Speaking foreign language).

(Translated). We believe the average ticket size is going to be maintained in a rather steady level. And in 2020, even though we've been through the COVID-19 pandemic, the overall property price in China was still rising a little bit slightly. Because we're holding a very stringent [cape] of LTV to the 70% of the collateral value, as the market price of the property goes up, our average ticket size also goes up. Besides, as the loans were facilitated, gathered across the cities, each city may take a different percentage of our total -- of our whole picture; while that change is going to influence the average LTV as well. But just all in all, the LTV didn’t really change that much, and so does the average ticket size.

William Gregozeski: Okay. All right. Thank you.

Operator: [Operator Instructions]. Neil Gagnon from Gagnon Securities.

Neil Gagnon: First of all, let me congratulate you on getting through 2020. You did it very well, and all of your team is to be congratulated.

Bin Zhai: Thank you.

Neil Gagnon: My first question is management's thinking about balancing growth and profitability, given that it seems as if you have almost unlimited opportunity if you want to go after it. So what's the balance between how fast you want to grow, and what kind of profitability you'd like to achieve?

Bin Zhai: (Speaking foreign language).

(Translated). [Looking] through the fluctuations in the market condition during the year, as I mentioned earlier, one of the fluctuations was the COVID-19 pandemic. We also experienced the Supreme People's Court order to limit the cap of private landings. And the interest we charge our customers make up the main percentage of our revenues.

And our profit margin is mainly made up by our -- the interest difference between what we charge the customers and what we pay to the trust companies. And the sales partners mainly -- their revenue is made up by the interest we charge our customers and the interest we charge them. So in the past year, first, the income of our prospective customers has dropped as compared to past years.

However, to respond to the fluctuation of the market, we also adjusted our process a little bit with our sales partners. For example, once the overall interest we can charge the customer dropped, it's not only beared by us, but rather, by the joint party of us and the sales partners. So the incentive we paid to the sales partners are usually not as sensitive as what we charge from the borrowers. When there is a change, it's usually smaller.

After a whole year of adjustment, I think the profits that we are having with our sales partners right now has reached a rather steady level. So based on that, I don’t think to scale up is really conflict with remaining the profitability, but rather, it's a linear coalition. So our main focus in the future is to get a more economic financing cost from the trust company partners. So I think that will be the main driver of our profitability. So if we can get the financing cost to be stable, our profit margin will [be] stable as well. I hope that answers your question.

Neil Gagnon: Yes, it does. Thank you. And that was a very good explanation. If you achieve those kinds of levels, of course, there are no guarantees in life, but if you achieve them, what is the thinking about getting to share some of the profitability with your shareholders in the form of a cash dividend?

Bin Zhai: (Speaking foreign language).

(Translated). That's always in our daily schedule of consideration. But we will also mutually consider our revenue, profitability, liquidity before we put that into the Board meetings for discussion. Thank you.

Neil Gagnon: Thank you. That was a complete answer, I appreciate it. Thank you very much.

Operator: We have no more questions in the queue. This concludes our question-and-answer session. I'd like to turn the conference back over to [Jane Jenn] for any closing remarks.

Jane Jenn: That will be all for today. Thank you for joining us. If you have any further questions, please free to contact us at ir@cashchina.cn. Thank you.

Li Ning: Thank you.

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