OneConnect Financial Technology Co., Ltd.

SEHK:6638

Earnings Call

Monday, March 13, 2023 12:00 PM GMT

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Call Participants

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Chairman of the Board & CEO

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Presentation

Operator

Hello, everyone, and welcome to the OneConnect Financial Technology Fourth Quarter and Full Year 2022 Earnings Release Call. My name is Bruno and I will be operating your call today. [Operator Instructions] I will now hand over to your host, Danielle Gao, Head of Investor Relations. Please go ahead.

Danielle Gao
Head of Investor Relations

Thank you, operator. Hello, everyone, and welcome to our 2022 first quarter and full year earnings conference call. Our financial and operating results were released earlier today and are currently available on our IR website. Today, you will hear from our Chairman and CEO, Mr. Shen Chongfeng, who will give opening remarks and the business highlights. Afterwards, our CFO, Mr. Luo Yongtao will offer a closer look into our financials. And then in question-and-answer session, our management team will be available to you. We have our CTO, Mr. Li Jie, Head of Digital Banking, Ms. Ellen Jia; and the Chief Executive of Ping An OneConnect Bank, Mr. Michael Fei.

In today's conference, our management team will make statements in Mandarin or in English. For those in Mandarin, a consecutive translation will be provided. If any discrepancy, our statement in our original language will prevail. Let me quickly cover the safe harbor statements before we start, as we will be making forward-looking statements, which involve a number of risks and uncertainties that could cause actual results to differ materially. Please note that we may present both IFRS and non-IFRS financial measures. So with that, I'm now pleased to turn the call to our Chairman and CEO, Mr. Shen Chongfeng. Mr. Shen, please.

Chongfeng Shen
Chairman of the Board & CEO

[Interpreted] Hello, everyone. Thank you for taking the time to join OneConnect 2022 Q4 and a full year earnings release.

Economic headwinds in 2022, had been a challenge to all technology companies. Despite impact on parts of our businesses, we still achieved solid growth in our results. Revenue from third-party customers reached CNY 1,478 million full year, representing a year-over-year growth of 6.5%. Premium plus customers increased by 9 year-over-year to 221. Significant improvement in operational efficiency also narrowed our losses by a big margin.

Next, I will share with you OneConnect business development in Q4 and 2022 full year. You can go to Page 3 of our slide. 2022 was a crucial year for broadening customer engagement in our Stage 2 strategy. Now could you please go to Page 4.

In our second stage, we continue to execute One body two wings initiative that is focusing on financial institutions while expanding ecosystem and overseas. Next, please go to Page 5. This year, we continued product innovation and upgrade efforts in digital banking, digital insurance and Gamma platform and released over 100 new product versions. As a result, we saw higher efficiency in consideration for customized demand as well as greater coverage of business scenarios.

In digital banking, we updated our cloud-native-based banking system 2.0. The latest version comes with over 400 APIs and is fully adapted to self-controlled technology. In digital insurance, we collaborated with a global top 50 insurers in the Omni-channel agent solution project, which also marked our first success with this product.

In Gamma platform, we continued to upgrade product scenario loads and features in AI customer services and had achieved multiple technological breakthroughs in key functionality such as multimodal machines, human robot collaboration as well as dialogue analysis insights.

Thanks to OneConnect's continuous product innovation capability, customer recognition is also improving. In

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2022, our new products have demonstrated strong momentum in revenue, new customer acquisitions and customer stickiness.

Next on Page 6. Home developed technologies or self-controlled technologies have become an important investment for financial institutions in recent years. OneConnect products and integrated solutions fully accommodate home developed technologies. All our products in 3 business segments are 100% adaptive to meet customers' demand in this front.

At the same time, leveraging finance experience in self-controlled IT, we also launched a consulting plus implementation solutions, which is uniquely positioned with business plus technology to help our customers with their efforts to shift to home developed IT. So far, over 30 customers have implemented our products and solutions.

Next page, on Page 7.The Omni-channel Agent Solution in digital life insurance is a key product in 2022. Targeted at the international life insurance transformation market, we see huge potential in this offering. We collaborated with a global top 50 insurer who is also an insurance giant in emerging markets, in the Omni-channel Agent Solution project. Our solution stemming from integration of business technology offers end-to-end empowerment in Agent transformation, reaching a proven transformation experience, together with our leading AI technology as a foundation to our success.

Next on Page 8. Product standardization remains a key initiative in 2022. Although this generates some R&D investments, we are convinced that product standardization is fundamental to our long-term product competitiveness. We standardized over 1,200 models this year boosting delivery efficiency by nearly 30%.

Looking ahead, we will remain committed to product standardization efforts, which we believe will reflect in gross margin improvement.

On Page 9. We also noted encouraging results in broadening customer engagement, which is also a crucial part of our Stage 2 strategy. Despite the impact from the pandemic, OneConnect still managed to achieve 221 premium plus customers, up by 9 compared with last year. Our cooperation with many financial institution customers for new depth this year, including the National Development Bank, Bank of Ningbo Bank, China Guangfa Bank, China Continent Insurance, Guoren P&C Insurance. Our engagement with these institutions demonstrate breakthroughs and progress in business development in different segments.

Looking forward to execute Stage 2 strategy, OneConnect will continue to acquire new customers and also improve value from existing customers. Next on Page 10. Overseas business as an important wing of our one body two wings strategy also recorded rapid growth this year. In Singapore, we successfully replicated our SME financing platform in Guangdong province and jointly developed an SME digital financing platform with Abu Dhabi Global Market. In addition, we also launched a core system, mobile banking and lending platform with CIMB Philippines.

In Hong Kong, PAOB doubled its interest income in 2022 and introduced the short-term lending products tailored for SMEs in the construction industry. Our credit referencing agency officially qualified to commence business, and is expected to launch in late 2023.

Next, on Page 11. In technology and product launch, we have been awarded by many renowned institutions this year, including Wu Wenjun AI Science and Technology award, National High-tech Enterprise, IDC Financial Insights Innovation Award, to name just a few.

Moving ahead into 2023. Despite mild signs of economic recovery, operation and development remain challenging, as it still take time for businesses to fully restore their order. For OneConnect, we do expect the course of recovery to take a while as a result of the business nature in the industry.

Therefore, in 2023, we will continue prudent operation strategy and focus on improving revenue from third-party customers and narrowing losses. Next, I'll hand it over to Mr. Luo to brief you on our financial performance. Thank you.

Yongtao Luo
Chief Financial Officer (CFO)

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Okay. Thank you. Good evening, everyone. Just as Mr. Shen mentioned, despite the pandemic and the market environment headwinds, we recorded solid results in 2022. In this presentation, I will spend more time on our full year results. For the fourth quarter details, please refer to our results release.

My portion starts from Page 13. In 2022, our third-party revenue reached RMB 1.48 billion, improved by 6.5% on a year-over-year basis. Our top line revenue was RMB 4.46 billion, which was 8% higher than that in 2021. Benefited from continuous efforts on customer upgrade in Stage 2 development. The number of our Premium Plus customers increased to 221. Our adjusted net loss reduced to RMB 802 million, and corresponding profit margin improved by 12.7 percentage points to negative 18%.

Next page. Our revenue mix by customer type remained stable in 2022. Revenue from third-party customers grew by 6.5% to CNY 1.48 billion, representing 33.1% of our total revenue. We are glad to see that our products in Gamma platform and the overseas business continued strong momentum along the whole year, making up the shortfalls of reduced usage from certain products and delayed implementation caused by pandemic.

Revenue from Lufax increased by 7.3% to CNY 459 million and revenue from Ping An Group increased by 9.1% to CNY 2.53 billion, representing 10.3% and 56.6% of our total revenue, respectively. Moving to revenue mix by business type. Implementation revenue accounted for 19.3% of total, reached CNY 862 million and increased by 17.5%.

Despite the pandemic imposed pressure on our product delivery to third-party customers, we were able to achieve the growth mainly attributable to ongoing digital transformation demands from Ping An Group and overseas expansion of our life insurance business. Revenue from business origination decreased by 14.8% on year-over-year basis to CNY 384 million.

Revenue from risk management decreased by 22.3% on a year-over-year basis to CNY 415 million. The decreases of these 2 types of revenue are mostly due to reduced transaction volume from insurance claim system products and banking loan products as a result of the pandemic as well as less customers demand. Revenue from operation support increased by 3.9% on a year-over-year basis to CNY 1,141 million, which was mostly benefit from increased demands for AI customer service products in Gamma sector.

Revenue from cloud services platform grew by 25.3% on a year-on-year basis to CNY 1,316 million from CNY 1,050 million in the same period, last year. It was largely benefited from increased demands from Ping An Group. It was also worthwhile to mention that revenue from third-party customers continued strong momentum from the whole year. Post implementation and other revenue was up by 3.8% on a year-over-year basis to CNY 241 million.

We recorded strong revenue growth performance from our virtual banking business in Hong Kong in 2022, which increased by 210% to CNY 107 million from CNY 34 million in the prior year, which made a strong contribution to our above-average growth of overseas business.

Let's turn to revenue mix by product sectors. Gamma platform sector, our focus on product innovation in Stage 2 strategy, contributed the biggest chunk of our revenue, recording a 24.1% growth in 2022 and accounting for 45.2% of total revenue. Digital banking sector, which accounted for 32.6% of total revenue, reduced by 12.1% on a year-over-year basis, which was mainly caused by a reduction in transaction volume of our loan products as a result of the pandemic and adverse macro circumstances.

Digital insurance sector, which accounted for 19.8% of total revenue increased by 8.4% on a year-over- year basis. Benefited from newly launched life insurance agent product in the overseas market, while having the shortfall of reduction in transaction volume from insurance claim system products we were able to achieve overall revenue growth in digital insurance sector. Last but not least, our virtual banking sector, which I've mentioned before, accounted for 2.4% of our total revenue.

On next page, we are very glad to see our gross profit reached CNY 1.64 billion in 2022, with the gross margin achieved 36.6%, which was 1.8 percentage points higher than that in the same period last year. However, on a non-IFRS basis, gross margin was 40.1% compared with 42.1% in the prior year.

As Mr. Shen mentioned, in 2022, we have developed more than 1,200 standardized models and have improved

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about 30% delivery efficiency. Such ongoing product and delivery standardization efforts helped us improve our gross profit margin and it will be one of the main drivers for OneConnect to achieve our midterm target of profitability.

Moving to our expenses and net profit, you can see that we are well on track to our break-even meeting target. First of all, our research and development expenses came to CNY 1.42 billion from CNY 1.35 billion. As a percentage of revenue, it amounted to 31.8% compared with 32.7% in the prior year. We continued to implement our Stage 2 strategy focusing on product integration.

Our upgraded products are more mature and will further improve our product development efficiency. Looking forward, we will keep investing in research and development to enhance our product competitiveness against our competitors. Sales and marketing expenses for 2022 decreased to CNY 411 million compared with CNY 588 million in the prior year. As a percentage of revenue, sales and marketing expenses decreased to 9.2% from 14.2%. Such improvement was benefited from enhanced sales capability and efficiency.

Meanwhile, on-site marketing and travel-related expenses also decreased compared with that in 2021, which was mainly caused by COVID travel restrictions last year. Regarding our adjusted general and administrative expenses in which we have deducted our one-off Hong Kong listing expense incurred in 2022. It came to CNY 755 million from CNY 829 million in the same period of last year. As a percentage of revenue, it decreased to 16.9% from 20.1%.Based on all these above, our adjusted net profit improved to negative CNY 802 million from negative CNY 1,269 million in the same period last year.

And our adjusted net profit margin improved by 12.7 percentage points from negative 30.7% to negative 18%. Despite a very challenging business environment last year, we again managed to deliver double-digit narrowing of net loss margin.

The next page represents a comparison of loss ratio in the past 4 years. From this page, we can see a very clear trajectory of our path to profitability. We will further upgrade our products and boost our gross profit margin, and we will further improve operating efficiency to reduce expenses. We are very confident about breaking even by midterm.

Lastly, we summarized the adjustments in non-IFRS gross margin for reference. Thank you.

Danielle Gao
Head of Investor Relations
Thank you, Yongtao. Operator, we are ready for questions. Please open the line.

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Question and Answer

Operator

[Operator Instructions] Our first question is from Timothy Zhao from Goldman Sachs. Please go ahead.

Timothy Zhao
Goldman Sachs Group, Inc., Research Division

[Interpreted] I have 2 questions. First question is about the IT spending of financial institutions in 2023 equipment share, any outlook about the recovering pace, and recovering pace difference in different financial institutions' customers.[indiscernible]. Second is about our third-party revenue. I saw in the fourth quarter last year a revenue pretty well. If you can share the outlook on the growth rate of third- party revenue in 2023. And what single product, that we could expect actual growth rate?

Danielle Gao
Head of Investor Relations

Thank you, Timothy. Mr. Shen will take your questions.

Chongfeng Shen
Chairman of the Board & CEO

[Interpreted] I will answer your first question now. Over the short term, we do expect that financial institutions will be more prudent with their IT spending. However, over the medium to longer term, financial institutions need technologies and digital transformation to bolster their business development and growth. Therefore, we expect that in 2023, starting from the second quarter of 2023 and on to the second half of this year, their actual IT spending will pick up. OneConnect is uniquely positioned to satisfy the digital transformation demand from banks in the following front. In summary, technologies such as self- controlled risk management, data secured digital operation as well as a shift to home developed technology will be the key areas where banks will have demand and OneConnect has products to satisfy their demand in these areas. The shift to self-controlled technologies have attracted quite a lot of investment from financial institutions. And if we see the IT budget of banks to pick up it is because of the shift to home developed IT.

For medium to large-size banks, they will have a higher demand for data security as well as home developed IT. For medium and small-sized banks, they have higher demand for IT partners to help them satisfy regulatory requirements as well as to improve their operational efficiency. Next, on your second question, our OneConnect long-term growth ultimately stems from the broadening of customer engagement in our Stage 2 strategy.

Two of the key metrics for us -- for 2023, improvement in third-party revenue as well as improvement in gross profit margin. If we look at the product by segment, get to our consistent investment and efforts in product innovation, we do see positive trends in most of our products. Risk management and smart management in the banking segment, life insurance products in digital insurance, AI customer services in Gamma platform are expected to be the key drivers for growth in 2023.

Over the long-term, our overseas business, our financial cloud business as well as our push for home developed technology will also become our long-term growth drivers.

Operator

Our next question is from Tianen Zhou from Orient Securities.

Tianen Zhou
Orient Securities, Research Division

[Interpreted] I would share quick translation myself. The first question is a self-controlled technology. It's a very hot topic among the tech sector and what's the OCFT's strategy on it? And second question is what's the OneConnect 2023 guidance? And the last question is what's the coming cash position? And is it accurate to support to breakeven? And what's your exposure in SVB?

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Danielle Gao
Head of Investor Relations

Thank you, Tim. Our CTO will take your first question, and Yongtao will take your second and third questions.

Jie Li
Chief Technology Officer (CTO)

[Interpreted] Developing self-controlled technologies in the financial industry has been one of the most relevant trends in the industry. And we see huge market potential and adaption is needed -- in both the application layer core system as well as in the infrastructure level. And the CBIRC has launched a full fresh push for the home control, home developed technologies in 2022. And overall, about 5,000 institutions are involved in the pilot. OneConnect will fully accommodate self-controlled technologies and both the infrastructure level as well as the application level. Our financial cloud are 100% satisfied the requirement for self-controlled technologies. At the application level in our products, in the banking segment as well as in the Gamma platform, they are 100% adapted to self-controlled IT.

At the same time, OneConnect is also closely involved in the push for self-controlled technology in the banking industry through our consulting plus implementation model. So far, we now have over 30 customers using our solutions.

Yongtao Luo
Chief Financial Officer (CFO)

[Interpreted] Okay. I will do the translation myself. First of all, we won't give official guidance for 2023, due to the external and internal factors and reasons. I think external factors are the recovery and the macro environment are still uncertain and a lot of challenging factors. And internally, we are experiencing the Stage 2 transition and we are still in that period. Having said that, we will communicate more information about our profitability in different aspects. As we said, in midterm we will break even for the whole company. And first of all, our business in Mainland China will breakeven and we will communicate more information with markets on this side.

And there are 2 points we want to emphasize again, the 2 main tasks in 2023. One is improvement in quality and structure of our revenue, where we will put first priority on the third-party revenue growth. And at the same time, we will make more reduction in our losses. I think we are well on track to the path of break-even in midterm.

Okay, by end of 2022, we have cash available CNY 2.6 billion. And in 2022, all the reduction in the cash is due to the operating activities, mainly due to the operating activities. And in 2022, the narrowing of the loss-making and the acceleration of the receivable collections helped us a lot to get a very healthy cash position. And we are very confident that we have enough cash to support our operation until we break-even in the midterm.

And within the CNY 2.6 billion, CNY 520 million is with the PAOB banking in Hong Kong and else almost CNY 2.1 billion is with other business units of OneConnect, and we have no deposits with Silicon Valley Bank.

Operator

[Operator Instructions] Our next question is from Lydia Lin from Morgan Stanley.

Chenyueya Lin
Morgan Stanley, Research Division

[Foreign Language] So my first question is a follow-up on the localization. So will the localization affect all the businesses lines or just the implementation? And the second question is about the operating expenses, arrangement and allocation in 2023.

Danielle Gao
Head of Investor Relations

Thank you, Lydia. Your first question, Mr. Li and Mr. Luo will take your first question and the second question respectively.

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Jie Li
Chief Technology Officer (CTO)

[Interpreted] As I mentioned before, the drivers for self-controlled technologies range from infrastructure to the application level. Therefore, implementation part is the major part of our efforts in self-controlled technology. And as for the consulting class implementation solution we offer, it is mostly about implementation and consulting is used as a tool for us to break into the deal.

Actually, our 3 main business segments are quite relevant to self-controlled technologies. With the huge potential among the application level, core system level, as well as the infrastructure layer.

Yongtao Luo
Chief Financial Officer (CFO)

Okay. I think in 2023, the hiring process actually is pretty much back to normal, ready we started hiring new talents. While we will make some additional efforts related to the product's optimization. Referring to the 3 types of expenses, we continue to put more resources into research and development. And for the sales and marketing, and general and administrative expenses, we will continue to have a very cost control policy. And looking forward, the ratio of all 3 expenses to revenue, we will keep going down until we break-even.

Operator

We currently have no further questions. I would like to hand back now to Danielle Gao for final remarks. Please go ahead.

Danielle Gao
Head of Investor Relations

Thank you, everyone, for joining the call today. If any questions, please feel free to contact our IR team. We appreciate your interest in following us and looking forward to speaking with you again. Thank you.

Operator

Thank you. Ladies and gentlemen, this concludes today's call. You can now disconnect your lines. Thank you.

Portions of this transcript that are marked
[Interpreted] were spoken by an interpreter present on the live call.

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