

X Financial (XYF)
Third Quarter 2020 Earnings Conference Call
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Executives:

Tanya Wen, Investor Relations
Simon Cheng, President
Frank Fuya Zheng, Chief Financial Officer

Presentation

Operator: Good day, and welcome to the X Financial Third Quarter 2020 Earnings Conference Call. (Operator Instructions). After today's presentation, there will be an opportunity to ask questions. (Operator Instructions). Please note, this event is being recorded.

I would now like to turn the conference over to Tanya Wen. Please go ahead.

Tanya Wen: Thank you, operator. Hello, everyone, and thank you for joining us today. The Company's results were released earlier today, and are available on the Company's IR website at ir.xiaoyinggroup.com.

On the call today from X Financial are Mr. Simon Cheng, President, and Mr. Frank Fuya Zheng, the Chief Financial Officer. Mr. Cheng will give a brief overview of the Company's business operations and highlights, followed by Mr. Zheng, who will go through the financials. They are all available to answer your questions during the Q&A session.

I remind you that this call may contain forward-looking statements under the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995. Such statements are based on 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 and 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 statement as a result of new information, future events, or otherwise, except as required under law.

It is now my pleasure to introduce Mr. Simon Cheng. Mr. Cheng, please go ahead.

Simon Cheng: Hello, everyone. Despite the impact from COVID-19 and the tightened regulatory environment in China, we delivered encouraging operational and financial results in the third quarter. Thanks to the solid recovery in loan facilitation amount of Xiaoying Credit Loan, our

total loan facilitation amount increased by 30.4% quarter-over-quarter to RMB8,027 million.

We continued to adhere to our prudent risk management approach. The delinquency rates for all outstanding loans that are past due for 31 to 90 days and 91 to 180 days as of September 30, 2020 decreased further to 2.13% and 4.62%, respectively, compared to 3.53% and 9.44%, respectively, as of June 30, 2020. As the pandemic continues to ease and the macroeconomic environment recovers gradually in China, our credit risk profile continues to improve.

Based on the solid progress we have made on the operational front, we improved both our top and bottom lines. Our total net revenue increased by 44.3% quarter-over-quarter and net loss attributable to X Financial shareholders narrowed to RMB113.0 million from RMB343.7 million in the previous quarter, demonstrating our strong capability to navigate in an uncertain regulatory environment and challenging economy.

In August 2020, the Supreme People's Court of the PRC lowered the ceiling of the private lending interest rate protected by law. We believe this new policy is currently only applicable to private lending, which mainly refers to loans made to individuals or companies by private organizations or individuals, instead of financial institutions. The regulation does put pressure on the whole lending sector, but it's not directly applicable to our business at this moment, as we are a financial institution regulated by local financial regulatory authorities.

Recently, the Chinese government also planned to impose tighter regulations on small loans offered online by microloan companies. The regulators have started seeking public opinion on the interim measures for the administration of online small lending businesses. The new ruling will significantly affect the fundamentals of the online small lending industry with requirements on borrowing limits, fund leverage, prohibition of multi-regional lending and other measures. It is expected that the new regulations will be finalized by the end of this year.

Due to the low visibility caused by the regulatory uncertainties, it is difficult for companies in this sector to precisely evaluate its impact on their businesses at this moment. But they will need to adjust their strategies and bring substantial changes to their operations over a transitional period of 1 to 3 years to comply with the new policies.

Despite all the challenges ahead, we will continue to expand and improve our offerings to cater to the growing demand for personal financing in China. We are on track to apply for an online microcredit license and will keep a close watch on the evolving market dynamics and regulatory environment. We have experienced reforms and navigated difficult periods before, and emerged stronger as a key player in this industry. We are confident that we are capable of making strategic adjustments in a timely way to fit into the new business environment.

During the third quarter, we continued to expand our cooperation with financial institutions. In the third quarter, we successfully achieved 100% institutional funding for the new loans facilitated through our platform, compared with 97.4% in the previous quarter. Both the total available credit lines and the number of financial institutional partners have continued to expand. Our risk management capabilities and proven record have been fully recognized by our financial institutional partners.

Our exit from the P2P business has progressed in an orderly manner. The outstanding loan balance of the P2P business continued to decrease from RMB1.6 billion as of June 30, 2020 to RMB0.4 billion as of September 30, 2020 and further decreased to RMB0.3 billion as of October 31, 2020. Protecting the interests of our investors is always our top priority, and we believe it helps us minimize regulatory risks and establish a solid foundation of trust and integrity in the personal finance sector.

During the third quarter, our number of active borrowers continued to grow to 692,997, representing an increase of 10.8% from 625,707 in the previous quarter, mainly due to an increase in the number of active borrowers of Xiaoying Credit Loan. This is further acknowledgement of the high value and quality of the loan products we offer to borrowers, as well as the traction and growth momentum we gained as the market continues to gradually recover.

Overall, we will continue to strengthen our cooperation and relationships with financial institutions, and keep diversifying our institutional funding sources. With China's steady economic rebound and implementation of favorable policies to support domestic consumption, we are confident in our execution capabilities to create long-term value for our investors and shareholders.

Now I will turn the call to Frank, who will go through our financials.

Frank Fuya Zheng: We are pleased to have seen gradual recovery during the third quarter, thanks to the overall improving market conditions and our continuous efforts to enhance the top line growth and reduce costs across various parts of our business.

We continued to strengthen our risk management capabilities and focused on expanding the quality of our borrower base. The improvement in our credit risk profile has brought a significant decrease of RMB56.3 million in the bad debt provisions for accounts receivable and loans receivable in the third quarter when compared with the previous quarter.

Together with other cost control measures, we successfully narrowed the net loss for the quarter. So far into the fourth quarter, we are seeing more positive signs on the borrower side. As of October 31, 2020, the delinquency rates for all outstanding loans that are past due for 31 to 90 days and the 91 days to 180 days further dropped to 1.94% and 3.84%, respectively, an outstanding performance showing the high effectiveness of our risk control model and improvements in the quality of our borrowers.

In addition, our efforts to expand and deepen our cooperation with financial institutional partners continued to bear fruit. The total number of financial institutions which we cooperate with continued to increase during the third quarter. And at the same time, we also managed to reduce the overall funding costs in this quarter. We will continue to engage with more financial institutions to further optimize our cost structure. And in the meantime, we continued to diversify our partnerships with third-party financial guarantee companies.

In conclusion, we will continue to closely monitor regulations and market conditions, and ensure we will adapt quickly in response to any potential impact on our business due to changes in the macro environment.

In addition, we will continue to provide more attractive loan products, further improve the credit quality of our borrower base and explore additional cooperation opportunities with financial institutions to capture untapped growth in the personal finance industry.

Now I'd like to brief some financial performance for the third quarter 2020. Total net revenue decreased by 34.5% to RMB559.8 million, about US\$82.5 million, from RMB854.3 million in the same period of 2019, primarily due to a decline in total loan facilitation amount in this quarter when compared with the same period of 2019.

Origination and servicing expenses increased by 19.9% to RMB561.2 million, about US\$82.7 million, from RMB468.2 million in the same period of 2019, primarily due to the following factors: One, an increase in collection expenses resulting from a more active policy taken to address the impact of COVID-19; and two, an increase in interest expenses related to financing income.

Provision for accounts receivable and contract assets decreased by 71.2% to RMB24.3 million, around US\$3.6 million, from RMB84.7 million in the same period of 2019, primarily due to the combined effect of, one, a decrease in accounts receivable and contract assets, and a decrease in the estimated default rates.

Provision for loans receivable was RMB58.1 million, about US\$8.6 million, compared with RMB3.9 million in the same period of 2019, primarily due to an increase in loans receivable from credit loans and revolving loans.

Net loss attributable to X Financial shareholders was RMB113.0 million, about US\$16.6 million, compared with net income attributable to X Financial shareholders of RMB169.6 million in the same period of 2019.

Finally, business outlook. Given the ongoing regulatory changes, all market players are taking a more prudent risk management approach. And the Company is in the process of reassessing its institutional cooperators. Based on the Company's preliminary assessment, the deposits paid to its institutional cooperators are subject to impairment risks. Consequently, the Company is unable to reasonably determine a near-term outlook for its business.

Now, this concludes our prepared remarks, and we'd like to open the call to questions. Operator, please.

Questions and Answers

Operator: Thank you. We will now begin the question-and-answer session. (Operator Instructions).

Showing no further questions at this time, this concludes our question-and-answer session. I would like to turn the conference back over to Tanya Wen for any closing remarks.

Tanya Wen: Thank you, everyone, for joining us on the call today. If you haven't got the chance to raise your questions, we will be pleased to answer them through follow-up contacts. We look forward to speaking with you again in the near future. Thank you.

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