Yiren Digital (ADR)
Q3 2024 Earnings Conference Call
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Executives
Keyao He, Investor Relations
Ning Tang, Founder, Chairman, Chief Executive Officer
Yuning Feng, Chief Financial Officer

Analysts
Kris Wu, Look Capital

Presentation

Operator: Good day, and welcome to the Yiren Digital Third Quarter 2024 Earnings Conference Call. (Operator Instructions). After today's presentation, there will be an opportunity to ask questions. (Operator Instructions). Please note today's event is being recorded.

I would now like to turn the conference over to Keyao He, IR Officer. Please go ahead.

Keyao He: Thank you, operator. Good morning and good evening, everyone. Today's call features the presentation by the Founder, Chairman, and CEO of CreditEase, our CEO, Mr. Ning Tang, and our CFO, Mr. Yuning Feng will also attend the Q&A session after the prepared remarks.

Before beginning, we'd like to remind you that discussions during this call contain forward-looking statements made under the Safe Harbor provision of U.S. Federal Security Litigation Reform Act of 1995. Such statements are subject to risk, uncertainties, and factors that can cause actual results to differ materially from those contained in any such statements.

Further information regarding such risks, uncertainties, or factors is included in our filing with the U.S. Securities and Exchange Commission. We do not undertake any obligation to update any forward-looking statements as required under the relevant laws.

During the call, we will be referring to certain non-GAAP financial measures and supplemental measures to review and assess our operating performance. These non-GAAP financial measures are not intended to be considered in isolation, or as a substitute for the financial information prepared and presented in accordance with U.S. GAAP. For information about those non-GAAP measures and reconciliations of GAAP measures, please refer to our earnings press release.

I will now pass it to Ning for opening remarks.

Ning Tang: Thank you all for joining our earnings conference call today. I'm pleased to report a stable and healthy quarter with concrete business development and strategic exploration, driven by our quality over quantity strategy. This quarter's results underscored our consistent focus on sustainable, high-quality growth.

Before I go into the operational details, I'd like to share some highlights from this quarter. First, our financial services business made notable improvements in asset quality, thanks to our continued focus on strong risk management and borrower optimization. Second, we've been proactively exploring new online business models for our insurance division and have seen visible progress, driving an increase in sales of retirement-themed insurance products.

As a tech-powered platform, Yiren Digital prioritizes the use of technology and digital capabilities to enhance our business model. Our going online business model is expanding from financial services to the insurance brokerage space. Third, our ongoing investment in AI is already bearing fruit, with proprietary AI applications now largely integrated into our daily operations, driving efficiency and improving customer experience. All together, these efforts are laying a solid foundation for the next phase of higher-quality growth, one that will continue to drive value for our shareholders in the years to come.

Now, let me go through our key business highlights. First, regarding our financial services business. The third quarter of 2024 saw continued growth, with total loan volume reaching RMB 13.4 billion, a 36% increase year-over-year.

The number of borrowers stayed relatively stable quarter over quarter at 115 million, a 24% growth compared to the same period last year.

Meanwhile, our lending platform, Yixianghua, remains highly popular, with monthly active users staying steady at around 4.5 million, a 52% year-over-year increase. Growth has been primarily driven by strong demand for our small revolving loan product and an increase in repeat borrowing from high-quality customers.

As I mentioned earlier, we have enhanced the quality of our customer base by focusing on higher-quality customers with stronger repayment capabilities and better risk profiles. And now those new customers are contributing to a growing proportion of repeat loans, becoming an important growth driver. Over 60% of the loans facilitated during the quarter came from repeat borrowers, up 5 percentage points from the previous quarter.

As our efforts to upgrade our customer segments yield success in phases, we are now focusing on increasing the repeat borrowing rate among existing customers, while maintaining a balanced mix of new and returning customers.

Furthermore, as a result of our customer quality upgrade and highly-effective AI-driven risk management, we've seen significant improvements across various risk indicators, confirming the effectiveness of our approach. In the third quarter, our FPD 30+ rate dropped by 32 basis points to a record low. As of September 30, 2024, delinquency rates for the 1 to 30-day, 31 to 60-day, and 60 to 90-day buckets fell by 10, 20, and 30 basis points quarter-over-quarter, respectively.

Additionally, M1 recovery rates rose by 1.82 percentage points, reaching an all-time high. The shift in our customer structure establishes a solid foundation for our sustainable growth.

On the funding side, we made essential progress in expanding our funding partnerships. By the end of the third quarter of 2024, we had added nearly 20 new funding partners for the year. Meanwhile, our funding cost saw another 64 basis points reduction quarter-over-quarter.

Moving on to our international business. Our growth momentum remains strong. In the Philippines, both loan volumes and revenues posted double-digit increases quarter-over-quarter. We also began optimizing our customer base there while iterating our product offerings. And we expect these efforts to positively impact profitability in the fourth quarter of 2024.

On our AI strategy, we made substantial progress with six proprietary AI systems now supporting customer acquisition, customer service, asset management, and collections in our daily operations. I will now highlight several updates to demonstrate this progress. Firstly, for our domestic business operations, AI has significantly enhanced our collection and quality assurance processes. As of the end of third quarter, 77% of Day 1 overdue cases were covered by AI robots, resulting in labor cost savings of nearly RMB 2 million in Q3 alone. Meanwhile, to ensure the high professionalism of our services, we deployed 20 AI models for quality assurance in loan collections and 8 AI models for quality assurance in customer service, with the collections models achieving over 96% accuracy.

Additionally, we strengthened our AI talent pool by hiring over 50 professionals specializing in AI development, data science, and modeling, further enhancing our digital capabilities.

Secondly, in our overseas operations, we fully developed and refined our AI-powered ID verification model in the Philippines, achieving an accuracy rate of nearly 95% in the third quarter, with performance now stabilizing.

Moving to our insurance brokerage business, the overall industry has faced profitability pressure due to regulatory changes, including lower interest rates and the policy of Unified Commissions and Fees in Reporting and Underwriting. Despite these challenges, our total premiums this quarter recovered to RMB 1.35 billion, a 27% quarter-over-quarter increase. The rebound was partially driven by our online business initiatives.

As I mentioned earlier, we've made progress in customer acquisition through social media, supported by AI-generated content. During the quarter, new policy premiums from social media channels contributed RMB 7.5 million -- 7.1 million. This is a promising start, and we also built a dedicated team to focus on private traffic operations, driving efficient customer acquisition and conversion.

Additionally, we are working on creating more synergies between our lending platform and insurance services by offering customized insurance products to our borrowers. And we expect to see growth from these efforts in the fourth quarter.

In the consumption and lifestyle services segment, our total GMV was RMB 508 million for the quarter, a 10% year-over-year decline. As our customer base evolves, we are refining our product range to better serve our evolving demographic. Looking ahead, we plan to introduce more high-quality, tailored products to meet their specific needs.

In summary, our priority remains ensuring long-term, sustainable growth. In times of external uncertainty and market fluctuations, it is critical to stay focused on maintaining the quality of our business. We will continue to expand our online operations and enhance synergies across our businesses, while further investing in R&D and increasing AI penetration.

Furthermore, regarding our AI development, I would like to reiterate that we have been executing our AI strategy through the AI Lab, which incubates, invests in, and provides value-added services to AI startups, targeting enterprises, developers, and consumers. We have made several early-stage investments this year, and we are exploring business cooperation with them.

Additionally, I'm pleased to share that the commercialization of our proprietary AI systems is already underway, and we expect to see corresponding revenue reflected in our P&L in the near future.

Now, I will pass it to Yuning, who will go through our financial performance.

Yuning Feng: Thank you, Ning. Hello, everyone. On this call, I will only focus on our key financial highlights. Please refer to our earnings release and IR deck for further details, both available on our website.

First of all, we are glad to have delivered a healthy quarter with stable financial performance. In the third quarter of this year, our total revenue reached RMB 1.5 billion, up 13% year-over-year.

In the financial services segment, total loan facilitation continued to grow steadily, reaching RMB 13.4 billion, up 36% year-over-year. This was primarily driven by strong demand for our small revolving loan products and the rise in repeat borrowing from our high-quality borrowers.

Revenue from our financial service business increased 25% year-over-year to RMB 836 million, maintaining a healthy and steady growth rate in line with our quality over quantity business guideline, given external fluctuations.

In the insurance sector, our gross written premiums were RMB 1.4 billion, down 5% year-over-year, but up 27% quarter-over-quarter. The annual decrease was primarily due to a significant decline in our life insurance sales, resulting from regulatory changes and product adjustments. The quarterly rebound was driven by our online insurance sales. As our going online initiatives continue to progress, we expect further recovery in our overall insurance volume in 2025.

So earlier this year, the guaranteed return on life insurance products was further capped at 2.5% annually under the new regulations, following a rate reduction from 3.5% to 3% last August, which has further impacted the overall profitability of the life insurance sector in China. Moreover, the ongoing implementation of the Unified Commissions and Fees in Reporting and Underwriting regulation is adding pressure to commission rates industry-wide.

Consequently, in the third quarter this year, revenue from the insurance segment was RMB 85.5 million, down 68% year-over-year.

In the consumption and lifestyle segment, the total GMV for this quarter stood at RMB 508 million, a decrease of 10% year-over-year. The decline was due to already high product penetration among existing customers, and our strategic reduction in product offerings as we move up-market with our customer base. As our customer demographic evolves, we are strategically phasing out older product offerings and developing new products tailored to their specific profiles and needs.

On the expense side, sales and marketing spend increased 71% year-over-year to RMB 336 million. This annual growth was mainly fueled by the swift expansion of our financial services segment and enhanced marketing efforts focused on attracting new and high-quality customers. Research and development expenses increased 287% year-over-year to RMB 151 million due to our ongoing investments in AI enhancements, technological advancements, and the hiring of AI talents.

Origination, servicing and other operating costs decreased 16% year-over-year to RMB 206 million. This was mainly because the decrease in the insurance business volume, which resulted in lower channel rebates and associated settlement costs.

G&A expenses increased to 50% year-over-year to RMB 80 million. The annual growth was mainly due to the increasing incentive bonus and employee benefits. The allowance for the contract assets and the receivables was RMB 95 million, up 31% year-over-year. The increase was mainly driven by growth in loan volume facilitated.

Provisions for contingent liabilities this quarter increased to RMB 272 million from RMB 11 million in the same period of 2023. This is a result of the continued growth in loan volumes under our new risk-taking model, which requires substantial upfront provisions according to current accounting standards. However, this provision will be periodically recognized in the P&L as guarantee service fees over time. In other words, there is a time difference in revenue recognition under this product model.

However, from a loan's lifetime perspective, profitability will show better performance compared to loans under a non-risk-taking model. In the third quarter, the revenue from guarantee services reached RMB 137 million, which is 5x that in the same period last year.

Now on the bottom line, net income of this quarter was RMB 355 million, decreased 36% year-over-year. The decrease of net income due to three reasons: so firstly, as noted earlier, overall profitability in the insurance business decreased. Secondly, marketing expense and R&D expense rose due as we continued investing, attracting new, high-quality borrowers from our financial services business, and investing in developing our in-house AI capabilities. Thirdly, significant upfront provisions have been set aside as we increased loan volumes under our risk-taking models.

Regarding cash flow, so as our loan facilitation business continues to grow and our loan balance expands, our funding sources, which are banks, financial institutions, etc., and associated guarantee companies have requested that we provide a strategic deposit, a common practice in the industry. This quarter, we made one-time deposit payment based on our current loan balance, resulting in a notable decrease in our operating cash flow. We generated approximately RMB 50 million net cash from our operations this quarter. But looking ahead, cash flow is expected to return to normal level next quarter.

On the balance sheet side, our cash and cash equivalents remained strong at RMB 3.7 billion, though reflecting a notable decrease. This change is related to our long-term investments in business expansion and potential license acquisitions, which are still in progress. We will disclose more details once the deals are secured.

Now, regarding shareholder return, firstly, for share buybacks. In the third quarter of this year, we allocated USD 3 million to repurchase shares in the public market. As of September 30, 2024, the company had purchased approximately 5 million ADSs in the open market for a total of approximately US$16.5 million excluding commissions, under the 2022 share repurchase program. Additionally, we distributed a cash dividend in October under our semiannual dividend policy, with a total payout ratio of 14% of our earnings for the first half of 2024.

Lastly, on our business outlook, based on our assessment of current business and marketing conditions, we expect our revenue for the fourth quarter 2024 to stand between RMB 1.3 billion to RMB 1.5 billion, with a healthy net profit margin. This represents our current and preliminary assessment, which may be subject to change and uncertainties. This concludes our remarks.

Keyao He: Operator, we are open for Q&A session.

Questions and Answers

Operator: Thank you. We will now begin the question-and-answer session. (Operator Instructions). Kris Wu with Look Capital.

Kris Wu: Looking at the financial results, we have actually seen your loan volume increased by 3.5% quarter-to-quarter, and going a bit down from last quarter, which is 9%. And may we know why there are slowdown? And then also going into Q4, have you seen any further pickup in credit demand and loan application October and November? And any updates on your new customer acquisition strategy?

Ning Tang: Thank you. I'll take the first crack and Yuning can, yes, add to it, please. We see this demand forcredit remains high, and but it's very like uncertain market conditions. And we are focused on this quality first, or quality over quantity strategy, which makes it a must to do greater risk management. That's where you see our results are very encouraging. Going forward, we will maintain this strategy, but we are also working harder on bringing in higher-quality customers with reasonable customer acquisition cost associated with it.

Yes, so Yuning, please, add to it.

Yuning Feng: Thank you. So, yes, I think you're reflecting that in Q4, we are still carry on our strategy and our customer acquisition strategy. As we are a 100% online business model, so in this year, we're a corporation with TikTok, Douyin, and WeChat and co-built and AI-driven real-time analysis model, which efficiently screens unqualified borrowers based on their credit score and acquired qualified borrowers.

But as this year comes to an end, I think in Q4, we're expecting the cost of customer acquisition still a little bit high in this quarter, as we see a lot of competition from the market, and also to manage our risk level. So we'll see how it goes out. But to summarize, I think we are still keeping a steady strategy, and will trying to acquire new customers at a reasonable price -- cost, and trying to, well, enlarge our -- expand our repeat borrowing pool. So that's the answer.

Ning Tang: Yes, the idea is we keep our risk management really robust and try our best to grow, and we have confidence, yes, we will have relatively high growth in the quarters to come. I hope that answers your question.

Kris Wu: Sure, sure. It's encouraging to know --

Keyao He: Do you have any further questions?

Kris Wu: Yes, sure, sure, sure. Let me follow-up. It's encouraging to know that we are maintaining a healthy momentum, and also to care for risk management at the same time. Perhaps the next interesting aspect to look at is AI.

Since we're seeing that you are increasing your investment in AI and hiring quite a number of professionals, could you explain what makes you competitive in the AI space, especially given that we have so many AI native companies in the market? And could you also tell us more about the AI systems that will be commercialized, as you mentioned in your remarks?

Ning Tang: Thank you for the question, and so we are not a general-purpose AI firm ; we are an application of AI company position. So we have like use cases; we have data, yes, accumulated through all the years. So we are uniquely positioned, yes, therefore, to really build like credit-related like models, the insurance-related models, yes. So this is our edge as a AI application company. And as I reported early on, AI models systems have been built across our business, yes, like from and to like back-end.

So like customer acquisition, marketing intelligence, risk assessment, like customer service, like collection, and so on, yes. So many of the modules based on our preliminary market research, very welcome in the marketplace, yes. So we are working on monetizing these valuable assets, yes.

Yuning, can you add to it?

Yuning Feng: Yes, so as we mentioned in the early -- in the calls that we have developed six major AI systems that support our business operations. I think some of them are quite mature used in our day-to-day business; some are in early development. So we are evaluate which one to maybe can use in our -- for our business partners. Some can be used in our peers; some are maybe in financial institutions.

We're trying to -- well, the system -- actually, their developers are mostly in-house use, but we commercialize it to make it more useful in the market, and trying to, well, develop the business in our -- especially in our peers and the financial institutions. I think we are going to see some progress in the near future, and maybe in 6 months to a year.

Ning Tang: Let me add two things, if I may. One is that finance-related like exchanges, interactions, need to be, in many cases, very precise. So we are prudent in developing and utilizing AI models, knowing that generative AI has certain shortcomings, yes. So we use like an REG (inaudible), to mitigate that, but still, certain models are still in the last phase of testing and they haven't been fully used. But there are many others in great deployment stage and ready for external commercialization.

Secondly, I'd like to add that, the overseas markets can be quite good places for AI, because there is like China 5, 10, even 15 years ago. So using AI, we can just leapfrog, right? Like in China, with the experience like internet, mobile internet, big data, knowledge grabs, so on, to, yes, AI, different phases of AI, until today, generative AI.

But in, some overseas markets like in the Southeast Asia, in South America, so on. So these markets really ideal for AI deployment. Of course, we will be careful also in terms of risk management compliance, so on, yes. I'd like to just add this to thoughts.

Keyao He: We hope that answers your question, Kris, and thank you very much for your question.

Operator: Thank you. This concludes our question-and-answer session. If you have any further questions, please contact the company's IR team for assistance. Today's conference has now concluded. We thank you all for attending today's presentation. You may now disconnect your lines, and have a wonderful day.