

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

Tanya Wen, Investor Relations
Simon Cheng, President
Kevin Zhang, Chief Financial Officer

Presentation

Operator: Hello, and welcome to the X Financial Second 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. Kevin Zhang, Chief Financial Officer. Mr. Cheng will give a brief overview of the Company's business operations and highlights, followed by Mr. Zhang, who will go through the financials and guidance. 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 expectation and the 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. We continued to face great challenges due to COVID-19. However, we have shown and strengthened strong signs of gradual recovery in the market, and made timely and strategic decisions that will help the business deal with these uncertainties and the adverse impact on the economy and market environment. As a result, we believe we are well

positioned to capture potential market opportunities ahead under the accelerated industry consolidation due to COVID-19.

During the second quarter, our number of active borrowers reached 625,707, representing an increase of 46% from 428,366 from the previous quarter. It is mainly due to an increase in the number of active borrowers of Xiaoying Credit Loan.

In addition, the credit quality of our borrowers improved greatly during the quarter in part due to our comprehensive risk management capabilities and stringent assessment criteria for borrowers.

Our total loan facilitation amount in July has recovered to the level in January 2020 before COVID-19, and so were the delinquency rates for outstanding loans.

We implemented more stringent risk policy and control measures to improve margins during the quarter. The total cumulative registered users on the platform increased 10.6% to 47.1 million as of June 30, 2020, demonstrating the continued value and quality of the loan products that we offer borrowers and consumers, even during such a challenging environment.

Regulatory compliance has always been our top priority and a key competitive edge in the market. So far, our transition to 100% institutional funding has been very smooth, and we expect to strengthen our relationship with financial partners and keep diversifying our institutional funding resources. At present, we have achieved 100% institutional funding for new loans facilitated through our platform.

Despite the impact from COVID-19, our risk management capabilities continue to be well recognized by our institutional partners. As of June 30, 2020, the total credit lines provided by our institutional partners expanded to RMB62.1 billion from RMB58.6 billion as of March 31, 2020.

As of June 30, 2020, the outstanding loan balance of our P2P business was RMB1.6 billion, less than one-seventh of the total outstanding loan balance, a significant decrease from RMB8.8 billion as of December 31, 2019 and RMB14.9 billion as of June 30, 2019.

We are always doing more to step-up our efforts to protect the interests of our investors with greater transparency and timely information.

Furthermore, we are applying for a small loan credit license to provide more convenient financial services to our customers. We have made encouraging progress at this front, and we are expecting to get a license by the end of this year. This initiative will further expand our product offerings to meet the demands of underserved consumers and SMEs in China.

In the meantime, we are continuing to expand our institutional funding bases. The number of financial partners continued to increase during the quarter. We are also in negotiations with more financial partners to reduce funding costs even further. Building our platform out to scale with our technology-driven risk control infrastructure, we use cutting-edge data analysis and machine learning to profile our borrowers on a variety of reliable social and behavioral data. We then use this information to set appropriate credit lines and based on individual assessment results.

Our proven risk management capabilities and data intelligence have been well received by our institutional partners. As our business recovers with high-growth momentum, we expect to maintain closer cooperation with our financial partners and increase our institutional funding sources.

In conclusion, as China's economy continues to rebound, thanks to the government's recent efforts to revive the economy and drive domestic consumption with continued policy stimulus. We expect that the Chinese government will continue to stabilize the domestic economy with a series of supportive and long-term sustainable policies to be adopted.

We will continue to closely monitor market conditions and ensure that we are well positioned to capture the potential market opportunities ahead, and to foster the development of the business in a healthy and stable manner. We are confident of the strategic measures we have implemented to ride out these challenging market conditions, and our capability to create long-term value for our investors and shareholders.

Most importantly, we have ample funding sources to capture the enormous growth opportunities in China's personal financial industry, and thrive when the market revives.

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

Kevin Zhang: Thank you, Simon, and hello, everyone. Although the last quarter was challenging, we continued to make progress on the execution of our business transition strategy. We did see an increase in the number of our active borrowers by 46% on a sequential basis, and the total cumulative registered users reached to 47 million as of June 30, 2020.

Institutional funding accounted for 97% of the total loan facilitation amount, compared with 81% in the first quarter of 2020. During the second quarter, the percentage of loan products we facilitated that were covered by ZhongAn Insurance decreased further to 54% as we continued to reduce our insurance coverage rate to lower customer borrowing costs and enhance credit quality.

In the early onset of the third quarter, our business was already on track for a steady recovery. In July, our total loan facilitation amount was back to the level in January 2020 before COVID-19, and so were the delinquency rates for outstanding loans. The delinquency rates for all outstanding loans that are past due for 31 to 90 days as of June 30, 2020 was 3.53%, compared with 6.71% as of March 31, 2020. We expect this improvement trend to continue in the upcoming quarters.

In the meantime, we continue to take a disciplined and prudent approach on cost control, and will conform our business operation towards a healthy margin profile.

In light of the accelerated combination of efforts to improve our top line and reduce operational expenses, we expect to resume the profit during the second half of 2020.

We will continue to prioritize long-term value for our shareholders by focusing on improving operational efficiency and lowering our customer borrowing costs. In addition to improving the quality of our underlying assets and risk control management systems, we have largely

strengthened our internal efforts to acquire more quality borrowers for Xiaoying Credit Loan, our core loan business, and expect to facilitate more loans in the coming quarters.

Now I'd like to brief some financial performance. The total net revenue decreased by 51% to RMB388 million from RMB792 million in the same period of 2019, primarily due to a decrease in transaction volumes as a result of our more stringent risk policy put in place to address impact of COVID-19; and also partially offset by an increase in the proportion of total net revenue generated by the loans facilitated through the Consolidated Trusts, which was recorded over the life of the underlying financing using the effective interest method.

The origination and servicing expenses increased by 17.6% to RMB496 million from RMB422 million in the same period of 2019, primarily due to the following factors: First, an increase in customer acquisition costs; and second, an increase in interest expense related to loans facilitated through the Consolidated Trusts.

Sales and marketing expenses decreased by 43% to RMB15 million from RMB27 million in the same period of 2019, primarily due to a reduction in promotional and advertising expenses since the outbreak of COVID-19.

Provision for contingent guarantee liabilities was RMB3.7 million, compared with nil in the same period of 2019, primarily attributable to the increase caused by the pandemic, in estimated default rate of the loans subject to guarantee liabilities facilitated in prior periods.

Provision for accounts receivable and contract assets decreased by 25% to RMB28 million from RMB38 million in the same period of 2019, primarily due to a combined effect of a decrease in accounts receivable and contract assets, and a change in the estimated default rates.

Provision for loans receivable was RMB110 million, compared with RMB25.8 million in the same period of 2019, primarily due to an increase in loans receivable, which was in line with an increase in the proportion of total net revenue generated by the loans facilitated through other financial partners.

Loss from operation was RMB341 million, compared with income from operation of RMB224 million in the same period of 2019.

Non-GAAP adjusted net loss attributable to X Financial shareholders was RMB326 million, compared with non-GAAP adjusted net income attributable to X Financial shareholders of RMB355 million in the same period of 2019.

In light of the continued steady recovery in the business that is seeing, the Company currently expects a quarter-on-quarter growth over 20% in the total loan facilitation for the third quarter.

Providing the stable situation in China, as well as the accelerated combination of efforts to improve the top line and reduce operational costs and expenses, the Company expects to be able to resume profit during the second half of 2020.

This forecast reflects the Company's current and preliminary views, which are subject to change.

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

Questions and Answers

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

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 today on the call today. If you haven't got a 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.