

[FINV] - FinVolution Group
Q2 2023 Earnings Conference Call
August 28, 2023, 8:30PM ET.

Officers

Tiezheng Li, Chief Executive Officer
Jiayuan Xu, Chief Financial Officer
Jimmy Tan, Head, IR

Analysts

Yada Li, CICC
Frank Zheng, Credit Suisse
Alex Ye, UBS
Thomas Chong, Jefferies
Cindy Wang, China Renaissance

Presentation

Operator: Hello, ladies and gentlemen. Thank you for participating in the Second Quarter 2023 Earnings Conference Call for FinVolution Group. (Operator Instructions). After management's prepared remarks, there will be a question-and-answer session. Today's conference call is being recorded.

I'll now turn the call over to your host, Jimmy Tan, Head of Investor Relations for the Company. Jimmy, please go ahead.

Jimmy Tan: Hello, everyone, and welcome to our second quarter 2023 earnings conference call. The Company results were issued via newswire services earlier today and are posted online. You can download the earnings release and sign up for the Company's email alerts by visiting the IR section of our website at ir.finvgroup.com.

Mr. Tiezheng Li, our Chief Executive Officer, and Mr. Jiayuan Xu, our Chief Financial Officer, will start the call with their prepared remarks and conclude with a Q&A session.

During this call, we will be referring to several non-GAAP financial 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 these non-GAAP measures and reconciliation to GAAP measures, please refer to our earnings press release.

Before we continue, please note that today's discussion will contain forward-looking statements made under the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. Forward-looking statements involve inherent risks and

uncertainties. As such, the Company's results may be materially different from the views expressed today.

Further information regarding these and other risks and uncertainties are included in the Company's filings with the U.S. Securities and Exchange Commission. The Company does not assume any obligation to update any forward-looking statements except as required under applicable law.

Finally, we posted a slide presentation on our IR website providing details of our results for the quarter.

I will now turn the call over to our CEO, Mr. Tiezheng Li. Please go ahead, sir.

Tiezheng Li: Thanks, Jimmy. Hello, everyone, and thank you for joining our earnings call. This is Tiezheng Li, CEO of FinVolution Group. We're happy to speak with you today.

Since our expansion into the Indonesian market back in 2018, we have continued to execute our Local Focus, Global Outlook strategy in the Pan-Asia region with unwavering determination. To date, we have cumulatively served over 28 million borrowers in China, Indonesia, and the Philippines.

By integrating our local business focus with an international perspective, we are able to leverage our expertise and insights derived from diverse markets to drive growth and foster innovation within our organization. We expect this strategy to produce further benefits as we expand into additional countries and strengthen our presence in our existing markets.

As China transitions into the post-Covid era, the recent July macroeconomic data continued to be challenging with pockets of improvement in certain areas. However, macroeconomic data from the ASEAN markets in which we operate currently paints a more positive picture, reflecting growth across different operational metrics. Given these circumstances, we are adopting a strategy of progressive growth in the China market while pursuing rapid growth in the international markets.

While we await the domestic macro environment's recovery from the current challenges, we have been continuously investing in R&D. We have substantially enhanced our technologies enabling us to streamline our processes, upgrade our customer experience and achieve improvements across the various markets in which we operate.

We are pleased to share that FinVolution's total transaction volume in the second quarter increased to RMB47.3 billion, while our outstanding loan balance reached RMB63.7 billion, up 14% and 13%, respectively, year-over-year. This growth validates our company's ability to efficiently adapt to the changing economic landscape while continuing to meet the needs of our customers across our markets in the Pan-Asian region.

Technological innovation continues to be the core of our mission and the primary source of our competitive advantage. In July, we hosted the eighth FinVolution Technology Cup

Competition, our annual event showcasing and cultivating technological talent and creativity. This year's event focused on the development of automatic speech recognition, ASR, to improve the technology's grasp of Chinese dialects and languages, aiming to increase chatbots' efficiency and accuracy when communicating with customers from different regions.

Our commitment to innovation was recently recognized at the 2023 World Artificial Intelligence Conference, where the thesis we developed in cooperation with University of Zhejiang, Drop Message: Unifying Random Dropping for Graph Neural Networks was nominated for the Outstanding Thesis award.

Our investment in A.I and Machine Learning began years ago, with R&D spanning across different product categories such as self-help services, chatbots, data analytics and credit risk assessment. Over the past several years, we have been training our models utilizing billions of dollars of transaction data, steadily increasing their accuracy. We currently employ a fully automated loan approval process with all our funding partners, and our automated chatbot resolves about 80% of customer inquiries on average.

We consistently embrace new technologies and deploy them into our daily operations to deliver a more personalized and tailored experience for our users. Along with the use of chatbots in customer service and to address early-days delinquencies in the loan collection process, we have also upgraded and streamlined user experience by automating self- help functions and providing instant responses for our users.

In addition, we have incorporated AIGC into our advertisements for our overseas business, increasing our campaigns' audience targeting accuracy and achieving greater visibility on leading social media platforms such as Facebook, Instagram, and Tik Tok. As a result, during the month of July, our followers on Tik Tok grew to around 700,000, while followers on Facebook and Instagram reached 967,000 and 220,000 respectively.

Furthermore, we strove to advance our commitment to promoting financial inclusion during the quarter. Aligning our ESG efforts with this business goal through better borrowing rates, we further optimized our average borrowing rates in China to 22.3%, ensuring our services are accessible and affordable for our borrowers.

On a related note, I would like to share some updates on our ESG progress. We recently published our 2022 ESG report, the fifth in our Company's history, demonstrating our dedication to transparency and sustainability. Responsible ESG reporting allows us to showcase our strong governance practices and our actions addressing the environmental and social issues affecting our industry, while also empowering us to design effective future initiatives.

For instance, since the launch of our interest-free loans for eligible small business owners in China, we have cumulatively supported over 11,000 small business owners in pursuit of their dreams. Our subsidiaries in the Indonesian and Philippine markets are also proactively engaging in ESG work, such as conducting cost management workshops to educate borrowers and launching a large-scale mangrove tree planting project to improve

people's livelihoods in the local community, among other activities. We firmly believe that aligning our ESG and business goals will ultimately create long-term value for all our stakeholders while achieving a positive societal impact.

Before we move on to additional operational and financial metrics with our CFO, I'd like to share that FinVolution celebrated its 16th Anniversary during the second quarter, a milestone that affords us a glimpse of our future outlook as an enterprise with sustainable growth. As we have grown and built the business throughout the years, we have accumulated a suite of technologies, skillsets, and capabilities that enable us to navigate and succeed in all the markets in which we operate.

We will remain committed to our vision of leveraging innovative technology to make financial services better, propelling FinVolution's long-term sustainable growth along the way.

With that, I will now turn the call over to our CFO, Jiayuan Xu, who will discuss our operational and financial results for ER.

Jiayuan Xu: Thank you, Li, and hello, everyone. Welcome to our second quarter 2023 earnings call. In the interest of time, I will not go through all of the financial line items on this call. Please refer to our earnings release for further details.

As Li mentioned, the domestic macro environment continued to be challenging with pockets of improvements in certain areas. The official manufacturing purchasing managers' index came in at 49.3 points in July compared to 49 points in June and 48.8 points in May, according to data released by the National Bureau of Statistics on July 31, 2023.

Meanwhile, total social financing data in July increased by just RMB528 billion, below market expectations. Total retail consumption in July only increased by 2.5% compared with the same period last year. However, despite the challenging macro environment, we are encouraged by the strong operational and financial results we delivered in the second quarter of 2023.

Driven by our stable and better-quality borrower base, we achieved solid operational metrics in the second quarter in the China market. Cumulatively, we have served over 24 million borrowers in China, with the number of unique borrowers at around 2.3 million, up 5% sequentially.

Additionally, our China transaction volume reached RMB45.5 billion, while our outstanding loan balance reached RMB62.6 billion as of June 30, 2023, both up 12% on a year-over-year basis.

Bolstered by our prudent approach to risk management with proven fraud detection technologies, we have maintained a stable risk level. In the second quarter of 2023, our Day-1 delinquency rate was around 5.6%, and vintage delinquency rate is expected to be around 2.3% for the quarter.

Finally, thanks to our loan collection team's impressive efforts, our loan collection recovery rate maintained stable at around 90%.

As we continued to fine-tune our strategy of serving better-quality borrowers, our proportion of category A-and-B borrowers in the China market further expanded to 80% of our total borrowers in the second quarter, compared with 74% in the same period last year.

Furthermore, our transition to better-quality borrowers helped us to further optimize our funding cost during the quarter.

We have also expanded our number of cumulative funding partners to 82 financial institutions, and our pipeline of potential partners remains robust. All these operational improvements enable us to maintain a healthy take rate of around 3.1% during the second quarter.

As a company deeply committed to social responsibility, we continued to support small business owners during this challenging period. We have also noticed that our small business owners' segment has been recovering at a healthy pace. Most of our borrowers from this segment are focusing on wholesale, retail, food and beverages industry.

During the quarter, we served around 459,000 small business owners and facilitated RMB11.5 billion of loans for them, representing an increase of around 11% compared with the same period last year and up 12% sequentially.

Now I'd like to share some additional details on our international expansion efforts. Indonesia, our largest overseas market, recorded continued growth in its macro-economy during the second quarter. Notably, on a monthly basis, the Manufacturing PMI grew by 2.2 points to 52.5 points, and the Business confidence index reached 99%. Indonesia's economy continued to remain robust in the second quarter and has maintained growth of 5% over the past several quarters.

Going forward, Indonesia economy is expected to maintain growth of around 5% in 2023. We anticipate that its domestic consumption will remain robust.

We are excited about the progress we've made in our overseas markets across multiple operational and financial metrics. Cumulatively, we have served over 4 million borrowers in Indonesia and the Philippines and continue to demonstrate significant growth in these countries, with the number of unique borrowers served during the quarter reaching a new high at 786,000, up 22% from the same period last year.

International transaction volume soared by 100% year-over-year during the second quarter, reaching RMB1.8 billion, while we set a new record in our outstanding loan balance at RMB1.1 billion, up 131% year-over-year.

Our operations in the Philippines have also exhibited stronger-than-expected growth across numerous operating metrics. On a year-over-year basis, the number of unique

borrowers, transaction volume and outstanding loan balance all grew by several times compared with the same period last year.

Alongside these impressive operational metrics, international revenue maintained its robust growth trajectory, reaching RMB503 million, an increase of 112% year-over-year, and contributed around 16% of total revenue in the second quarter.

We have consistently strengthened our relationships with both local traditional financial institutions, such as Bank Permata and OCBC bank, as well as innovative internet banks such as Bank Jago and Sea Bank. Thanks to these flourishing partnerships and our partners' validation of our technologies and operational capabilities, our percentage of loans in the second quarter facilitated by these institutions reached 65%, compared with 39% in the same period last year.

Going forward, we will further deepen our relationships with these institutions to increase our proportion of facilitation by local institutions and expand our network of local partners in the region.

Driven by our ongoing investments in technology and our strategic shift toward serving better-quality borrowers, our net revenues for the second quarter rose to RMB3.1 billion, up 15% year-over-year. Net income for the second quarter reached RMB590 million, up 1% year-over-year.

Our leverage ratio, which is defined as risk-bearing loans divided by shareholders' equity, remained stable at 4.3x.

During such times of uncertainty, our strong balance sheet and liquidity position continue to provide confidence to all our stakeholders and support the business growth for all our markets. In particular, our cash position remains robust with over RMB8.2 billion of cash and short-term liquidity as of the end of June 2023, representing an increase of 58% year-over-year and 6% quarter-over-quarter.

We also remained committed to optimizing shareholder value through our annual dividend policy and share repurchase policy. We believe the current macro environment offers an attractive opportunity to return value to shareholders, and as such, during the first half of the year, we deployed around US\$46 million to repurchase our stock from the secondary market.

As of June 30, 2023, we have cumulatively returned US\$491 million to our shareholders through our dividend and stock repurchase programs.

In addition, our Board of Directors has also approved a new share repurchase program of USD150 million, reflecting our strong commitment to enhancing shareholder value.

On a related note, our Chairman and other senior management have also expressed their confidence in the company through personal shares repurchases totaling around 630,000 ADS in the first half of 2023.

Given favorable macroeconomic conditions in our international markets, and the progress we have made across numerous operational metrics for our international business, the Company has increased its international transaction volume guidance for the full year of 2023 to RMB7.7 billion, representing year-over-year growth of around 80%. Taking the current China macro environment into consideration, the Company's 2023 guidance for its China market remains unchanged at between RMB189 billion to RMB205 billion, representing year-over-year growth of between 10% to 20%.

Before I conclude my remarks, let me provide some additional color on our business outlook for the third quarter of 2023. Despite some uncertainties in the macro environment, our business trajectory remains solid.

We expect our transaction volume in China for the third quarter of 2023 to be around RMB49 billion, representing an increase of around 10.4% year-over-year. We expect our transaction volume in international markets for the third quarter to be around RMB1.9 billion, representing an increase of around 73% year-over-year.

In summary, our outstanding performance in the second quarter of 2023 underscores our dynamic business model, technological knowhow, and dedication to advancing our international initiatives.

Entering into the second half of 2023, we remain focused on refining our risk assessment and management framework, expanding our healthy customer base and optimizing our product mix. Looking ahead, we believe that we are well positioned to capitalize on the massive opportunities in both China and International markets, driving growth while creating greater value for our customers, shareholders and all of our stakeholders.

With that, I will conclude my prepared remarks. We will now open the call to questions. Operator, please continue.

Questions and Answers

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

Yada Li: (Speaking foreign language). My first question today is about asset quality trend. Considering the current macroeconomic condition, what is the latest trend of the leading indicators like Day-1 delinquency through July and August? And what can we expect going forward? And how will it affect our provision strategies?

And my second question is related to the international business. Could you please give us more color on the update, such as the progress of business expansion in new countries, business model and long-term strategic goals?

Tiezheng Li: (Speaking foreign language).

Jiayuan Xu: This is Jiayuan Xu, let me do the translation for Alexis.

(Translated). Your first question is related to our risk assessment performance. As mentioned, our vintage delinquency performance is around 2.3%, and it has always been around 2.3% levels over the past 3 years. And our 30-day loan collection recovery rate is around 90%. And over the last few quarters, these metrics have been relatively stable. And our vertical delinquency rate is at 1.68%, which is also at a low level.

From observation, the current macro environment is relatively weak with recovery expectation. And from observation, the credit market is doing okay, and we expect that it is going to maintain stable going forward with risk performance staying stable as well. We have been through multiple credit cycles including the Covid and the lockdowns, and we have proved that throughout all these cycles, we have successfully navigated them and succeed after all these cycles.

Tiezheng Li: (Speaking foreign language).

Jiayuan Xu: So let me do the translation for Alexis.

(Translated). As we know, we are already in the leading position in Indonesia and the Philippines market. And apart from these countries, we are also looking at opportunities in other countries in Southeast Asia and also looking for high-growth opportunities in countries, such as Africa and Latin America. Our business model is not only restricted to online lending; we are also looking at other opportunities.

For example, we are looking at opportunities in Indonesia for offline consumption scenarios. And as you know, the population in Indonesia is young, and we are looking with leading mobile phone branders in the Indonesia market to target these borrowers for mobile, offline mobile consumption.

Do you have any further questions?

Yes, the CEO would like to offer a few more lines.

Tiezheng Li: (Speaking foreign language).

Jiayuan Xu: Now let me translate for Mr. Li.

(Translated). As you know, FinVolution was established 16 years ago, and we are very experienced in different business models, such as online/offline and has very good relationships with different partners. Some of the business models might not work in China market, but is useful for penetration into other countries. As you know, we also not the earliest company to penetrate into overseas market, but we are in leading position in Indonesia and the Philippines because of our tech capabilities, our operational capabilities and also, we have a huge base of talent pools. And with these advantages, we are able to

leverage our leading capabilities and technologies in our overseas market. And going forward, we are confident for further success in all these international markets.

Tiezheng Li: Okay. Thanks, Yada. And operator, please continue.

Operator: Frank Zheng of Credit Suisse.

Frank Zheng: (Speaking foreign language). The first [question] is a follow-up on the international markets. From a medium-term perspective, for example, 1 years' time, how would you foresee the profitability of international market operations?

And the second question is on [domestic] market. Do we have plans to further attract prime customers with APR 18% in order to further expand the volume, as well as improve the risk performance?

Tiezheng Li: (Speaking foreign language).

Jiayuan Xu: Let me do the translation for Alexis.

(Translated). Okay. In the midterm, regarding our international market profitability, our international business is already profitable in the second quarter. But it is still relatively small compared to the China market. There are several reasons for this. Number one, it is affected by the rapid growth for our international business as we need to invest continuously. For example, our percentage of new borrowers in the Indonesia market is around 37%. And also, it is being affected by the deferred revenue policy because all these loans are conducted in installment loans.

Jiayuan Xu: Let me translate for Alexis for this question.

(Translated). In the second quarter, we further optimized our pricing to 22.3% from 22.7% in the first quarter. As you have seen, we are continually trying to acquire better-quality borrowers. Through our historical experience, lower pricing helps us to attract better-quality borrowers, and better-quality borrowers will have a higher level of stickiness on our platform.

And if you observe, we have also higher ROA compared to the industry average. And in the second quarter, our ROA from our reported earnings was about 3.7%. And we have also optimized our funding cost structure by around 30 bps in the second quarter. And going forward, we will consider a balance between pricing and our ROA.

Tiezheng Li: Okay. Frank, do you have any other follow-up questions?

Frank Zheng: No, that's all. Thank you very much.

Operator: Alex Ye of UBS.

Alex Ye: (Speaking foreign language). So my first question is on the shareholder return. So we're happy to see management announce USD150 million of share buyback plan,

which shows management's focus on informing shareholder value. So if we go back to your track record on this buyback, how should we consider your pace on deploying such (indiscernible) going forward? Should we consider the 150 million focus be deployed over to year horizon, as indicated by your organization [experience]?

And also, is there any target payout ratio, if we take into account both your dividend and buyback?

Tiezheng Li: Hello, Alex. (Speaking foreign language).

Jiayuan Xu: Hello, Alex, let me do the translation.

(Translated). Share repurchase and buyback programs began in 2018, and we already have a period of track record. And cumulatively, we have return about USD262 million in the form of dividend to our shareholders and 230 million for share repurchases. In total, it is about USD500 million returned to our shareholders. And our payout ratio is around 30% to 40%.

In terms of absolute amount, we are ahead of our peers. In the first half of 2023, our buyback amount is close to 50 million and the payout ratio for our annual dividend was [18.5]%. So the payout ratio for 2023 is slightly to be higher than our historical average.. And as long as the market conditions allow and is favorable, we will continue to return value to our shareholders as validated by our past historical performance.

Tiezheng Li: Okay. Alex, is it okay for you?

Alex Ye: Thank you.

Operator: Thomas Chong of Jefferies.

Thomas Chong: (Speaking foreign language). My question is about the competitive landscape in overseas market. Can management share your thoughts about the future outlook? And on marketing spending, given the report about Facebook is one of our channels, can you comment about the customer acquisition cost in overseas versus domestic market?

Tiezheng Li: (Speaking foreign language).

Jiayuan Xu: Hello, Thomas, let me do the translation.

(Translated). As you have known, our operations are mainly in the Indonesia and Philippines market, and the macro environment in these countries are relatively positive. For example, in Indonesia, the GDP growth has been growing at over 5% for the last 7 quarters. And in 2023, the GDP growth is expected to maintain at around 5%. The Philippines market is slightly slower compared to the Indonesia market, but the GDP growth is still growing at around 4.3%. And the reason why we are able to maintain our leading status position in these countries is because we have deployed our technological capabilities and operational capabilities in these countries.

And in the second quarter, our number of unique borrowers has also reached a new high at 786,000, and we are constantly among the top-three players. These markets, Indonesia and Philippines, are huge markets, and are at early stages for us. So we will continue to invest and maintain leading position in these countries, as supported by our technologies and operation capabilities.

Our efforts and capabilities have also been recognized by local financial institutions. For example, this can be validated by the increase in the proportion of loans funded by local partners from 65% in the second quarter compared to only 39% in the same period last year.

For sales and marketing, the amount we spend is around RMB80 million, has been invested into sales and marketing in the second quarter. And apart from Facebook, we are also advertising on Tik Tok. We believe all this information from these channels will be good channels for us to acquire our new borrowers going forward.

Tiezheng Li: Okay. Thomas, do you have any other questions?

Thomas Chong: (Speaking foreign language). My question is about AI. In the prepared remarks, we talk about we have been investing in AI for many years, and that's why AI, in different scenarios, different (inaudible) such a hot topic in the internet sector these days. And people talk about big data model or industry industry model. Just want to get some thoughts from management with regards to this area (inaudible) thinking of developing our own big data model or we are seeking a partnership with the top players?

Tiezheng Li: Thank you, Thomas. (Speaking foreign language).

Jiayuan Xu: Hello, Thomas, let me do the translation for Mr. Li.

(Translated). Honestly, the generative data model is not for a company of our size, as it needs to be at a country level where huge resources are required for development. Our focus is on the implementation of AI models into our operations and to our daily operations in order -- in an attempt to increase our efficiency. And also, we will be looking at specific opportunities that (inaudible) for deployment into our business where we can also consider to work with other partners to increase our efficiency.

Operator: Cindy Wang of China Renaissance.

Cindy Wang: (Speaking foreign language). So I have two questions. The first question is related to the overseas institutional funding. So we've seen that institutional funding has been going up pretty quickly. So in the meantime, what's the percentage contribution will be contributed from the institutional funding?

The second question is related to provision. So we see the asset quality has been improving in second quarter. However, the provisions, compared to first quarter, have been slightly up. So can we talk about what's the difference between here, and whether we have any write-back in the second quarter? And how do we foresee the provision in the second half of this year?

Tiezheng Li: (Speaking foreign language).

Jiayuan Xu: Cindy, let me do the translation.

(Translated). As mentioned, we have around 65% of the loans in Q2 were funded by local Indonesian partners in the second quarter. And we expect this amount to be around 80% by the end of the year. Going forward, we still think that there's opportunity for us to further increase this proportion, but our main focus will be on the funding costs where we need to do some optimization on our funding costs for the international markets.

Going to the next question, when we take a look at provisions, we need to divide into domestic and international provisions. The main reason is because our international business is growing rapidly. This is the reason for the provisions that have to be higher. In the first quarter, there was a write-back. And now if you take a look at the domestic China recovery, the recovery is still weak and below expectations. So we don't have any plans for a write-back at the moment, but all this will change when the economy is recovering at a faster pace and there will be opportunity for write-back going forward.

Tiezheng Li: Okay. Thanks, Cindy.

Cindy Wang: (Speaking foreign language).

Operator: At this time, I'd like to turn the call back over to the Company for closing remarks.

Jimmy Tan: Thank you once again for joining us today. If you have further questions, please feel free to contact me or my Investor Relations team. Thank you so much.

Operator: This concludes this conference call. You may now disconnect your line. Thank you.