PPDAI Group Inc. [PPDF]
Q3 2017 Earnings Conference Call
Wednesday, December 13, 2017

Company Participants
Sally Huo; Investor Relations Manager
Cliff Jun Zhang; Chairman and Chief Executive Officer
Simon Ho; Chief Financial Officer
Feng Zhang; Chief Operating Officer

Analysts
Alice Li; Credit Suisse
Daphne Poon; Citigroup
Sanjay Sakhrani; Keefe, Bruyette & Woods
Chris Birney; JPMorgan Asset Management
Matthew Larson; Wells Fargo
Tian Hou; T.H. Capital

Presentation

Operator: Hello, ladies and gentlemen. Thank you for standing by for the third-quarter 2017 earnings conference call for PPDAI Group Inc., also known as Paipaidai. At this time, all participants are in listen-only mode. After management's prepared remarks, there will be a question-and-answer session. Today's conference call is being recorded. I will now turn the call over to your host, Ms. Sally Huo, Investor Relations Manager for the Company. Sally, please go ahead.

Sally Huo: Hello, everyone, and welcome to the Paipaidai third-quarter 2017 earnings conference call. The Company's 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 distribution list by visiting the IR section of our website at ir.ppdai.com.

Mr. Cliff Jun Zhang, our Chairman and Chief Executive Officer, and Mr. Simon Ho, our Chief Financial Officer, will start the call with their prepared remarks. Mr. Feng Zhang, our Chief Operations Officer, will join the call during the question-and-answer session.

Before we continue, please note that today's discussion will contain forward-looking statements made under the safe harbor provisions of the US 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 is included in the Company's filings with the US 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 on our results for the quarter.

I will now turn the call over to our CEO, Cliff. Please go ahead.

Cliff Jun Zhang: Hello, everyone, and thank you for joining our first -- we are pleased to report our first earnings as a public company. For the third quarter 2017, we reported total operating revenues of RMB1.25 billion, an increase of approximately 245% over the same period last year.

As of September 30, 2017, Paipaidai had 57.6 million registered users and approximately 9 million cumulative borrowers, making us one of the largest online consumer finance marketplaces in China. Our expanded user base led to robust growth in loan origination volume, which increased by 256.5% year over year to RMB21 billion in the third quarter of 2017.

Our successful IPO in mid-November was an important milestone and testament to our consistent strategy and execution, continuous innovation and solid 10-year track record, which is the longest operating history of any online lending platform in China. I'd like to take this opportunity to state a few key points about our business.

First, we are a technology-driven marketplace platform that matches underserved borrowers who need consumer loans with investors who have limited investment options in the market. Our growth is not limited by capital requirements, making our business highly scalable.

Second, we are a market leader and have a massive proprietary dataset.

Third, we have proven technologies and core end-to-end capabilities ranging from our diversified and low-cost borrower acquisition to our highly effective risk management system. We deploy advanced big data and AI technologies across each stage of our business to improve operational efficiency and risk management capabilities.

Finally, we have a large and loyal retail investor base. Our strong retail investment business is a key competitive advantage and an important source of operational stability and sustainability, as we see retail funds being more stable than institutional funds. We plan to leverage our large investor base to build a wealth management business and create a second engine for sustainable long-term growth.

Before I conclude my prepared remarks, I also want to say a few words on regulation. We have always and will continue to fully embrace and implement government regulations. We believe an improved regulatory framework will lead to a more orderly and healthy competitive landscape. With our large scale and strong core business, Paipaidai is well positioned to consolidate the market and gain market share in the long run and capture the massive opportunities in China's consumer finance market. We will continue to fulfill our mission of utilizing the most innovative technologies to deliver highly accessible and convenient financial services solutions.

With that, I will now turn the call over to our CFO, Simon Ho, who will discuss our financial results and an update of our business.

Thank you.

Simon Ho: Thank you, Cliff, and hello everyone.

We delivered a strong quarter with excellent operational and financial performance. While many of our third-quarter operating metrics and financial results were disclosed in our IPO offering prospectus, I'd like to take this opportunity to draw attention to a few highlights. In the third quarter, we achieved significant improvement in our operational efficiency, as we continued to benefit from strong operating leverage provided by our technology-driven and highly scalable marketplace platform. As such, our operating margin increased to 46.4% in the third quarter of 2017, compared with 33.1% in the same period of last year, and our operating income reached RMB579 million, representing a 375% increase year over year.

Before diving into a more detailed look at our financial results, I'd like to share with investors a few recent business developments.

As investors know, recently issued government regulatory policy changes have placed a 36% cap on total annualized borrowing costs. We fully embrace and endorse this new regulatory measure and have adjusted our lending products to meet this 36% cap requirement. Paipaidai has a long operating history demonstrating a strong culture of compliance with industry regulations. I echo Cliff's earlier statement that we will always embrace and strive to implement government regulations.

We believe this new policy of capping total annualized borrowing costs will not have a significant impact on our business. Putting the requirement in perspective, it mainly affects our Handy Cash Loan business, one of our smaller product lines that represented approximately 7% of our total revenues for the first nine months of 2017, and a small number of core standard loan products for which we are now focusing on loan originations with longer terms of approximately 9 to 12 months. We have a wide and dynamic product portfolio and believe that going forward the impact to this small part of our business can be easily offset through product mix adjustments.

Secondly, in light of the tightening regulatory environment we've decided that, effective January 1, 2018, we will discontinue operating our investor reserve funds. We made this decision in a proactive manner and believe it is well aligned with the new regulations and removes any chance of misperception in the minds of consumers that the investor reserve funds provide an unlimited guarantee. Practically speaking, this decision will not have a material impact on our operations, as, going forward, we expect the spread between the return on our underlying assets and the return we give to investors in our investment programs will continue to exist and will continue to be reflected in our income statement. We are in close discussion with our auditors regarding the future accounting treatment on this matter, and will update the market in due course.

Now, I'd like to walk you through our detailed financial results for the third quarter of 2017.

As Cliff mentioned, the 245% year-over-year increase in operating revenues for the third quarter was primarily due to the increase in loan facilitation fees, post-facilitation service fees and other revenues as a result of the substantial increase in loan origination volume.

Loan facilitation service fees increased by 194% year over year to RMB907 million for the third quarter of 2017, primarily due to the substantial increase in loan origination volume and the number of unique borrowers on our platform.

Post-facilitation service fees increased significantly, by 942% year over year, to RMB200 million for the third quarter of 2017, primarily due to the substantial increase in loan origination volume and the rolling impact of deferred transaction fees. Note that our post-facilitation service fees represent the portion of transaction fees received from borrowers in relation to services we provide after loan origination, such as the facilitation of loan repayments. This portion of transaction fees is deferred and recognized over the life of the loan.

Other revenue increased by 307% year over year to RMB143 million for the third quarter of 2017, primarily attributable to an increase in loan collection fees.

Net interest income and loan provision losses for the third quarter of 2017 was an expense of RMB3.4 million, compared with an income of RMB5.7 million in the year-ago period. This was primarily due to provisions for expected loan losses related to the trusts that were newly set up during the period. Note that trusts are a method for institutional investors to invest on our platform and we may co-invest with these investors. A provision reflecting the expected loan losses is made upfront while the income is recognized over time, so there is a timing difference in recognizing the provisions and income.

Origination and servicing expenses increased by 172% year over year to RMB298 million for the third quarter of 2017, primarily due to the increase in headcount particularly for consumption loan products and loan collection services, and to a lesser extent, an increase in referral fees paid to third parties for successful loan originations.

Sales and marketing expenses increased by 140% year over year to RMB225 million for the third quarter of 2017. The increase was primarily due to the increase in expenses associated with online customer acquisition cost, which mainly include expenses paid to internet marketing channels for online advertising and search engine marketing as well as to certain websites that enable Paipaidai to reach quality borrowers.

General and administrative expenses increased by 235% year over year to RMB145 million for the third quarter of 2017, primarily due to the increase in staff costs.

Other income increased by 30% year over year to RMB121 million for the third quarter of 2017. Other income primarily consisted of RMB131 million gain from the quality assurance fund resulting from the growth in loans facilitated on the platform that are protected by the quality assurance fund; a RMB42.4 million realized gain from financial guarantee derivatives due to the amount of investment programs maturing during the year; and a negative RMB67.4 million fair value change of financial guarantee derivatives due to an upward adjustment in the expected default rate for loans underlying outstanding investment programs resulting partly from our testing and experimentation in new products and customer segments.

Income tax expense was RMB158 million for the third quarter of 2017, compared with RMB21.3 million for the third quarter of 2016. The increase was primarily due to the improved profitability in the third quarter of 2017.

Because of the foregoing, net profit increased to RMB541 million for the third quarter of 2017 from RMB134 million (sic -- see press release; RMB193.5) in the year-ago period.

Net loss attributable to ordinary shareholders of the Company was RMB279 million for the third quarter of 2017, compared with net income attributable to ordinary shareholders of RMB60.8 million in the year-ago period due to the accretion losses on our Series A, B and C preferred shares.

Turning to our balance sheet, we have a solid balance sheet and ample liquidity. As of September 30, 2017, we had cash and cash equivalents of RMB715 million and short-term investments, mainly in money market funds, of RMB1.5 billion. These figures exclude the US$271 million of proceeds raised in our IPO and the concurrent private placement.

It is important to note that our investor protection programs are adequately funded. Firstly, the total balance of our quality assurance fund, which includes restricted cash of RMB930 million and the quality assurance fund receivable of RMB975 million, was equivalent to 16.6% of the total outstanding loans protected by the quality assurance fund. Secondly, the total balance of our investor reserve funds, which includes restricted cash of RMB194 million and the financial guarantee derivative of RMB245 million, was equivalent to 4.5% of the total outstanding loans protected by the investor reserve funds.

I'd like to turn next to provide an update pertaining to an accounting treatment change.

To fully comply with recent regulatory announcements, since last week we have discontinued charging upfront transaction fees on all our loan products and changed to a monthly fee model. We are now collecting transaction fees to be repaid over the first three months of the loan. This adjustment will impact the accounting treatment for the recognition of our loan facilitation service fees for the remainder of December, in accordance with existing US GAAP accounting standards. I say, "for the remainder of December" because, effective January 1, 2018, new US GAAP revenue recognition standards take effect that will allow us to recognize our loan facilitation service fees as revenues upfront upon loan origination.

So in essence, from an accounting perspective, it is only for the brief period in December that our accounting treatment is impacted. To be clear, there will be a small impact in the fourth quarter, but it will only be limited to three to four weeks in December. Because the revised GAAP recognition standards become effective January 1, the adjustment to our transaction fee model will not have any meaningful impact on our reported revenues in 2018. We have undergone extensive discussions with our auditors on the new standards and they are in agreement with this treatment.

Now before we turn the call to questions, I'd like to close with a few comments on our business trends.

In light of the recent uncertainty in the market, we have begun to take a more conservative stance on our lending activities in an effort to manage our risk. Overall, the industry is currently undergoing a tightening that could have an impact on our business in the short-term, as some players adjust and some players exit the market.

Having been through multiple lending and economic cycles, we know the current market uncertainty is just a bump in the long road that is before our industry. We see this development as necessary growing pain that always precede development and eventual maturity. Ultimately, we believe these changes will lead to consolidation in the market and allow for healthy growth in the long term.

In view of these current conditions, we expect fourth-quarter loan volumes will be approximately 15 to 25% south of third-quarter 2017 levels. We believe this is only temporary, and we have taken appropriate cost structure adjustments during this time. At the same time, we are closely monitoring industry trends to be agile in making adjustments when market cycles occur.

We fully expect our industry will continue to go through changes that are necessary to create a healthy environment not only for companies in our space, but for all consumers in China. As Cliff has said many times in the past, we have just begun our evolution as a public company and we will remain focused on the long-term growth and prosperity of our company. China has over 440 million people underserved by the traditional banking system. This is larger than the total population in the US and presents a significant growth opportunity for us. As a technology-driven marketplace, our goal is to continue to grow and flourish as a leader in the online consumer finance marketplace industry and stay at the forefront of change and innovation.

Finally, I'm pleased to announce, as disclosed earlier today in a press release, that Paipaidai has entered into a joint cooperation partnership with Sun Hung Kai & Co., to jointly explore collaboration opportunities including new products, internet technologies, as well as asset and funding sides for each party. Sun Hung Kai & Co. is a leading Hong Kong based investment firm with a diverse portfolio of financial services businesses and became Paipaidai's strategic investor at the time of our IPO. We are excited to be collaborating with Sun Hung Kai & Co., and I encourage investors to reference today's press release on this announcement for further details.

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

Questions and Answers

Operator: (Operator Instructions) Alice Li; Credit Suisse.

Alice Li: Hi. Thanks for taking my question. This is Alice from Credit Suisse. So I have two questions. The first question is about the recap. So you mentioned that you have made adjustments to comply with the 36% borrowing cost limit. Could you please explain more about the adjustments and how does this affect your transaction fee rate? This is my first question.

And my second question is about your asset quality. Because we know that the vintage delinquency ratio for the second-quarter loan was higher than before and the delinquency ratio in terms of the balance, saw a similar trend. So what are the main reasons?

And you also mentioned that the recent tightened regulation led to some -- the exit of many payday loan players. So I would like to know what's the latest trend of your delinquency ratio and how are you mitigating that impact. Thanks very much.

Simon Ho: Thank you, Alice, for your question. I will take the first question and Feng, our COO, will take the second question.

Regarding your first question with respect to what changes have we made, obviously for loan tenures we are now originating at the longer end of our range for our standard loan products, limiting to 6 to 12 months, but mostly 9 to 12 months. We had adjusted the quality assurance fund contributions slightly higher for certain core categories to protect against risk.

With regard to the take rate, we have made some adjustments but it's too early to confirm the eventual impact, because it's only been a week since the change. So far, from what we have seen, the impact on our transaction fee has been relatively neutral. It's been little changed versus before we made our changes. Specifically, we have lowered our fee rate for higher-risk credit levels, but have offset this with slight increases for lower-risk credit levels.

So it's still too early to confirm the trend because, as you can see, the mix of the originations between the various credit levels is also an important factor that determines the overall transaction fee that you see. But so far, from what we've seen, the change has been relatively neutral.

And I'll hand over to Feng for the second question.

Feng Zhang: Sure. Thanks, Alice. This is Feng. I think there are really two parts to your question. One is we have seen some delinquency rise as of September 2017 from our portfolio vertical loss level table. And the second question is what [are we seeing] our risk level and given the recent regulatory developments.

For the first question, it is really, as we have communicated in the road show as well, we have a targeted risk target, of 4 to 6%. And if you saw our vintage loss curve, our loss level for the past two years, vintage level is around 4 to 5%. So given that, we have been doing some testing and experimenting in new products at our customer segments in the first half of the year. And that drives certain level of delinquency rise as we observed in Q3 2017, which is well expected, within our expectations.

Now for the second part of the question, yes, we have seen an increase recently due to recent regulatory development. I would say it is still very early observation and it is too early to call the ultimate impact. Now we are very closely monitoring and have proactively taken some measures, including tightening our credit policy for new bookings. We believe the impact will be short term as it is a credit squeeze caused by some payday loan players quitting the market and making adjustments. And the payday loans have very short period -- very short durations.

I want to call out we have been very conservative in this management in the past years and have built up a very healthy risk reserve, including the two protection funds, as Simon has mentioned in his earlier remarks.

Now going forward we also believe tighter regulation will lead to healthy environment. And overall the market opportunity remains vast. And Paipaidai as a leader is well positioned to consolidate the market. And realizing fast developments are after a temporary short period.

Alice Li: Thanks very much. And so could I have a follow-up question as well?

Simon Ho: Sure, go ahead, please.

Alice Li: You mentioned that the impact on the delinquency ratio, or the length of the delinquency ratio, might be short term. But do you have an estimate of how long the credit cycle will last or how long could we see the peak of the delinquency ratio?

Feng Zhang: That's a good question. I'm afraid I think at this stage it's just very, very early, and it's very, very difficult to call. And I think our guess is it probably will last maybe, like one, to three, four months. And the guess would based on the fact that most of the payday loan players are -- they're loan tenure is around one month, two, three months. So the squeeze is really caused by most of these players making adjustment. Some of those could leave the market. And if that is the case, I think the peak is probably going to -- you know, in the next quarter or so time.

But, again, I think it is very early. It is very difficult to predict. I think what we will do is we will very closely monitor the trend, checking all the leading indicators, keep nimble and keep agile and adjust our strategies accordingly and very quickly.

Alice Li: Thanks very much.

Operator: The next question comes from Daphne Poon of Citi.

Daphne Poon: Hi, Management. Thank you for taking my questions. So I've got the pile of questions here. The first one is regarding the investor reserve fund. So if you are stopping the IRF -- actually management is to remove any, like, regulatory concern regarding the offering of guarantee. Does that mean any chance that we may also stop offering the quality assurance in the future due to further regulation tightening, if that is also follow up on credit enhancement to the investors?

And regarding the IRF, what will we do with the remaining pool funds in the IRF? And also, how will that impact on the investor return for the investment program after we stop the IRF arrangement?

And the second question is regarding the APR cap. So given that we notice that actually moves of our standard loans under credit level grade 4 to 7, they are mostly well above the 36% APR. So will we actually can see the reducing loan exposure to these risk tier borrowers and shifting to more prime borrower? And given that you're trying to lengthen the loan duration to get around the APR cap, how do you see that impacting on our delinquency rate and our forward looking going forward?

And the third part of the question is regarding the partnership with Sun Hung Kai Co. So can you share with us more detail regarding what are the expected initiatives in terms of this cooperation? Thanks.

Simon Ho: Okay, Daphne, I will try to remember all your questions. So the first question, if I remember correctly, is about whether our quality assurance fund will remain or not. And we have not received any specific regulatory notification to stop or change our quality assurance fund. And our belief and understanding is that the regulator is not objecting investor protection but are against platforms providing unlimited guarantees. Okay? I think that's sort of where we think things are.

The second part to your first question is about the investor reserve funds and how -- basically what impact will this have. And we are still discussing internally how this new system will work in the future. But we don't believe investor protection systems will go away. And we'll obviously continue to monitor our -- any feedback we get. And also, from a financial perspective, as I said before, we expect the spread between the return on our underlying assets and the return we give to investors in our investment programs, it will continue -- this spread will continue to exist and will continue to be reflected in our income statement. So overall we don't expect this change to have a material impact on our business.

Now to your second question, if I get it right, your second question was firstly whether we are originating higher quality credits as opposed to previously. Is that correct?

Daphne Poon: Yes.

Simon Ho: Yes, I think in this environment we have obviously leaned on the conservative side. We are generally being much more conservative than earlier in the year. And, yes, so the answer is yes, we are leaning towards the higher quality borrowers at this stage.

And, sorry, the second part of your question was --?

Daphne Poon: It's about the measure to lengthen the loan duration -- how do you see that impacting on your delinquency rate and also your borrower stickiness, the repeat ratio.

Simon Ho: Yes. The repeat ratio will suffer a little bit as a result, because previously as you remember, in the first nine months of the year our average loan duration on the platform was about I think close to eight months. However, I think moving from an average tenure of 8 months to between 9 to 12 or 9 to 10 ultimately we don't think is going to have a material impact in the risk profile of our business.

And, Daphne, on the final question on Sun Hung Kai, so I think maybe just to give you a bit of background, of course Sun Hung Kai through UA Finance, they have a proven track record in consumer finance, with a leading position in Hong Kong and 10 years of history in mainland China. Obviously they -- is a strategic investor in us. And we believe their strategic partnership with us is a clear validation of our business model and core capabilities.

It is early days and we are obviously trying to, looking to areas to collaborate across the range of our business lines. So it is -- we are looking at this at the moment.

Daphne Poon: Okay, thanks. Actually, can I follow up for a bit on the IRF? So actually is the move to suspend the IRF arrangement due to regulatory pressure, or any notice from the regulator or is it our own proactive approach to suspend?

Simon Ho: So, Daphne, so as disclosed in our IPO prospectus, the authorities have commented on our IRF reform and they asked us to change the way we market this protection system in order to avoid misperception by investors that our investment programs are fully guaranteed. And as I said, our understanding is not that the regulator objects to investor protections and we have therefore decided to proactively discontinue our IRF to avoid any potential misperception.

Daphne Poon: Okay. Thanks.

Operator: The next question comes from Sanjay Sakhrani of KBW.

Sanjay Sakhrani: Thank you, and congratulations on the IPO. I guess I'm trying to pull up and think about 2018 and the respective implications. It sounds like the Handy Cash Loan you think you can offset doing the standard loan product. The IRF, Simon, you're saying is not a material impact. So when we think about the implications to 2018, is it just the origination volumes and whatever impacts there might be to credit and how it affects the QAF and the IRF?

Simon Ho: Yes, I think Sanjay, as you know, our top line is obviously very dependent on loan origination values. And I think your assessment would be largely correct.

Sanjay Sakhrani: And then when we think about this 15 to 20% decline in originations you're expecting, I mean, that's how we should think about 2018? Or is it too early to say?

Simon Ho: As we've previously discussed, I think it's -- clearly it's too early to say. We are, as our COO has said, we are keeping nimble, agile. We are paying close attention to what the indicators of our business and will adjust accordingly.

Sanjay Sakhrani: Okay. I'm also trying to understand the IRF piece and sort of the resetting of it and how it will work going forward. Maybe you could just go back and explain, Simon, sort of what happens with the IRF on a go-forward basis and then what happens in terms of the wind-down of the excess that's in there, given you're discontinuing that fund.

Simon Ho: I think, Sanjay, as we said before, we are still looking internally in how this new system will work. And we are still in discussions with our auditors in terms of how the accounting treatment will play out in the future. So at this moment I think it would be premature to try to give too much -- too many comments on this piece.

Sanjay Sakhrani: Okay. And I want to be clear. The QAF, that would be a part of the rate cap that they have instituted. Is that correct?

Simon Ho: Yes, we have assumed and we've built that into the 36% cap.

Sanjay Sakhrani: Okay. So to the extent that you guys winded the QAF, you can enhance the yield in some capacity to account for the risk that you're taking on.

Simon Ho: I guess technically yes, because we have been running a policy of requiring higher contributions from borrowers into the QAF than our expected payout. So if you -- what you're implying is that without the QAF, then there is none of this excess contribution required. Right? From that perspective I think your logic may be correct.

Sanjay Sakhrani: Okay.

Simon Ho: Again, I think we're speculating too much here again.

Sanjay Sakhrani: No, I'm not (inaudible). There's a lot in (inaudible) then. And two more questions. Just on the funding again and as part of the IRF is concerned, a decent amount of your investors take the IRF. As we look ahead, do you think it affects their appetite to want to invest with you all?

And then as you sort of deemphasize the retail channel for now, how are you staying relevant and engaged with those people so that they come back when you need them?

Simon Ho: Yes. I think in terms of the volume mix, the IRF portion of the volumes have been coming down. And we would anticipate that it will run at a lower level than before.

And in terms of how our investors will react, again, we no longer market the IRF protection to our investors. But, as I said earlier, we don't believe our investor protection systems will go away. And, as such, we will continuously monitor investor feedback and minimize any impact that we can see.

Sanjay Sakhrani: Okay. My final question is just on the peer-to-peer license and sort of where we are, if there were any updates. Have there been any constructive movements along that path or anything that you can discuss with us and share?

Simon Ho: Yes. We believe we remain on track for registration as a marketplace vendor. And in line with what we've been telling investors during the IPO is we do hope to receive registration approval in the first half of 2018.

And just to add on top of that, we do not require an online microcredit license to operate. So, because there has been a lot of news lately about online microcredit companies and licensing.

Sanjay Sakhrani: Okay. Well, great. Thank you very much. Those are my questions.

Operator: (Operator Instructions) The next question comes from Chris Birney of JPMorgan Asset Management.

Chris Birney: Hi. My question is about the wealth management initiative that you mentioned. As I understand it, wealth management products are typically not allowed to be sold by peer-to-peer platforms. So I'm just -- I guess you probably didn't mean literally having [new] products in that forum. But can you elaborate more on where you're going with this business initiative?

Feng Zhang: Hi, Chris. This is Feng. I would say, like, the situation has not changed much since we last spoke in the IPO process. I think at this point we -- as you correctly point out, that wealth management requires a certain license. And we are in the still process of acquiring certain licenses.

Operator: Was there a follow-up, Mr. Birney?

Chris Birney: No, thanks. I'll leave it there.

Operator: The next question comes from Matthew Larson of Wells Fargo.

Matthew Larson: Hi. Thanks for taking my call. Isn't the real question about investing with your firm and related firms is that the prices have come down dramatically from where they were just a few weeks ago because of some of these initiatives, but which might truncate some of your top-line growth near term?

But isn't the real investment thesis is that this is kind of a long term coming. It's been pretty much of a Wild West type of industry. But in the long term it should be quite a positive for well-capitalized, established companies like your firm because there's probably thousands of these short-term consumer lenders and only a few hundred will probably survive. So in the long term it would seem to me you would just make it up on volume, even if it's at a slightly reduced fee structure. And also the quality of your borrower is going to be better, because some of the borrowers who are effectively able to borrow funds now will be excluded because people aren't going to be interested in lending them money at a slightly reduced maximum rate. I mean, is that the simple investment thesis going forward?

Simon Ho: Yes. Yes, I think you've pretty much hit the nail on the head. And the reality is that the addressable market remains very significant. The underserved population in China, as we said earlier, is larger than the population of the US. And a lot of lending will move online. The barriers to entry is rising very rapidly due to regulations. The amount of competition will reduce -- already happening right now.

And then clearly the number of well capitalized listed players are few. And we are one of them. And we are already one of the largest in this space in China, with a 10-year operating history, with a proven track record, and very strong core capabilities, from customer acquisition to risk management. And so we are very optimistic about the long-term future of the industry and of Paipaidai's position in that industry. And we anticipate that we should be able to consolidate greater market share in what is a healthier competitive environment going forward.

Matthew Larson: All right. Thank you. Appreciate it.

Operator: (Operator Instructions) And we have a follow-up from Chris Birney of JPMorgan Asset Management.

Chris Birney: So this is a different question, which is about if you think the clearing out of so many competitors and the kind of cooling off of the market, does that help at all on the expense side, about getting ad placement or getting rankings on kind of financial supermarkets, things like that? I was on the Jianpu Technology and they said that they don't think that their pricing is going to move. But I wonder if you think this will produce any benefits on the cost side.

Simon Ho: Thank you, Chris. In terms of customer acquisition costs, again, because a lot of these developments in the industry have been very, very recent. So we'd say that it's too early to see any sustainable, real sustainable, trends and be able to really quantify where things will settle.

In the short term I can describe to you what we expect of some of the trends, is we do expect that the CPA -- this is the cost per registered account in the market -- will decline. But also, our conversion rate in the near term will also decline, as we tighten our credit risk standards. So there's two offsetting items here in the near term. But in the longer term as the industry consolidates, we do believe there is room for customer acquisition costs to be more efficient going forward.

Operator: And we have a question from Tian Hou of T. H. Capital.

Tian Hou: Good evening, Management. I have two questions relating to the recent regulations. And two things -- one is, so the regulation request, the type of business you guys are in [meet] a consumption scenario, (in Chinese 消费场景). So I wonder how you guys going to deal with that issue. That's number one.

And number two, in your press release you said you guys are going to cease to collect upfront transaction fees. So I wonder -- what's the impact of this cease upfront transaction fees going to have on your future business? That's my two questions. Thank you.

Simon Ho: Yes, thank you very much. I think your first question is about whether there -- requires a consumption scenario for our type of lending. And the answer is, no, there is no such requirement. The requirement that you read and you see being reported only applies, from our understanding, to online microcredit companies. This is not a requirement for online peer-to-peer lenders. Okay? That's the first question.

Tian Hou: Okay.

Simon Ho: Your second question is about the upfront transaction fee. I'm assuming I don't need to repeat the accounting impact. Right? You're just asking whether users and borrowers will -- whether they'll be an impact. Well, we've been testing this in the last several months, well before the regulations come out. And we believe this is well manageable. We don't see a significant impact. And, of course, the entire industry is moving in this direction anyway.

Feng Zhang: Yes, this is Feng. Just add, this is actually a better customer experience for the borrowers, because -- you know, it's very understandable. You borrow for CNY10,000 and now you get CNY10,000. And you pay the fees in three installments. So (inaudible) better acceptance rate by making this change.

Tian Hou: Okay, I see. Thank you for the answer. It's clear to me now.

Operator: This concludes our question-and-answer session. I would like to turn the conference back over to the Company for any closing remarks.

Sally Huo: Thank you once again for joining us today. If you have any further questions, please feel free to contact Paipaidai Investor Relations through the contact information provided on our website. Thanks.

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