

Event Name: Q3 FY2019 Hexindai Inc. Earnings Call (NASDAQ: HX)

Event Date: February 28, 2019

Corporate Participants

Daisy Wang Hexindai Inc.-IR Director

Xinming Zhou Hexindai Inc.-CEO

Johnson Zhang Hexindai Inc.-CFO

Other Participants

Joshua David Vogel Sidoti & Company, LLC-Analyst

Kaplan Leng Essence Security

Presentation

Operator

Hello ladies and gentlemen and thank you for standing by for Hexindai's third quarter fiscal year 2019 earnings conference call. At this time, all participants are in listen-only mode. After management's prepared remarks, there will be a question-and-answer session. As a reminder, today's conference call is being recorded. I would now like to turn the meeting over to your host for today's call to Ms. Daisy Wang, Investor Relations Director. Please proceed Daisy.

Daisy Wang - Hexindai Inc. - IR Director

Thank you, operator. Hello investors, analysts and colleagues thank you for joining us today. Our earnings release was distributed earlier today and is available on our IR website at ir.hexindai.com.

On the call today from Hexindai are Mr. Xinming Zhou, Chief Executive Officer and Mr. Johnson Zhang, Chief Financial Officer. Mr. Zhou will review business operations and company highlights, followed by Mr. Zhang, who will discuss financials and guidance. They will be available to answer your questions during the Q&A session that follows.

Before we begin, I'd like to remind you that this conference call may contain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements are made under the "safe harbor" provisions of the U.S. Private Securities Litigation Reform Act of 1995. These statements can be identified by terminology such as "will," "expects," "anticipates," "future," "intends," "plans," "believes," "estimates," "potential," "continue," "ongoing," "targets," "guidance" and similar statements. The Company may also make written or oral forward-looking statements in its periodic reports to the U.S. Securities and Exchange Commission (the "SEC"), in its annual report to shareholders, in press releases and other written materials and in oral statements made by its officers, directors or employees to third parties. Any statements that are not historical facts, including statements about the Company's beliefs and expectations, are forward-looking statements that involve factors, risks and uncertainties that could cause actual results to differ materially from those in the forward-looking statements. Such factors and risks include, but not limited to the following: the Company's goals and strategies; its future business development, financial condition and results of operations; the expected growth of the credit industry, and marketplace

lending in particular, in China; the demand for and market acceptance of its marketplace's products and services; its ability to attract and retain borrowers and investors on its marketplace; its relationships with its strategic cooperation partners; competition in its industry; and relevant government policies and regulations relating to the corporate structure, business and industry. Further information regarding these and other risks, uncertainties or factors is included in the Company's filings with the SEC. All information provided in this call is current as of the date of this call, and the Company does not undertake any obligation to update such information, except as required under applicable law.

It is now my pleasure to introduce our Chief Executive Officer, Mr. Xinming Zhou. Mr. Zhou, please go ahead.

Xinming Zhou - Hexindai Inc. – CEO

Thank you, Daisy, and thank you, everyone for joining our call today.

While the quarter remained challenging for us and the entire P2P sector, we have begun to see the environment improve as regulations are clarified and financially weaker and fraudulent firms are gradually weeded out. As we have said before, a clear and definitive regulatory environment will have a positive impact on the industry and allow it to grow sustainably over the long-term. The industry began to recover as the market regains its footing following a turbulent period.

Net revenue during the quarter was US\$1.9 million, while total loans facilitated was US\$29.1 million. While our top line continued to feel the impact from market turbulence, we have begun to see things improve sequentially following the cost cutting initiatives we put in place during the quarter and a re-shifting our focus from loan transfer products back to new loan products as the market rebuilds. Our net loss narrowed sequentially as a result. Meanwhile, the proportion of new loans facilitated to total investment amount increased to 30.4% during the quarter compared to 15.4% last quarter.

We continue to work on completing everything in the notice for a regulatory compliance inspection campaign issued in August 2018 which lays out three key steps for platform self-examination and correction. We were among the first P2P platforms to begin the inspection process and are actively working to complete it as soon as possible. We completed step 2 with the Beijing Internet Finance Industry Association late last year which included an on-site inspection. Hexindai was one of the only firms directly inspected by the Beijing Internet Finance Industry Association in step 2 which is an indication of our leading position and contributions in regulatory compliance. We have now completed two of the three key steps for compliance with industry reforms from the National P2P Rectification Office and are waiting for further instructions for the final step. The third and final step involves verification of inspection results by the Beijing Municipal Bureau of Financial Work with an additional field inspection and a possible final check by higher-level government organizations.

Recent stats show that the loan balance for the entire sector decreased 36% as of December 31, 2018 when compared with a year ago. Our loan balance however grew 21% year-over-year during the same period. I believe this speaks to management's ability to rapidly react to a deteriorating market, the

strength of our platform, the competitive advantage of our products, and the trust investors have in us.

In addition to keep expanding our core business, to improve our corporate flexibility to weather fluctuations in the market and better serve our customers, our focus now includes building out our microlending business, diversifying our funding sources, and expanding into consulting and referral services to financial institutions. We believe these new businesses are highly complementary to our existing core P2P and will become our additional growth drivers going forward.

Recently, we signed agreements with Bohai International Trust and Kunming Aotou during the quarter. By working together with each institution, we will be able to realize major strategic business synergies by leveraging our combined credit assessment capabilities to target our core demographic of borrowers. Bohai International Trust and Kunming Aotou will extend loans in an aggregate principal amount of RMB300 million and RMB30 million, respectively.

We acquired a 5.88% equity stake in Phoenix Intelligent Credit, a wholly owned subsidiary of Phoenix Financial Group Ltd., for a consideration of RMB200 million. This partnership will leverage our strong borrower acquisition and loan development capabilities to generate additional revenue by referring borrowers to Phoenix Intelligent Credit's P2P platform. We expect total loan volumes for borrowers referred by us over the three-year partnership to be about RMB10 billion.

In order to provide investors with enhanced protection and strengthen their confidence in our platform, we began offering insurance coverage through Shanxi Zhengxuan which became our insurance provider on December 1. Shanxi Zhengxuan will also help us strengthen deterrence against fraud and defaults on our platform by submitting default information to the Credit Reference Center of the People's Bank of China, which operates and maintains a database of personal credit reports.

Finally, in recognition of our leading position in the industry, diversified customer base, high-quality data, transparent operations, and regulatory compliance, we were admitted as a member of Baihang Credit. We will greatly enhance our credit services and strengthen compliance with the start of regular transfers of credit data to Baihang Credit. Baihang Credit will issue individual credit scores by aggregating, integrating and processing the data collected from many partner institutions. This will allow us to more accurately assess a borrower's creditworthiness and potentially reduce the cost of risk management.

As part of our efforts to develop more growth opportunities vertically across the industry, we've begun building a new online consumer loan service which facilitates smaller size and shorter duration loans compared to our traditional loan services. In the future, these types of loans will be designed to be e-commerce featured to help users finance online purchases.

Finally, we announced a \$25 million share repurchase program as part of our commitment to maximize shareholder value. Because of the timing of the announcement and trading window limits, we were not able to make any purchases during the quarter. We will begin purchasing shares once the trading window is open and believe the share repurchase program demonstrates our confidence and optimism in the long-term future of the P2P lending industry in China.

We remain confident in our capabilities and the future business prospects of the industry. Transaction volumes for the top 30 P2P platforms in December accounted for 76% of total volume, which came in at RMB106.0 billion, indicating the advantage the consolidators within the industry enjoy. We believe we are ideally positioned to benefit from the industry's consolidation with our strong financial resources, experienced management team, and clear strategy.

With that, I will now turn the call over to Johnson who will review the financials.

Johnson, please.

Johnson Zhang - Hexindai Inc. - CFO

Thank you, Mr. Zhou. Hello, everyone. Thank you for joining our earnings conference call today.

I'm pleased with our performance in this turbulent market environment where we were able to generate net revenue of US\$1.9 million, exceeding our guidance for the quarter. With the industry continuing to face significant headwinds throughout the quarter, we continued to focus our attention towards maintaining full regulatory compliance and improving operational efficiency. We diversified and expanded our funding sources during the quarter by partnering with Kunming Aotou and Bohai International Trust which will leverage our advanced technology and extensive experience in operating consumer lending business. We are also cooperating with Phoenix Intelligent Credit to assist them in acquiring qualified borrowers and facilitate loans. As our initiatives to improve operational efficiency take hold, operating expenses decreased by 38% or US\$8.0 million sequentially while our net loss narrowed by 45% or US\$7.8 million compared with last quarter.

Total volume of loans facilitated were impacted by investors lack of confidence in the industry following a large spike in the number of problematic platforms in China that collapsed. As a result, loans facilitated decreased by 92% year-over-year to RMB0.2 billion, or US\$29.1 million. Borrower demand on our platform remains high though. Once the market evens out and investor confidence in our platform returns, we will be ready to service them and benefit from the enormous growth potential across the retail financial services sector. As we further diversify our funding sources towards institutions, we expect to see a recovery which I believe will validate our business model and reflects our solid financials and healthy profitability.

Net revenue was US\$1.9 million, a decrease of 95.6% from the same period last year. The decrease was primarily due to the significant decrease in the volume of credit loans facilitated through our marketplace, which decreased from US\$388.7 million or RMB2.6 billion in the third quarter of fiscal year 2018 to US\$29.1 million or RMB0.2 billion in the same quarter of fiscal year 2019, and the decrease of gross billing ratio for credit loan from 12.1% in the third quarter of fiscal year 2018 to 9.1% in this quarter.

Operating expenses were US\$13.1 million, an increase of 11.7% from the third quarter of fiscal year 2018. The increase was driven primarily by an increase in sales and marketing expenses, and general and administrative expenses. Operating expenses decreased by 38% when compared with last quarter.

Sales and marketing expenses were US\$7.2 million, an increase of 30.8% from third quarter of fiscal year 2018. The increase was primarily due to an increase in advertising expenses associated with acquiring more customers.

Service and development expenses were US\$2.2 million, a decrease of 29.9% from same period of fiscal year 2018. The decrease was primarily due to the decrease of employee expenses.

General and administrative expenses were US\$3.2 million, an increase of 42.8% from same period of fiscal year 2018. The increase was due primarily to a loan provision made by our microlending business.

Share-based compensation during the third quarter of fiscal year 2019 was US\$0.4 million, a decrease from US\$0.7 million during the same period of last fiscal year. The decrease was attributable to awards granted under the 2016 Equity Incentive Plan since November 3, 2017 on which date the Company completed its IPO.

Net loss was US\$9.6 million, compared to a net income of US\$26.9 million during the third quarter of fiscal year 2018.

Net loss attributable to the Company's shareholders was US\$9.6 million during the third quarter of fiscal year 2019, compared to net income attributable to the Company's shareholders of US\$26.9 million in the same period of fiscal year 2018. Accordingly, basic loss per common share in the third quarter of fiscal year 2019 was US\$0.20, compared to basic EPS of US\$0.58 in the same period of fiscal year 2018. Diluted loss per common share in the third quarter of fiscal year 2019 was US\$0.20, compared to diluted EPS of US\$0.52 in the same period of fiscal year 2018.

Adjusted net loss attributable to the Company's shareholders, which excludes share-based compensation expenses was US\$9.2 million compared to an adjusted net income of US\$27.6 million in the same period of last fiscal year.

Adjusted EBIT, which excludes interest income, income tax and share-based compensation was a loss of US\$10.0 million compared to US\$32.5 million in third quarter of fiscal year 2018.

We maintained a strong cash position. As of December 31, 2018, our cash position stood at US\$47.4 million. During the nine months ended December 31, 2018, net cash used in operating activities was US\$0.5 million, net cash used in investing activities was US\$60.4 million and net cash used in financing activities was US\$18.9 million.

We believe that the continued expansion of our funding sources will develop new growth drivers for us and improve our overall operating model. We have the capacity and capability to establish a growing stream of steady recurring revenue and profits that will help reduce the natural volatility we may see from time to time in the lending business.

Turning to revenue guidance, for the third quarter of fiscal year 2019, we expect loan volumes to be in the range of US\$60 million to US\$64 million, and total net revenues to be in the range of US\$9 million to US\$10 million.

For full fiscal year 2019, we expect loan volumes to be in the range of US\$564 million to US\$568 million, and total net revenues to be in the range of US\$66 million to US\$67 million.

This concludes our prepared remarks. I'd now like to turn the call back over to the operator to begin the Q&A session.

Questions and Answers

Operator

(Operator Instructions). We have the first question from the line of Josh Vogel from Sidoti and Company.

Joshua David Vogel - Sidoti & Company, LLC - Analyst

I have 3 questions, if I may. We have seen you take some good steps to diversify your platform, whether it's with credit sharing, the online loan service, loan referrals. I'm curious whether there are other products or services that you plan to add to the mix. And, if so, do you have a timeline around that?

Johnson Zhang - Hexindai Inc. - CFO

We are still focusing on our medium-sized consumer loans and will extend our product lines, we will extend our loan size to the smaller-sized and shorter-duration loans compared to our traditional loan services.

Joshua David Vogel - Sidoti & Company, LLC - Analyst

Okay, thank you. You mentioned in your prepared remarks that in step 3 of the regulatory process, there may be additional final checks by higher government regulators. Is that -- do you think that is definitely going to materialize? And maybe if you could just give some commentary of what you believe the timing around the completion of step 3 will be.

Johnson Zhang - Hexindai Inc. - CFO

There is no official announcement by when will be that third step. But according to the expectation by the consulting firm, most of the analysts believe that the third step will be occurred on March. That means the next month there would be the third step.

Joshua David Vogel - Sidoti & Company, LLC - Analyst

Okay, thank you. And then a question on the microlending business. I believe you're fully invested there now. Are there any plans to increase the amount that you can lend with regard to the microlending business?

Johnson Zhang - Hexindai Inc. - CFO

No. We will keep our loan balance for the microlending business on the cap of RMB500 million.

Joshua David Vogel - Sidoti & Company, LLC - Analyst

Okay, thank you. And if I could just sneak one more in. I'm sorry. Do you know when the trading window opens with regard to potentially making share repurchases?

Johnson Zhang - Hexindai Inc. - CFO

I mean this would be, after this conference call, 2 trading days according to the regulation.

Operator

We have the next question from the line of Kaplan Leng from Essence Securities.

Kaplan Leng - Essence Security

Thank for taking my questions and I have 2 questions. The first question is could management provide more color on the outlook for 2019 in terms of loan volume growth and borrower and lender growth?

Johnson Zhang - Hexindai Inc. - CFO

Hello, Kaplan. I think you mean outlook for the 2019 means our next fiscal year. We will provide the outlook or guidance at the end of our -- this fiscal year end. Our fiscal year end is March 31st, and I think we will provide you the guidance for the next full fiscal year in our next conference call.

Kaplan Leng - Essence Security

Oh, yes. And my second question is; could you share with us your mergers and acquisitions strategy? And what specific areas are your strategic investment focus in the near future?

Johnson Zhang - Hexindai Inc. - CFO

We will continue seeking the investment opportunity in the online lending business. For example, we have already invested in this year in Indonesian online lending platform. And we also have announced that we invested in Phoenix Intelligent firm, minority shareholder. We are also seeking out M&A opportunities in emerging markets such as Southeast Asia where we see similar market environments and user demographics. Our acquisitions of a 20% equity stake in Indonesian online lending platform Musketeer late last year was our first step in this regard. We are still in early stage of assessing overseas opportunities and we will continue to look for other opportunities.

Operator

(Operator Instructions). We have the next question from the line Josh Vogel from Sidoti and Company.

Joshua David Vogel - Sidoti & Company, LLC - Analyst

One more question if I may. The number of borrowers on your platform are understandably down, some of this a result of you implementing stricter credit scoring standards. Can we assume that this will be the new norm, the new normal for you and the industry? Or once the regulatory period is in the past and only the compliant platforms remain like yours, you may start to loosen those scoring standards?

Johnson Zhang - Hexindai Inc. - CFO

I think the decrease of borrower is temporary. On our platform, the demand from the borrower side is still strong. And the decrease of the borrower number is the most because of we have decreased our pass-through rate for implementing the more strictly risk control standard on the turbulent market

environment. And the second reason is investor on our platform have preferred to transfer their existing loans other than facilitated new loans. But we believe that after this temporary environment, our borrower number will recover as well as our loan volume will be increased in the future.

Operator

As there are no further questions, I would like to hand the conference back to our presenters for today.

Xinming Zhou - Hexindai Inc. - CEO

Okay. Thank you again for joining us this evening. We believe for the P2P industry, borrower demand is the key growth driver and market indicator. Being short on capital is really a temporarily problem, as the business potential is defined by demand. We remain confident in the solid business foundation we have built and believe we will gradually attract investors to return. We believe investors are not going to wait for the final registration deadline before making their choice of platform and will instead assess a short list of the top platforms with trustworthy brands. We believe that these platforms on the short list will benefit from the industry rectification process.

Again, I am confident in our strategy and our ability to execute and look forward to updating you next quarter on the progress we have made.

Daisy Wang - Hexindai Inc. - IR Director

Thank you, Mr. Zhou. In closing, on behalf of the entire Hexindai management team, we'd like to thank you for your interest and participation in today's call. If you require any further information or have any interest in visiting us in China, please let us know. Thank you for joining us today. This concludes the call.

Operator

Ladies and gentlemen, that does conclude the conference for today. Thank you for participating. You may all disconnect now.