

LexinFintech (LX US)

Rising credit cost on legacy problem loans

LX's 3Q20 non-GAAP net profit fell 2.2% QoQ/ 38.0% YoY to RMB 443mn, largely in line with our forecast. The earnings decline was mainly due to rising provisions (+25.8% QoQ), as credit quality worsened for part of existing loan book. Management attributed this to lower-quality borrowers acquired in previous quarters, and risks were magnified during the pandemic's aftershock. We expect provision overhang to last into 4Q20, deferring earnings turnaround to FY21.

- Healthy growth in loan volume and customer base.** LX's quarterly loan origination rose 17.5% QoQ to RMB48.3bn. Management kept full-year volume guidance of RMB 170-180bn unchanged, meaning potentially further pick-up in 4Q20. Thanks to the Company's new consumption strategy, user base continued robust expansion, with new registered users/ approved users/ active borrowers +10.7mn/2.5mn/1.7mn in 3Q20.
- Better quality for new loans, but legacy issue lingers.** LX's overall asset quality has been improving, with falling M3+ delinquency rate (-39bp QoQ to 2.6%) and stable vintage loss expectation (4.5%). However, the Company charged higher credit cost (+108bp QoQ to 7.4%) in 3Q20. Management acknowledged that provision rise was mainly for existing loan book, especially loans extended to borrowers acquired through certain online platforms (e.g. TikTok) in 2H19. LX has tightened standards for new borrowers and diversified acquisition channels with the help of its flagship products – Le Card and Lehua Card.
- Optimized revenue mix despite lower take rate.** LX's proportion of revenue from platform-based service (capital light/ profit-sharing loan facilitation) was lifted to 36.7% in 3Q20, from 31.0% in 2Q20. Loan originated under this model reached 50% of total loan volume in Oct. The shift in revenue structure to pure technology-enabled service may squeeze take rate, but will effectively transfer risk-taking to financial institutions, thus reducing LX's susceptibility to credit cycles and offering greater growth potential.
- Maintain BUY and trim TP to US\$10.3.** We adjust down FY21-22 earnings forecast by 6-8%, to reflect lower take rate assumption on higher revenue contribution from platform-based service. Our revised TP of US\$10.3 is derived from 1.6x target P/B and FY21E BVPADS of RMB 42.5.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	7,597	10,604	11,912	14,649	17,383
Net income (RMB mn)	1,977	2,295	476	2,036	2,504
EPADS (RMB)	10.9	12.3	2.4	9.9	12.2
YoY growth	2854%	12.7%	-80.6%	315.7%	23.0%
Consensus EPADS (RMB)	NA	NA	4.7	13.6	15.1
P/E (x)	4.5	4.0	20.7	5.0	4.1
P/B (x)	2.11	1.35	1.65	1.16	0.85
Dividend yield	0.0%	0.0%	0.0%	0.0%	0.0%
ROE	68.1%	42.9%	8.0%	31.3%	27.8%

Source: Company data, Bloomberg, CMBIS estimates

BUY (Maintain)

Target Price US\$ 10.30
(Previous TP) US\$ 11.80
Up/Downside +41.7%
Current Price US\$ 7.27

Internet Finance Sector

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Stock Data

Mkt Cap (US\$ mn)	1,315
Avg 3 mths t/o (US\$ mn)	11.7
52w High/Low (US\$)	16.93/6.04
Total Issued ADS (mn)	179.7

Source: Bloomberg

Shareholding Structure

LexinFintech Management	27.9%
K2 Partners	11.9%

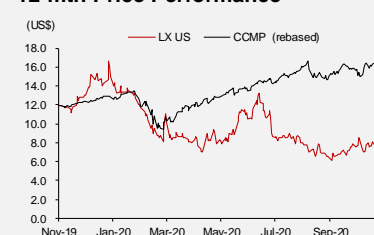
Source: Company data

Share Performance

	Absolute	Relative
1-mth	-7.0%	-10.8%
3-mth	-14.6%	-19.2%
6-mth	-7.5%	-28.3%
12-mth	-36.9%	-55.3%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: PwC

Related Reports

- Strong loan growth offset by lower take rate – 19 Aug 2020
- Internet Finance Sector – Quality player to outstand from industry recovery – 5 Aug 2020

Figure 1: LX's 3Q20 results summary

(RMB mn)	3Q19	4Q19	1Q20	2Q20	3Q20	QoQ	YoY
Operational indicators							
New registered users (mn)	12.4	10.7	10.9	11.1	10.7	-3.6%	-13.7%
New approved users (mn)	3.2	2.7	1.3	2.0	2.5	25.0%	-21.9%
New borrowers (mn)	2.5	2.1	1.0	1.4	1.7	21.4%	-32.0%
Loan origination	37,000	42,800	34,100	41,100	48,300	17.5%	30.5%
Loan balance	51,500	60,567	58,500	61,900	67,400	8.9%	30.9%
P&L							
Loan facilitation service fee	1,887	1,746	1,050	1,350	1,672	23.8%	-11.4%
Interest income	264	259	246	332	369	11.2%	39.5%
Guarantee income	-	-	677	706	598	-15.4%	NA
Other revenue	57	52	47	50	40	-20.8%	-30.5%
Total revenue	2,209	2,056	2,020	2,438	2,678	9.8%	21.3%
Origination and service expense	(177)	(210)	(313)	(356)	(362)	1.5%	104.4%
Sales and marketing expense	(508)	(520)	(244)	(327)	(360)	9.9%	-29.2%
General and admin expense	(111)	(120)	(110)	(114)	(103)	-9.9%	-7.7%
Provisions	(213)	(240)	(1,397)	(951)	(1,196)	25.8%	460.1%
Other expenses	(239)	(230)	(298)	(298)	(261)	-12.4%	9.3%
Total operating expenses	(1,248)	(1,320)	(2,332)	(2,046)	(2,281)	11.5%	82.7%
Other gain (loss)	(112)	(123)	(491)	104	(8)	-107.8%	-92.8%
Income tax	(124)	(96)	125	(77)	(45)	-41.7%	-63.9%
Net profit	724	518	(678)	419	345	-17.7%	-52.4%
Net profit (Non-GAAP)	714	571	(624)	453	443	-2.2%	-38.0%
Key ratios							
Net revenue take rate (% of avg loans)	16.3%	12.0%	3.2%	8.8%	8.3%	-0.5ppt	-8.0ppt
Net yield (% of avg loans)	6.3%	3.7%	-4.6%	2.8%	2.1%	-0.7ppt	-4.2ppt
Leverage (loan/equity)	8.6x	9.2x	14.4x	13.7x	13.7x	0.0x	5.1x
ROE	51.4%	32.8%	-50.9%	39.0%	29.2%	-10ppt	-22ppt
M3+ delinquency rate	1.40%	1.56%	2.57%	2.99%	2.60%	-39bp	120bp

Source: Company data, CMBIS

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Loan facilitation fee	2,076	5,628	5,783	7,702	9,292
Interest income	2,743	1,147	1,309	1,475	1,470
Guarantee income	-	-	2,578	2,558	2,833
Others	2,778	3,829	2,241	2,914	3,788
Total revenue	7,597	10,604	11,912	14,649	17,383
Origination expense	(324)	(642)	(1,394)	(1,580)	(1,896)
Funding costs	(898)	(509)	(593)	(553)	(551)
Marketing expense	(590)	(1,539)	(1,306)	(1,550)	(1,705)
General & admin expense	(280)	(412)	(452)	(474)	(498)
Provisions	(922)	(834)	(4,683)	(4,877)	(5,673)
Others	(2,761)	(4,040)	(2,553)	(3,265)	(4,159)
Total expenses	(5,775)	(7,976)	(10,980)	(12,299)	(14,483)
Operating profit	1,822	2,627	932	2,350	2,900
Other gain (loss)	288	79	(391)	46	46
Pre-tax profit	2,110	2,707	541	2,396	2,946
Income tax	(132)	(412)	(65)	(359)	(442)
Net income	1,977	2,295	476	2,036	2,504

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Cash and equivalent	1,148	2,085	1,520	3,282	5,230
Net loans	6,424	4,411	5,619	5,713	5,581
Receivables	1,832	4,974	5,617	6,805	8,260
Others	3,066	7,765	9,888	10,055	10,705
Total assets	12,471	19,236	22,645	25,855	29,777
Funding	4,804	6,252	7,924	8,057	7,871
Guarantee liabilities	456	1,726	3,729	4,368	5,316
Other liabilities	3,104	4,658	5,622	5,792	6,192
Total liabilities	8,364	12,637	17,275	18,217	19,379
Additional paid-in capital	2,329	2,520	2,736	2,968	3,223
Retained earnings	1,592	3,734	2,292	4,328	6,832
Others	186	345	342	342	342
Total equity	4,107	6,600	5,370	7,638	10,398

Source: Company data, CMBIS estimates

Key operating indicators

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Loans (RMB mn)					
Origination	66,100	125,900	175,288	225,705	270,846
Outstanding balance	32,397	60,567	72,691	87,084	104,497
Growth, YoY					
Loan origination	38.6%	90.5%	39.2%	28.8%	20.0%
Loan balance	68.1%	87.0%	20.0%	19.8%	20.0%
Revenue	36.1%	39.6%	12.3%	23.0%	18.7%
Operating expenses	13.1%	38.1%	37.7%	12.0%	17.7%
Net income	7507%	16.0%	-79.3%	327.9%	23.0%
Total assets	-15.3%	54.3%	17.7%	14.2%	15.2%
Total liabilities	-35.8%	51.1%	36.7%	5.5%	6.4%
Total equity	141.4%	60.7%	-18.6%	42.2%	36.1%
Margin					
PPoP margin	36.1%	32.6%	47.1%	49.3%	49.3%
Operating margin	24.0%	24.8%	7.8%	16.0%	16.7%
Net profit margin	26.0%	21.6%	4.0%	13.9%	14.4%

Profitability

Revenue / avg loans	29.4%	22.8%	17.9%	18.3%	18.1%
Funding cost	9.0%	8.0%	7.7%	7.4%	7.4%
Origination exp / avg loans	1.3%	1.4%	2.1%	2.0%	2.0%
Marketing exp / avg loans	2.3%	3.3%	2.0%	1.9%	1.8%
G&A exp / avg loans	1.1%	0.9%	0.7%	0.6%	0.5%
Net income / avg loans	7.7%	4.9%	0.7%	2.5%	2.6%
Loans / equity	7.9	9.2	13.5	11.4	10.1
Assets / equity	3.0	2.9	4.2	3.4	2.9
ROA	14.5%	14.5%	2.3%	8.4%	9.0%
ROE	68.1%	42.9%	8.0%	31.3%	27.8%

Per ADS data (RMB)

EPADS	10.9	12.3	2.4	9.9	12.2
BVPADS	23.4	36.7	29.9	42.5	57.9
DPADS	-	-	-	-	-

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