Qudian Inc.

Third Quarter 2017 Earnings Conference Call Transcript

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Executives

Min Luo, Founder, Chairman, Chief Executive Officer
Carl Yeung, Chief Financial Officer
Sissi Zhu, Director of Capital Markets

Analysts

Charles Zhou, Credit Suisse
Richard Xu, Morgan Stanley
Victor Wang, CICC
May Yan, UBS
John Davis, Stifel Nicolaus
Mayank Tandon / Jinjin Qian, Needham & Company
Binnie Wong, Merrill Lynch
Linda Sun-Mattison, Bernstein
Alex Zhou, UBS

Presentation

Operator: Hello, ladies and gentlemen. Thank you for standing by for Qudian's third quarter 2017 earnings conference call. At this time, all participants are in listen-only mode. (Operator Instructions). After management's prepared remarks, there will be a question-and-answer session. Today's conference call is being recorded.

I would now like to turn the conference over to your host, Ms. Sissi Zhu, Director of Capital Markets for the Company. Sissi, please go ahead.

Sissi Zhu: Hello, everyone, and welcome to the third quarter 2017 earnings conference call for Qudian Inc. The Company's results were issued via newswire services earlier today and are posted online. You can download the earnings press release and sign up for the Company's distribution list by visiting the IR section of our website at ir.qudian.com.

Mr. Min Luo, our Founder, Chairman and Chief Executive Officer, and Mr. Carl Yeung, our Chief Financial Officer, will start the call with their prepared remarks.

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 is included in the Company's prospectus as filed 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.

Please also note that Qudian's earnings press release and this conference call include discussions of unaudited GAAP financial information as well as unaudited non-GAAP financial measures. Qudian's press release contains a reconciliation of the unaudited non-GAAP measures to the unaudited most directly comparable GAAP measures.

Finally, we posted a slide presentation on our IR website providing details on our results in the quarter. We will reference those results in our prepared remarks, but will not refer to specific slides during our discussion.

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

Min Luo: Hello, everyone, and thank you for joining our quarterly earnings conference call today.

Before we start, we want to welcome our new shareholders and thank everyone for their support as we became a publicly listed company on the New York Stock Exchange.

Our successful IPO in October was an important milestone for Qudian, and we are pleased to report strong financial results for the third quarter, our first time reporting as a public company. We believe the key to Qudian's success is its strong technology and highly competitive operational efficiency. We continue to experience strong demand from our customers and see exceptional growth opportunities, reflecting our leading market position in online small consumer credit.

The third quarter results were achieved with a self-enforced, all-in service fee to users that translates to 36% APR or less across all our products.

We also continued to practice a disciplined and effective, yet user-friendly collection effort. We believe this approach is in line with our core values to set the best practices in the developing consumption credit market. And our goal is to help users access credit responsibly, while remaining competitive and delivering sustainable growth for our investors.

Although we spoke to many of you a few weeks ago during our IPO roadshow, I want to reiterate a few key points. First, we see a very large opportunity for consumer credit. Although we are already growing very fast, with 7.5 million active borrowers in the third quarter, we have significant room to further penetrate and make our consumption credit accessible to the hundreds of millions of young consumers in China.

We are also expanding our product offering to include more value-enhancing consumption installment scenarios, focusing on our core user base that has a monthly income range of RMB 3,000 to RMB 5,000. This includes further expanding our established consumption installment service while at the same time testing the market with new installment scenarios, such as affordable budget auto installments.

Second, we continue to strike a healthy balance between growing revenues and managing credit risk.

Finally, we have established best practices in the industry and standard operating procedures with our automated systems and staffed call center for dealing with delinquent loans.

We follow specific steps with regard to collecting delinquent payments, all of which are described in our prospectus filed with the SEC. As of September 30, 2017, we had approximately 300 employees primarily responsible for collections and they are mainly based in our call center in Jiangxi Province.

In short, we are excited about our future and will continue to explore new growth opportunities, develop new data technologies and offer enhanced services for our users, while operating within the developing regulatory framework.

With that, I will now turn the call over to our CFO, Carl Yeung, who will discuss our key operating metrics and financial results.

Carl Yeung: Thank you, Min, and hello, everyone. First, I'd like to touch base on a couple highlights for the quarter. We delivered excellent results in the quarter with year-over-year revenue growth of 308% and net income growth of 322% as a result of our strong operational efficiency.

With total registered users reaching 56.6 million and approved users of 23.6 million, the significant growth in active borrowers to 7.5 million led to a strong year-over-year transactional growth.

Most notably, sales commissions contributed 20% of total revenues in the quarter, up from 5% last year, resulting in higher profitability in the quarter.

The volume of data we collect and process continues to grow in scale and velocity, with over 26 million credit drawdowns facilitated in the quarter, which provides us a significant competitive advantage in the risk models we build to analyze the Chinese consumption credit users.

In addition, we continue to set industry-leading responsibility practices in areas that protect user data and help our users borrow responsibly, while expanding the market of providing consumption credit to the underserved.

Finally, as Min mentioned, we are proud to reiterate that since April of this year, the all-in annualized interest rate fees charged for all our products have been capped at 36%.

Now, I'd like to walk you through our detailed financial results in the third quarter of 2017. Total revenue for the quarter increased by 308% to RMB1.45 billion from RMB355.6 million in the prior year period, primarily due to the increase in financing income as a result of the substantial increase in the number of transactions we processed in the quarter.

Financing income totaled RMB1.05 billion for the quarter, increasing 214% from RMB335.7 million for the third quarter of 2016.

Sales commission fees increased to RMB294.8 million for the quarter. That's nearly 15x the same period a year ago. The significant year-over-year growth in sales commissions was driven by an increase in merchandise credit utilized by borrowers to purchase merchandise on our marketplace, and an increase in the fee rate on sales commissions we charge on merchants. We believe that one of the factors contributing to the strong year-over-year growth was the expansion of products we offered on the marketplace.

Total operating cost and expenses increased by 358.7% to RMB757.5 million for the quarter from RMB165.1 million for the third quarter of 2016.

Cost of revenues increased by 278.5% to RMB258.9 million for the quarter from RMB68.4 million for the third quarter of 2016. This year-over-year increase was primarily the result of higher interest expenses on borrowings because we had a larger proportion of funding coming from institutional funding partners as well as higher payment processing and settlement fees.

Sales and marketing expenses increased by 384.7% to RMB187.9 million for the quarter from RMB38.8 million for the third quarter of 2016. The increase was primarily a result of higher borrower engagement fees in the third quarter of 2017 compared with the same period last year.

General and administrative expenses increased by 336.9% to RMB51.1 million for the quarter from RMB11.7 million for the third quarter of 2016. The increase was primarily attributable to higher professional service fee expenses, higher share-based compensation expenses for general and administrative personnel, and higher salaries and benefits paid to such staff.

Research and development expenses increased by 342.6% to RMB52.7 million for the quarter from RMB11.9 million for the third quarter of 2016. The increase was primarily due to higher salaries and benefits and higher share-based compensation expenses for such staff. We have increased our spending on R&D with the goal of enhancing our data analytics and risk management capabilities.

Income from operations for the quarter was RMB695.8 million, representing a 259.2% increase from RMB193.7 million for the same period last year.

Income tax expenses increased by 19% to RMB45.9 million in the quarter from RMB38.6 million in the prior year period, primarily due to the increase in taxable income.

Now, because of the forgoing, net income totaled RMB650.7 million for the quarter, up 321.8% from RMB154.3 million for the third quarter of 2016. Net income attributable to the Company's shareholders per diluted share was RMB2.20, compared with RMB0.51 in the prior year period.

Adjusted net income attributable to the Company's shareholders, which excludes share-based compensation expenses, increased by 329.9% to RMB663.3 million from RMB154.3 million in the prior year period.

Adjusted net income attributable to the Company's shareholders per diluted share increased to RMB2.24 from RMB0.51 in the same period last year.

As of September 30, 2017, the Company had cash and cash equivalents of RMB1.48 billion, compared to RMB785.8 million as of December 31, 2016.

The Company also had restricted cash of RMB2.04 billion, compared with nil as of December 31, 2016. This restricted cash is mainly representing the cash in consolidated trusts that can only be used to fund credit drawdowns or settle these trust obligations. Such restricted cash is not available to fund the general liquidity needs of the Company.

As of September 30, 2017, the Company has established more than 30 trusts in collaboration with trust companies.

As of September 30, 2017, the Company had short-term amounts due from related parties of RMB599.7 million, compared with short-term amounts due from related parties of RMB585.9 million as of December 31, 2016. Such amounts include RMB596.7 million and RMB404.6 million deposited in our Alipay account as of September 30, 2017 and December 31, 2016, respectively. Such amount is unrestricted as to withdrawal and use, and is readily available to the Company on demand.

As of September 30, 2017, the total balance of outstanding principal for on-balance sheet transactions for which any installment payment was more than 30 calendar days past due was RMB194.6 million. The balance of allowance for principal and financing service fee receivables at the end of the period was RMB247.3 million, indicating an M1+ Delinquency Coverage Ratio of 1.3x.

Net cash provided by operating activities for the third quarter of 2017 was RMB889.4 million.

Now this concludes our prepared remarks. We will now open the call to questions. Operator, please kindly go ahead.

Questions and Answers

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

For the benefit of all participants on today's call, if you wish to ask your question to management in Chinese, please immediately repeat your question in English.

Charles Zhou, Credit Suisse

Charles Zhou: Hello everyone and hello, Carl. Congratulations on your excellent results. I think you beat the market's expectation by 15% to 16%, so congratulations. So ask two questions -- the first one is we know there's a lot of the regulations talking about in your local news. So you can share with us about the regulatory direction, and also how will the Company cope with the potential changes? Meanwhile, I also want to just confirm again that you have fully complied with the regulations now, that your APR interest rate is capped at 36% and also violent collection as well.

Now the second question is also what is the relationship with Alipay? So do you see any changes with so much media coverage on the Company and also the sector? Thank you.

Carl Yeung: Thank you, Charles, and we really appreciate the comment. We have, in fact, achieved a new milestone with the third quarter results and I'm glad to see the market is reacting quite positively to that.

Regarding your question, first of all, on regulation and directions, the regulatory environment in China for emerging consumption credit is developing and emerging. So it is difficult to specifically say what it is, but as far as we are concerned, we practice the industry's best practices, including a strict limit on the all-in interest rates we charge to our users.

From April on -- now this is the third quarter -- the full quarter, all products have been confirmed to be within the 36% APR rule and it's enforced internally by us, and we believe this is what very few companies are practicing in the entire industry.

Secondly, we have no violent collection efforts. We practice disciplined, yet user-friend collection. The most we will do is currently, we make phone calls to our users to remind them to repay. We believe these best practices are in line with potential regulatory requirements, and we will be in the best shape if such regulations become in force.

The second question relating to Alipay, we continue to have a strategic relationship and a healthy relationship with Alipay. In this single quarter, we have provided a new milestone in terms of cashless transactions, all facilitated on the Alipay platform, as well as feeding back a new record of data back to the Alipay ecosystem. In addition, the campus business continues to grow and thrive as a strategic partnership between Alipay and us. We believe that nothing has changed between us and Alipay and we will maintain the healthy relationship. But just as a reminder to all listeners on the call, we are one of the partners of Alipay, a strategic partner, but Alipay is a fair platform and we transact on an arm's-length basis.

Richard Xu, Morgan Stanley

Richard Xu: Thank you, Min and Carl, for the opportunity for questions. A couple of questions on the expense side -- I just noticed basically the provision has increased quite notably during the quarter. Could you talk a little bit why that's the case? Basically any changes in risk profile or risk preference during the quarter?

Secondly, we've also noticed that sales and marketing expenses also almost doubled during the quarter. Just wondering whether there's any marketing initiative, whether that's also related to the notable increase in the sales commission related fees as well during the quarter? Thank you very much.

Carl Yeung: Thank you, Richard; thank you for the questions. First of all, related to the provisions we made in the quarter, our company continues to practice a balance of risk versus return that can allow us to have sustainable, profitable growth. In the quarter, we actually -- you'll see two things. Number one, the increase in the merchandise component of our business. Because the merchandise transactions have a longer duration on average, they will have a slightly higher delinquency performance.

But by nature, the risk is the same; it's the same homogeneous diversified user group that we're targeting. So if just the duration is longer, it will lead to a slightly higher delinquency but the merchandise profitability is significantly higher, so we can achieve a new milestone in terms of profits this quarter.

And in general, the Company believes that we will be sitting in a faster growth pace, better user experience as well as profitability as we increase that M1+ delinquency to approximately 1 %. We believe that currently, at 0.5% or less, it's probably too conservative within the known risk that we're dealing with. So we will be targeting a medium term of 1% as a delinquency on a proactive basis.

Secondly, on the sales and marketing side, as we all know, as disclosed in the prospectus, since April of 2017, we have been added to the front landing spot in the Alipay application. With that, it comes with a sales and marketing cost we have to pay to that platform. That payment was on a cost-per-click basis in the second and third quarter. Therefore, we were, in fact, paying for all traffic visiting our store, visiting our assets regardless if it results in a transaction or not. Therefore, you see the sales and marketing increase in both the second quarter and third quarter.

We expect that to be more reasonable going into the fourth period since we have changed the transaction basis from a cost-per-click to another market rate, which is a cost per sale basis since October 1, and we believe that sales and marketing as a percentage of our transaction will actually be lower going into the fourth quarter.

Victor Wang, CICC

Victor Wang: (Spoken in Chinese and repeated in English). My question is regarding the plans how to help utilize the proceeds coming from the recent IPO, given the size is bigger than USD 1 billion. And also if you look at the second quarter 2017, the delinquency rate, this seems that in the second and third months, the delinquency rate trend is picking up quite substantially. Is that related to the fast growth of merchandised product?

Carl Yeung: Thank you, Victor, for the questions. Relating to the use of proceeds, we have disclosed in the prospectus exactly what our use of proceeds are and we'll stick with that for the foreseeable period until we make another disclosure on such. Basically, we don’t plan to use that use of proceeds to fund our current credit drawdowns.

Our Company's strategy is to continue to be operating a light business model for our institutional funding partners to fund the credit transactions that we facilitate. So the use of proceeds is largely targeted for general corporate purposes and our potential sales and marketing efforts to enhance our brand, as well as potential strategic investments. As of this moment, we don’t have any targets in mind.

Regarding delinquency rate, yes, they have increased in both second and third quarter. You can see the delinquency by vintage line has been a bit more trending up, and that's actually a direct result of our proactive increase to take on more known risk, so we can approve more users. You'll see in the third quarter, we have approved a record number of approval rate, in terms of approval rate. At the same time, we have increased our merchandise sales significantly and that's driving that delinquency rate up.

Now, as stated just now in the previous question from Richard, our medium-term delinquency rate by vintage is approximately 1%, and 1% is still industry-leading in terms of how low it is. Thank you.

May Yan, UBS

May Yan: (Spoken in Chinese and repeated in English). My question -- okay, two questions; one is on collection. We saw in the announcement that about -- there are about 300 call center people that focus on collection. Are these people part of the 1,000 sort of employees that have been disclosed before, and they're full-time collection people, or they're doing these part-time? And secondly, and also what's the recovery rate for the collection recently?

And then secondly, my other question is on the provisioning that as mentioned before, longer term is going to target to increase to about 1%, and then I saw the coverage right now is about 1.3x. So as the delinquency is going up over time, is that the target that you -- the Company tries to maintain, or is it going to be going down to 1x or maybe 2x? Where will be the target level? Thank you.

Carl Yeung: Thank you, May, appreciate the questions. The first question relating to the 300 staff that we mentioned in the earnings call script, our earnings call dialogue, is all these 300 staff is full-time employees of the Company and is within the disclosed number of staff in the prospectus.

So these staff are sitting in the call center in Jiangxi Province collecting by phone, helping users to repay by calling and reminding them there's a payment to be made. So these are our full-time staff. We currently do not outsource any collection efforts to control that good user experience, and to make sure that we stay in regulatory compliant in terms of collection efforts.

And then number two, regarding the provision coverage ratio, we mentioned that we have a target of about 1% in terms of M1+ delinquency, and the current third quarter provision coverage ratio by the amount of balance that has been provided for under the P&L is 1.3x of real M1+ and we believe that 1.3x is a good stable number. Over the longer period, we believe 1.1x, just slightly over coverage, is the best way to reflect a true P&L, not being conservative, not being aggressive from an accounting perspective. Thank you very much, May.

John Davis, Stifel

John Davis: Good evening. I just wanted to follow-up on credit as well. Carl, I think we've talked a lot about this 1% delinquency. Can you help us? Is this something that's going to happen kind of the next quarter or two, or is this a year out? I'm just trying to figure out timing-wise as far as how long you think it'll take to get to that 1% level in the M1 delinquencies.

Carl Yeung: Thank you, John, appreciate the question. Yes, one really strong part of our culture is execution and doing things faster than any industry participant, as you can see from our results in the third quarter. We have grown faster than any other company in the sector and our fast execution culture will also reflect in our targets. For example, this 1% delinquency we expect to achieve in the short-term, in the next one or two quarters, right, and a year or two out. So we will deliver on what we say.

John Davis: Okay. That's very helpful. Then I also wanted to touch on the commission rate. I think it came in a little bit higher than what I'd expected and what has been historic. Can you just comment on what's driving that higher and is that sustainable longer-term? Thanks.

Carl Yeung: Thank you. Thank you, John. The commission rates was approximately 16% in the third quarter, so it has been a new high for the amount of commissions we can achieve from our merchandise partners. This is in reflection of several things. Number one, it's the substantial growth in our merchandise platform business which makes it an attractive marketplace to be for our merchandise partners, so they're willing to share more economics to us.

Secondly, the shift of traditional handset focus, higher weight, has been adding -- we have been adding substantially more alternative products beyond handsets, such as light luxury, which has higher sales commission margins. Some items we sell like watches, like luxury handbags, they carry a 40%-plus sales commission margin. Those two combined have been helping us in achieving new sales commission milestones. Thank you, John.

John Davis: Thank you.

Mayank Tandon / Jinjin Qian, Needham & Company

Mayank Tandon: Thanks a lot for taking my questions. This is Jinjin on for Mayank. I just had a question about kind of the funding side of the business. Since your IPO, do you see it help bring more funding partners to the platform? So maybe update us on the net adds. I think previously mentioned you have 21 funding partners, maybe how many do you have now?

And also in terms of percentage funding for on-balance sheet versus off-balance sheet, could you give us an update on that, and maybe remind us in terms of funding costs on-balance sheet versus off-balance sheet. Thank you.

Carl Yeung: Thank you, and really appreciate the questions. As of September 30, we've grown a new milestone also the number of funding partners. So we've grown from 21 partners as of June

30, 2017 to now 26 partners by September 30. We'll continue to grow that beyond September 30 as well.

And the funding mix for a total loan balance in terms of mix as of September 30 is 23% is our own equity; 30% from our trust structures; 19% from asset exchanges; about 10% from others such as asset management company. And we've grown to a record percentage contribution of 17% in terms of off-balance sheet, which is contributed by banks and consumer finance companies.

This is directly in line with what we want to achieve from a strategic perspective, as we disclosed in the prospectus, increasing the institutional funding partners as well as increasing the off-balance sheet, so that we become a pure play data and technology-focused company to help funding partners provide credit to users. So again, we're delivering what we said. Thank you.

Operator: The next question --

Carl Yeung: Oh, sorry, one more to add. I know you asked the question regarding the funding costs. The funding cost has remained pretty much stable from June 30, 2017. Thank you.

Binnie Wong, Merrill Lynch

Binnie Wong: Congratulations, Min and Carl, on a strong quarter of results. My question is coming on the user acquisition strategy. Can you share with us more on the -- in terms of how you -- because you also have an e-commerce platform -- how you see that later on; how much of the traffic you think you can grow organically? And then also maybe from directing traffic now currently from Alibaba, will you consider also working with other platforms?

And then my second question on the breakdown that you just mentioned on the on-balance sheet and off-balance sheet, given the interest rate environment now, how will you see potentially what are some of the strategies we have to manage down the borrowing costs? Thank you.

Carl Yeung: Thank you, Binnie, appreciate the questions. Regarding user acquisition strategy, we believe the Alipay ecosystem remains the most attractive ecosystem to reach this underserved user in China, so we're committed to that ecosystem. But even if you look into that ecosystem --

[Loud noise]

Binnie Wong: I'm sorry.

Carl Yeung: So we have babies joining! [Funny].

Binnie Wong: (Laughter). Yes, probably some new user, a potential new user, right? (Laughter). Sorry, yes, (inaudible). Thank you.

Carl Yeung: Oh, it's always fun to have something. So yes, I'll continue on. So even within the Alipay ecosystem, so Alipay is an open platform and we're one of the participants in that platform. When we look at new borrower engagement, almost 50% comes from word-of-mouth which they search by us so -- through the service window or our own apps. So for the foreseeable future, we don’t see user acquisition strategy to change that much because as Alipay grows and remains open platform, it's still the best place to be.

Secondly, regarding the breakdown on the on and off-balance sheet question -- sorry, I -- [technical difficulty]. And then the breakdown is in the -- by the balance by September 30, off-balance sheet funding is 17%. It's actually a significant increase from 11% by June 30, so again, this Company is executing all we talked about.

And then how do we manage our overall funding cost down is by continuing to generate the most attractive asset class in the entirety of China. Our assets represent diversified, small-ticket size, short duration, low delinquency credit that is inaccessible until we have come to the market. We continue to provide access to this asset class and we, by having that most attractive asset class, are finding partners fight to get a piece of it, and that's how we manage and make sure our funding costs stay low. So thank you, Binnie.

Binnie Wong: Thank you. Just a quick follow-up on the user acquisition side -- if you think about that over -- we'll be getting more new users because we have been saying that, that's more like getting the users that are mostly unserved by the traditional finance channels, say, traditional banks, how do you think about going beyond our core user group; say, going into expanding more into middle class or maybe going into more white-collar beyond just our core young-young generation? How does your Company see that evolve?

Carl Yeung: Thank you, Binnie, for the question. It's a very good question and we have thought about it for a long, long time. Our position and our strategy is to say within the class of users that are making RMB 3,000 to RMB 5,000 a month because that's where our Company can possess the largest competitive advantage in terms of cost, efficiency and serving their consumption credit needs.

Going to the larger ticket size would be very easy for us. In fact, it's very easy for us to make money there, but we believe the larger ticket size is not the market that we can really demonstrate our strong, super-strong, competitive advantage in terms of cost when the ticket size becomes very, very large.

Now, in the small ticket size, we're still just at a drop in the pond in terms of the potential market that we're penetrating. As disclosed in the current quarter, we have 7.5 million active borrowers, but we're looking at a market with approximately 400 million users, so there's a lot of penetration still to go. So we remain focused and a long way to go from here. Thank you.

Binnie Wong: Got it. Thank you.

Linda Sun-Mattison, Bernstein

Linda Sun-Mattison: Carl, I really appreciate your statement just now about staying to your core customer segment and being -- offering us more ticket items as one of the key concerns from the investors I have talked to that the credit costs being low, and it's very dependent on more ticket and short duration. So I'm very pleased to hear the Company stay focused on the core business.

I have a question regarding the regulation risk and I notice, and as you said, the off-balance sheet funding went up from 11% to 17%, and that will help reduce your reliance on your own capital and on-balance sheet loans. That's a good thing, but on the other side, we know the biggest problem with China's banking system and regulator is so-called shadow banking system. With off-balance sheet asset funding, it often comes with the worry that this is a channel (inaudible) that is channeling an asset that has an implicit guarantee, or has all these kind of things.

And so I'm just wondering how you see the off-balance sheet, whether you see a ceiling or cap on off-balance sheet funding? And on the same kind of string, I want to kind of ask your perspective, both Min and Carl's perspective, what is the unknown risk, the regulatory risk? We know the known risks, for example interest rate, collection on the debt. Are there any things that could be the blind spot for the investors? Thank you very much.

Carl Yeung: Thank you very much, Linda. This is a very good question regarding the regulatory risk regarding our funding structure. As you can see, our Company's strategy is to diversify our funding structure so that any single funding channel which may face volatility, we have other channels to cover the short change in that specific -- if there's any volatility in any specific one.

So yes, yes, our off-balance sheet funding has increased from 11% to 17%, but we have also diversified into other funding channels, such as trust structures, asset exchanges, directly with licensed asset management companies, as well as we have a very strong balance sheet of our own cash in the worst-case scenario. So our goal is not to leverage our cash and equity to provide loans, but in the very worst-case scenario, we have, ourselves, two licenses to make Internet micro loans. And we can quickly inject capital to make sure our growth is not affected if any single structure is impeded.

But to get back to the off-balance sheet problem, we actually do not see any potential regulatory hurdle right now, but it's difficult to guarantee. As of right now, we work exclusively with licensed banks and consumer finance companies and they have their own internal regulatory compliance procedures that they have done to ensure these structures are satisfying current regulatory requirements. Now if the regulatory requirements change, I'm sure we can have ways to adapt to these new changes because we are industry-leading players. We intend to keep our licenses and we intend to make sure there's a large opportunity is captured within the framework of our regulators being able to see what's going on.

So I think we're in a very good position there. And our strategy is continue to diversify the number of partners, the type of channels, so we don't see any potential risk there at the moment.

Now, the second question regarding anything that's unknown on the regulatory side, my response is unfortunately, it's unknown to us as well. So I think everything that we know, I think everything the market knows, I think it's quite public and we are already practicing all of our business operations within these regulatory guidelines, including 36% or below interest rate, including very civilized collection efforts, including having an institutionalized funding structure and not taking deposits.

So from a known realm, I think we're in very good shape. For anything unknown, I have to apologize, I can't comment. Thank you.

Linda Sun-Mattison: Yes, so just on the unknown risk because currently, I think your Company and generally the micro-lenders regulated by the central office are kind of consulting by various regulators. I'm wondering whether you see any kind of risk or potentiality of you being regulated by CBRC, almost like a bank?

Carl Yeung: I think it's difficult to provide a comment on that because that is a position by the Chinese regulators, but whatever that regulation is, I think our Company is confident in being able to meet these requirements because we have been operating with a self-enforced rules and guidelines ahead of potential regulations.

Linda Sun-Mattison: Thank you very much, Carl.

Alex Zhou, UBS

Alex Zhou: Hi Carl. I have two questions. The first is regarding user approval rates. We noticed approval rate has gone up quite a lot in the third quarter, up to 55% right now. So we're wondering where the target level is going forward, and also, can you confirm whether Qudian is still only lending to customers with a Sesame score that is over 600?

Also, could you please expand a little bit on the implication for asset quality in the sense that if we're targeting an M1+ delinquency ratio of 1%, does that relate in any way to the approval rate?

The second question is regarding loan volume. We notice in the third quarter, our result actually beats the market consensus by 15% to 20% in terms of loan volume. And we just noticed that Alibaba and Taobao had a very successful double 11 campaign. So can you give us some guidance in terms of loan volume into the fourth quarter? Thanks.

Carl Yeung: Thank you so much, Alex, for the question and thank you again for observing our increasing approval rate. This is in line with our strategy to continue to increase the approval rate as our Company is indeed in the business of inclusive finance. We help people with -- underserved by the traditional credit providers, to give them credit.

We do have a longer term approval rate target of approximately 80%. That will have an impact on increasing our model, our Company's delinquency rate. That's why we have a longer term target of 1% as the delinquency ratio, but what you'll see as we approach 80% approval rate and 1% delinquency ratio, we'll continue to reach new profitability milestones because our driver of profit is coming from merchandise sales. And that's again significantly higher of profitability and margin structure.

So we see that as a healthy way to grow our business, to reach out to more users, have more and more users in our pocket, as well as grow profitability from these users. So that's all in line with our strategy, so 80% is our target.

On loan volume growth, yes, we have grown our business again reaching a new milestone of loan volume in this third quarter. Unfortunately, as a policy of the Company, we do not provide forward-looking guidance specifically to financial metrics. So we want the industry and the investor community to think of this opportunity longer term. We're just at the beginning of the unfolding of the Chinese consumption credit opportunity. We're literally at the very early stages of it. So instead of from quarter-to-quarter, I think we will want investors to think longer term.

But yes, fourth quarter is traditionally a seasonally strong quarter, as you can see from last year. So we expect our first quarter to reach new milestones again. Thank you very much.

So thank you, Operator.

Operator: As there are no further questions, now I'd like to turn the call back over to the Company for closing remarks.

Sissi Zhu: Thank you once again for joining us today. If you have further questions, please feel free to contact Qudian's investor relations through the contact information provided on our website.

End of Transcript.