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loanDepot, Inc. NYSE:LDI

Earnings Call

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Call Participants

EXECUTIVES

David R. Hayes
Chief Financial Officer

Frank D. Martell
CEO, President & Director

Gerhard Erdelji
Senior Vice President of Investor Relations

Jeff Alexander Walsh
President of LDI Mortgage

ANALYSTS

Kyle Joseph
Jefferies LLC, Research Division

Taylor DeBey
Raymond James & Associates, Inc., Research Division

Presentation

Operator

Good afternoon, and welcome to loanDepot's Third Quarter 2023 Earnings Call. [Operator Instructions] I would now like to turn the call over to Gerhard Erdelji, Senior Vice President, Investor Relations. Please go ahead.

Gerhard Erdelji

Senior Vice President of Investor Relations

Good afternoon, everyone, and thank you for joining loanDepot's Third Quarter 2023 Earnings Call. Before we begin, I would like to remind everyone that this conference call may include forward-looking statements regarding the company's operating and financial performance in future periods. All statements other than statements of historical fact are statements that could be deemed forward-looking statements, including, but not limited to, guidance to our pull-through weighted rate lock volume, origination volume, pull-through weighted gain on sale margin and expense trends. These statements are based on the company's current expectations and available information. Actual results for future periods may differ materially from these forward-looking statements due to risks or other factors that are described in the Risk Factors section of our filings with the SEC.

A webcast and a transcript of this call will be posted on the company's Investor Relations website at investor.loandepot.com under the Events & Presentations tab. On today's call, we have loanDepot President and Chief Executive Officer, Frank Martell; and Chief Financial Officer, David Hayes, to provide an overview of our quarter as well as our financial and operational results, outlook and to answer your questions. We are also joined by our Chief Investment Officer, Jeff DerGurahian; and LDI Mortgage President, Jeff Walsh, to help address any questions you might have after our prepared remarks.

And with that, I'll turn things over to Frank to get us started. Frank?

Frank D. Martell

CEO, President & Director

Thank you, Gerhard, and thank you all for joining us today. I look forward to sharing my perspective on market conditions and our results. loanDepot continues to make significant progress against the imperatives we laid out on our Vision 2025 plan back in July of 2022. As you may recall, Vision 2025 focused on 4 main areas: first, transforming our originations business to drive purchase money transactions with an expanded emphasis on purchase-driven lending; second, investing in profitable growth generating initiatives and critical business operating platforms and processes to support operating leverage and best-in-class quality and delivery; third, aggressively rightsizing our cost structure to address current and future projected market conditions; and fourth and finally, optimizing and simplifying our organizational structure.

In the third quarter, our revenues were essentially unchanged from the prior quarter as we modestly increased our market share and improved gain on sale margins. Importantly, we benefited from positive contributions from our servicing platform, builder partnerships and home equity lending. The company's core mortgage origination revenues were down 3% for the quarter, modestly outperforming the overall market trend during the same period. Higher mortgage interest rates during the third quarter contributed to the modest decline in our revenue trend. David will discuss this area and other results of operations in a few minutes.

While in general, housing stock remains a short supply, new home construction has been a bright spot this year. In this regard, we continue to work closely with our builder partners and we believe new home construction will be a critical driver for adding much needed new housing stock in 2024 and beyond.

Another bright spot in recent quarters has been our HELOC product, which continues to serve as a powerful financial tool for our customers. Over the past several quarters, our HELOC revenue has grown

steadily, and this product is becoming a meaningful positive contributor to our financial performance. We expect this positive growth trend to continue as homeowners access record levels of home equity.

As I discussed on past calls, we believe that homeownership is the bedrock of the American dream and plays a vital role in helping to build strong and stable communities. Further deepening our support for diverse and first-time homebuyers is a critical component of Vision 2025. As a purpose-driven lender, our team is passionate about making homeownership accessible and achievable for more families. Along these lines, we recently launched our accessZERO program intended to make homeownership more accessible for aspiring homeowners grappling with a traditional down payment requirement, high interest rates and rising home prices. With affordability concerns eroding consumers' purchasing power, accessZERO offers up to 5% in down payment assistance. As we continue to unlock new ways for our customers to purchase homes in today's challenging environment, accessZERO helps to address a significant barrier, particularly for first-time homebuyers grappling with the obstacle of saving for the higher down payments that come with rising cost of housing.

Through the implementation of Vision 2025, we delivered our third successive quarter of lower operating losses. This important progress has come against the backdrop of continued significant challenges in the mortgage market. The improvements were driven by margin expansion and continued benefits of cost reduction, gains in productivity and increasing operating leverage. We continue to maintain our disciplined approach to expense management as we reset our cost structure to align with the size of the market.

In the third quarter, we lowered total expenses by \$25 million or 8%. Since the launch of Vision 2025 in the second quarter of last year, we have reduced our total quarterly expenses by approximately 45%. It's important to note that in addition to becoming more efficient, we're also making investments in the company to position us for leadership as the market emerges from the current downturn. These investments include our primary point of sale and loan production systems as well as customer contact and management capabilities.

As we look forward to 2024, our current expectation is that the market volumes will remain substantially similar to 2023 levels. We believe that the factors that have impacted the industry in 2023, including lack of housing stock for sale as well as record-low affordability, will be with us during 2024. In this volume-constrained environment, we expect to continue to capitalize on our multichannel go-to-market platform to deliver profitable areas of growth. In addition, we will continue to aggressively drive our productivity plan and become more efficient in our pursuit of reaching profitability. In this regard, we are taking actions over the next several quarters, which target an additional \$120 million of annualized expense reductions including \$100 million of nonvolume-related reductions. David will provide additional details on this plan in a few moments.

I'd like to conclude my prepared remarks today by thanking Team loanDepot and our other key stakeholders for their support. Our markets remain challenging, no doubt, but this is also a very important period of positive change, forward momentum for the company. I believe we are seeing a positive and tangible result from our continued focus on the 4 pillars of our Vision 2025 strategic plan. With over \$700 million of cash on hand, additional cost productivity programs in flight and consistent contributions from each of our business units, we believe that we are increasingly well positioned to navigate through the present market downturn and emerge a stronger and more valuable company.

With that, I'll now turn the call over to David, who will take us through the financial results in more detail.

David R. Hayes
Chief Financial Officer

Thanks, Frank, and good afternoon, everyone. During the third quarter, loan origination volume was \$6.1 billion, a decrease of 3% from the second quarter of 2023. This was within the guidance we issued last quarter of between \$5 billion and \$7 billion. Third quarter volume consisted of \$4.3 billion in purchase loan originations and \$1.8 billion in refinance loan originations primarily cash-out refinances. Our pull-through weighted rate lock volume of \$5.7 billion for the third quarter contributed to the total revenue of \$266 million, which represented a 2% decrease from the second quarter. Rate lock volume came in at the lower end of the guidance we issued last quarter of \$5.5 billion to \$7.5 billion. The decrease in revenue is

primarily a result of lower loan origination income from a decrease in rate lock volume, offset somewhat by a higher gain on sale margins in servicing revenue. Our pull-through weighted gain on sale margin for the third quarter came in at 293 basis points, above our guidance of 245 to 285 basis points.

Our higher gain on sale margin was primarily due to an increase in profit margins on our HELOC product, continued improvement in our repurchase activity and wider profit margins on our production offset by a larger proportional contribution from our joint venture channel. As Frank previously mentioned, one of the primary pillars of Vision 2025 is a focus on optimizing our organizational structure and improving the quality of our production. Thanks to the work of the team, we've substantially enhanced our quality, and as a result, there's been a significant decrease in the amount of loans that we've been asked to repurchase. Through these efforts, we have improved our financial results by reducing provisions for loan losses and increased our gain on sale margin.

Turning now to our servicing portfolio. The unpaid principal balance of our servicing portfolio increased to \$144 billion from \$142 billion quarter-over-quarter. Servicing fee income increased from \$118 million in the second quarter of 2023 to \$119 million in the third quarter of 2023. Similar to the second quarter's activities, during the third quarter, we sold excess agency servicing rights related to unpaid principal balances totaling \$12 billion, resulting in a gain of \$4 million. This transaction allowed us to monetize a portion of the asset while maintaining our direct servicing relationship with those customers.

We hedge our servicing portfolio, so we do not record the full impact of the changes in fair value and the results of our operations. We believe this strategy protects against volatility in our earnings and liquidity. Our strategy for hedging in the servicing portfolio is dynamic, and we adjust our hedge positions in reaction to changing interest rate environments.

We believe our servicing portfolio is well protected against the potential rising defaults. As of September 30, the weighted average FICO was 738, the weighted average coupon was 3.4% and the weighted average LTV at origination was 72%. These characteristics contributed to a low delinquency rate with only 86 basis points of the portfolio more than 60 days past due at any quarter end and should generate reliable ongoing revenue during these uncertain economic times.

Another major component of Vision 2025 is to align our expense base with a shrinking market size and create efficiencies to improve operating leverage and financial performance over time. Our total expenses for the third quarter of 2023 decreased by \$25 million or 8% from the prior quarter. Savings were recognized across almost all of our expense categories.

Our volume-related expenses consisting of commissions and direct origination expenses decreased by \$6 million, reflecting lower origination volumes. Vision 2025 related charges were \$2.5 million, down from \$7 million in the prior quarter, primarily due to a reduction of personnel-related charges. During the third quarter, we also accrued \$2 million of legal expenses related to the expected settlement of legacy litigation. Excluding volume-related expenses, Vision 2025 related charges and the litigation settlement accrual, our adjusted operating expenses decreased by \$9 million compared to the second quarter, reflecting the ongoing benefits of our efficiency improvements.

Looking ahead to the fourth quarter, we expect origination volume of between \$4 billion and \$6 billion and pull-through weighted rate lock volume of between \$3.8 billion and \$5.8 billion. We also expect our fourth quarter pull-through weighted gain on sale margin to be between 240 and 280 basis points.

The reduction in our volume guidance reflects the seasonal decrease in home buying activity, and the reduction in our gain on sale margin guidance primarily reflects a proportional increase in volume from our joint venture channel seasonality. During the fourth quarter, we expect expenses will continue to decrease driven primarily by lower volume-related expenses but also from lower salaries from headcount reductions and lower marketing expenses as we approach the seasonal decrease in volume.

Looking beyond the fourth quarter, as Frank mentioned, we are targeting an additional \$120 million in annualized expense savings. \$100 million of which will be non-volume related. This plan is already in flight, and we expect to achieve most of our run rate savings by the end of the first quarter of 2024. The majority of the planned savings consist of non-headcount-related reductions, including vendor contract

terminations and renegotiation, optimized marketing spend, lower corporate real estate costs as well as other savings across other expense categories. The remainder of the savings are FTE and organization related.

Our focus on cost reduction, efficiency, margin expansion and effective capital management have underpinned our ability to maintain a strong liquidity position in the face of the ongoing market contraction. Importantly, we ended the third quarter with cash balances essentially unchanged from the prior quarter end. We remain laser-focused on maintaining significant levels of liquidity as we progress toward run rate profitability.

With that, we're ready to turn it back to the operator for Q&A. Operator?

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of John Davis with Raymond James.

Taylor DeBey

Raymond James & Associates, Inc., Research Division

This is Taylor on for JD. Maybe just to start with how you're thinking about just timing of returning back to profitability. You obviously made pretty significant cost cuts already and announced an additional cost savings. I understand macro makes it difficult to predict, but just any further commentary or update that could give -- that you could give on your runway to get back to profitability would be great.

Frank D. Martell

CEO, President & Director

Taylor, it's Frank Martell. Appreciate the question. We're really pleased with the continued reduction in the loss profile. And if you look at \$35 million, roughly speaking, in the third quarter, accounting for seasonality, I think we're optimistic that we can get to profitability as we get into the spring selling season and into the second and third quarters of next year. I think that's what we're planning on barring any exogenous downside in the market that we can't see at the moment.

Operator

[Operator Instructions] There are no further questions -- Kyle Joseph from Jefferies has queued up.

Kyle Joseph

Jefferies LLC, Research Division

Just kind of want to get your take on the supply and demand dynamics in the industry. And has supply come down enough to, I think you talked about kind of muted originations into '24? Are we getting to an equilibrium? Or do we still need some supply to be taken out?

Jeff Alexander Walsh

President of LDI Mortgage

Yes. This is Jeff Walsh. I think from a capacity standpoint, we are seeing capacity come out of the market, both on the fulfillment side and the origination side. We see originators leaving as well. But the market production at this point is still greater than the capacity reduction. So in the kind of rates being higher for longer scenario, we likely need a bit more capacity reduction. And we're seeing that as really kind of forming up as an opportunity for us if that happens.

Kyle Joseph

Jefferies LLC, Research Division

Got you. And then just a quick follow-up for me. Just refresh us on your capital allocation priorities in terms of buying back debt or balancing that with originating loans and just how you're thinking about that.

David R. Hayes

Chief Financial Officer

This is David Hayes. So we're going to continue to maintain that sort of an opportunistic view on that perspective. We're continuing to invest into the company in all sorts of growth initiatives in automation, and we'll continue to do that. And from a debt perspective, we're very focused on maintaining higher levels of liquidity as we progress through the next several quarters into the tougher market. And as we address the 2025 notes that are out there, we'll look at their overall debt stack at that time. But I would say that's our near-time priority.

Operator

[Operator Instructions] There are no further questions at this time. Frank Martell, I turn the call back over to you.

Frank D. Martell

CEO, President & Director

Thank you, Jean. Look, thanks, everybody, for joining us today, and we appreciate the questions as well. On behalf of David, Gerhard, Jeff Walsh and Jeff DerGurahian and the rest of our team, I want to thank everybody and our key stakeholders for their support. We look forward to keeping everybody apprised as we continue to progress against the imperatives that I outlined as part of our Vision 2025. We are making significant progress, continue to reduce our operating losses and maintain very significant levels of liquidity and importantly, position the company for the eventual rebound in the market when that comes.

So again, appreciate your time today and look forward to updating you in the future. Thanks, everybody.

Operator

This concludes today's call. You may now disconnect.

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