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Earnings Call

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Call Participants

EXECUTIVES

David R. Hayes
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Jeff Alexander Walsh
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ANALYSTS

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Taylor DeBey
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Presentation

Operator

Good afternoon, and welcome to loanDepot's Second Quarter 2024 Earnings Call. All lines have been placed on mute to prevent any background noise. After the speakers remarks, there will be a question-and-answer session. [Operator Instructions] Thank you. 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

Thank you. Good afternoon, everyone, and thank you for joining loanDepot's Second Quarter 2024 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, the status of litigation 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.

Our presentation today contains certain non-GAAP financial measures that we believe provide additional insight into analyzing and benchmarking the performance and value of our business and facilitating company-to-company operating performance comparison. For more details on these non-GAAP financial measures, including reconciliation to the most directly comparable GAAP measures, please refer to today's earnings release, which is available on our website at investors.mondepot.com. A webcast and transcript of this call will be posted to our website after the conclusion of this call.

On today's call, we have Lone Depot President and Chief Executive Officer; Frank Martell; and Chief Financial Officer; Dave 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 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. I appreciate everyone taking the time to join us on the call this afternoon. Today, I look forward to sharing my perspectives on the following 3 topics: first, the progress we're making toward achieving our Vision 2025 strategic program; second, loanDepot's Q2 operational and financial performance highlights, which I believe validates the significant progress and impact of Vision 2025. And third and finally, our current view of market conditions and the outlook for the balance of 2024 and 2025.

As you know, we announced Vision 2025 in mid-2022 in response to one most abrupt and significant contractions in housing and mortgage volumes in a generation. Over the past 2 years, Vision 2025 with its 4 strategic pillars has been the battle plan that we followed to tackle market realities in the short term, while positioning the company for profitable growth, market leadership and sustained value creation in the years ahead. A brief description of the scope of the 4 pillars of Vision 2025, as well as a short synopsis of the progress we've made against each of these pillars follows. Pillar #1, focuses on transforming the company's origination business and driving purchase transactions with expanded emphasis on purpose-driven lending and first-time homebuyers. Over the past 2 years, we've added new products that address affordability issues such as AccessONE+ and AccessZERO. We've expanded our VA lending operation, and we've invested in our point-of-sale and mellohome platforms.

Pillar #2, which centers on investing in profitable growth generating initiatives and launching innovative cutting-edge solutions that form the foundation of a life cycle relationship with first-time homebuyers

and homeowners. In this area, we launched and expanded our home equity suite of products, including a home equity line of credit, and stand-alone second mortgage loan, we deployed our next-generation MelloNow digital underwriting engine, brought our servicing business in-house and expanded our unique joint venture business with homebuilders.

Pillar 3 calls for the reducing complexity and simplifying our organization structure with an emphasis on driving client engagement, quality, automation and operating leverage. To date, we have revamped our compensation programs to drive revenue and best-in-class quality, as well as support recruitment and retention of best available talent. We've also reduced the number of organizational management layers and eliminated unnecessary silos in many parts of the organization, including loan production and operations.

And finally, Pillar 4 targets the aggressive rightsizing of Loan Depot's cost structure to be in line with marketing realities, while investing in our long-term goal of becoming the lowest cost, highest quality producer of home lending solutions. By the end of 2023, we had reduced annualized nonvolume-related expenses by over \$660 million from the second quarter of 2022. During the first half of this year, we completed an additional \$120 million productivity program. The implementation of Vision 2025 has been instrumental in successfully navigating the historic downturn in the mortgage market over the past few years. We've reset the organization for the reality markets while building our operational capabilities. While we've delivered on a comprehensive set -- reduction of our expense base, Vision 2025 is far more than just a cost-cutting exercise. It also requires us to continually invest in our people, products and technology platforms. We believe these investments position the company to significantly expand market share and grow profitability going forward.

Over the coming months, we will be pivoting from Vision 2025 to a new strategic plan, which will lay out the road map we plan to follow to innovate and drive sustainable market leadership and durable profitable growth as a lifetime partner for customers over the course of their entire homeownership journey. We plan to announce the details of our new strategic plan during our upcoming Q3 earnings release cycle. Now in terms of our second quarter performance, by most measures, I believe we delivered our strongest operational results since the beginning of the market downturn. As I mentioned earlier, I also believe that loanDepot's Q2 operational financial performance provides important points of reference for the progress and impact of Vision 2025. Our positive operational momentum was driven by profitable adjusted total revenue growth, as well as our ongoing commitment to cost discipline and the progressive introduction of platforms and tools, which support automation and operating leverage. We also continued to see strong contributions from our well-regarded servicing operation. The combination of those factors contributed to higher margins and market share gain in our origination business in Q2. In terms of total profitability, in Q2, we achieved positive adjusted EBITDA of \$35 million, and reduced our adjusted net loss by 56% year-on-year to \$16 million.

One final and important note on Q2. During the quarter, we successfully completed a tender exchange of our 2025 unsecured notes and reached a tentative agreement to settle class action litigation associated with our January cyber-attack. These milestone achievements, which Dave will elaborate on a bit later, provide important clarity and visibility for all of our stakeholders. Looking forward to the balance of 2024 and into 2025. In July, the Mortgage Bankers Association increased their forecast of 2025 mortgage market volumes to \$2.1 trillion. This compares with our current estimate of \$1.8 trillion for 2024. As we look ahead, based on increasing potential for moderation of mortgage interest rates, as well as more homes for sale going into 2025, we believe there is an increasing possibility of an upward trend in housing transactions and mortgage market activity led initially by growing household formation trends, and the demand for home equity linked mortgage products for home improvement, debt consolidation and/or personal liability management.

Over the past 6 months, we have been investing in our origination capabilities by boosting the number of loan officers and our operational staff, as well as investing in products and processes that will provide operating leverage with specific focus on a range of home equity solutions as well as refinancing and purchase products. The company is also actively working to expand our in-market retail franchise with the additional staffing and product offerings, which primarily serves the largest portion of the market home purchase. With the investment in new products, people and platforms that we've made to date and those

currently in flight, we believe we are increasingly well positioned to expand market share and accelerate our revenue growth with our expanding portfolio of lending and lending adjacent solutions for homeowners as market volumes begin to track upward heading into 2025.

I want to conclude my prepared remarks today by thanking Team loanDepot and our other stakeholders for their ongoing support. Our focus on delivering against our Vision 2025 imperatives is positioning us for the future while creating a pathway for market leadership and profitability as the market returns to more normal levels of activity. With that, I'll turn the call over to Dave, who will take us through our financial results in more detail.

David R. Hayes
Chief Financial Officer

Thanks, Frank, and good afternoon, everyone. Our adjusted net loss decreased from \$36 million in the second quarter of 2023 to \$16 million in the second quarter of this year due both to higher adjusted revenues and lower operating expenses. Total expenses in the quarter were impacted by approximately \$37 million of nonoperational charges that Frank touched on. We accrued \$27 million, primarily as part of reaching an agreement in principle to settle the class action litigation related to the January 2024 cyber incident in which, as Frank noted, will put the impact of this class action cyber litigation quickly behind us. We also successfully completed a tender exchange of our 2025 unsecured notes, extending the maturity to 2027 and reducing outstanding corporate debt by \$137 million. As part of this transaction, we recorded a \$6 million loss on the extinguishment of debt. During the second quarter, pull-through weighted rate lock volume was \$5.8 billion, which represented a 5% decrease from the second quarter of 2023, and reflected the ongoing impact of higher rates and the lack of supply of home sales -- homes for sale.

Rate lock volume came in within the guidance we issued last quarter of \$4.5 billion to \$6.5 billion, and contributed to adjusted total revenue of \$278 million compared to \$269 million in the second quarter of 2023. The year-over-year increase in adjusted total revenue is primarily a result of higher service and fee income and pull-through weighted gain on sale margin. Our pull-through weighted gain on sale margin for the second quarter came in at 322 basis points above our guidance of 260 to 290 basis points and compared to 285 basis points in the second quarter of 2023. Our higher gain on sale margin benefited from the reversal of the loss provision reflecting the strong credit performance of our historical production vintages, as well as growing contributions of higher-margin home equity products.

Our loan origination volume was \$6.1 billion for the quarter, a decrease of 3% from the second quarter of 2023. This was also within the guidance we issued last quarter of between \$5 billion and \$7 billion. While origination volume was down, our market share resumed its growth sector following the cyber-related interruption of the business during the first quarter. Our market share improved to 142 basis points in the quarter compared to 136 basis points in the second quarter of 2023. Servicing fee income increased from \$120 million in the second quarter of 2023 to \$125 million in the second quarter of 2024 due in part to higher earnings credits on custodial balances from higher interest rates. As part of the debt exchange, we opportunistically took advantage of strong market conditions and monetized approximately \$29 billion of unpaid principal balance of our mortgage servicing rights. As a result of the smaller portfolio, we expect servicing revenue to decrease somewhat going forward.

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 the servicing portfolio is dynamic, and we adjust our hedge positions in reaction to changing interest rate environment. Our total expenses for the second quarter of 2024 increased by \$12 million or 4% from the prior year quarter. The primary drivers of the increase were the previously mentioned one-time charges related to the expected settlement of the cyber-related litigation and costs associated with the tender exchange transaction. These were offset somewhat by lower personnel-related costs, driven by head count falling by over 400 FTE during the period and lower marketing costs.

We are pleased to report that we completed our \$120 million supplemental productivity program during the second quarter. These improvements were primarily achieved through decreased third-party vendor spend, lower SAR expenses and reduced real estate-related costs. Restructuring related and impairment charges totaled \$4 million, down from \$6 million in the second quarter of 2023. Excluding the \$27 million

cost of the cyber incident, the \$6 million loss on the extinguishment of the debt and the \$4 million restructuring and asset impairment charges, we accomplished meaningful expense savings, reducing operating expenses by 6% to \$306 million in the second quarter of 24 from \$324 million in the second quarter of 23% on a comparable basis.

Looking ahead to the third quarter, we expect both pull-through weighted and origination volumes of between \$5 billion and \$7 billion. We also expect our third quarter pull-through weighted gain on sale margin to be between 280 and 300 basis points. During the third quarter, we expect expenses will decrease primarily reflecting the unique charges we incurred during the second quarter. Our cost reset balance sheet management activities and the proactive resolution of outstanding litigation has significantly reduced our risk profile and farther the pathway towards profitability while allowing us to maintain strong -- a strong liquidity position where we ended the quarter with \$533 million of cash. At the same time, we have continued to make investments in our people, platforms and programs. While persistently higher interest rates that put pressure on market volumes, we are laser focused on our commitment to profitability and continue to work with discipline to grow revenue and manage costs. With that, we're ready to turn it back to the operator for Q&A. Operator?

Question and Answer

Operator

Thank you. We will now begin the question-and-answer session. [Operator Instructions] Your first question comes from the line of Douglas Harter. Please go ahead.

Douglas Michael Harter

UBS Investment Bank, Research Division

Thanks. Could you first talk about what type of -- or what was the coupon on the MSR that you sold in the quarter?

Jeffrey Michael DerGurahian

Executive VP, Chief Investment Officer & Head Economist

Hey Doug, this is Jeff DerGurahian. It was a lower coupon originations largely from 2020 and 2021 vintages.

Douglas Michael Harter

UBS Investment Bank, Research Division

Great. And then just more broadly then, as you look at your servicing portfolio, how do you think about the potential refinance opportunity that could come from it both today? Or are there -- or is it more of a rate move needed before you can unlock more volume?

Jeffrey Michael DerGurahian

Executive VP, Chief Investment Officer & Head Economist

There's opportunity, whether it's today through our home equity products that we continue to expand and enhance or if rates do happen to move lower, we'll obviously look to do rate and term refinances and debt consolidation to continue to help our borrower base.

Douglas Michael Harter

UBS Investment Bank, Research Division

I mean is there a rate that you're thinking about that might switch that opportunity from home equity to rate term?

Jeffrey Michael DerGurahian

Executive VP, Chief Investment Officer & Head Economist

There's still a wide range of products and rates in the portfolio. So as the market moves, we continue to use the tools we have to optimize whatever outreach we have to our borrowers.

Douglas Michael Harter

UBS Investment Bank, Research Division

Okay, thank you.

Operator

[Operator Instructions] And your next question comes from the line of Derek Sommers. Please go ahead.

Unknown Analyst

Hey, good afternoon everyone. Just looking into your Q3 guidance, could you maybe break out what's embedded or what assumptions are embedded into that guidance, particularly on the volumes?

David R. Hayes

Chief Financial Officer

Yes, I can speak to it. So one of the probably biggest assumptions as we come off of the second quarter is we did have a loan loss reserve true-up that benefited the gain on sale margin, which was about 18 basis points for the year-over-year comparative. So that coming out will reduce our gain on sale margin closer to 305. And then I think just general market conditions, a little bit of mix shift maybe towards refinance inform our guidance for the third quarter.

Unknown Analyst

Okay. Got it. And then how do you guys think about capacity moving forward, both from -- on your warehouse lines and maybe from operational headcount perspective as well?

David R. Hayes
Chief Financial Officer

I'll speak to the warehouse lines. We don't have any concerns on that front. We feel like we've got ample capacity and can ramp up as needed operationally?

Frank D. Martell
CEO, President & Director

Yes. Thanks for the question. So operationally, as I mentioned in my prepared remarks, over the last 6 months, we have been gradually increasing the number of LOs that we have and our operational capabilities as well, some through automation, some through staffing levels. And we're leaning into the anticipation that the market will continue to rebound and rates will moderate. And as I mentioned, I think that's an increasing likelihood. So we believe that we have the capacity to pick up incremental volume. But I think also the automation to pick up the operating leverage associated with that. So it's not as people-intensive as it might have been in the past. So I think we're fairly well positioned, and we're more optimistic about the rate environment.

Unknown Analyst

Got it, thank you. I'll hop back in a few.

Operator

Your next question comes from the line of John Davis.

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

Hey, guys this is Taylor on for JD. So yes, it was going to see total market share tick up during the quarter. Can you just unpack that a little for us if there's anything of note that drove the higher growth rate relative to the industry?

Jeff Alexander Walsh
President of LDI Mortgage

Yes. This is Jeff Walsh. I think our unique channel mix allows us to lean into various parts of the market, specifically new home builds, which is a strong area for us and cash-out refinance, which is a growing segment that we're seeing both in the home equity side and also just the debt consolidation side. And the most unsure part of the market has been the resale market just due to the availability of inventory. But as Frank mentioned, we're well positioned there as well with our end market retail team and gaining share in that channel as well.

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

Great, thanks.

Operator

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, Kathleen. So look, thank you, everybody, for joining our call today. I want to thank Dave, Gerhard, Jeff Walsh and Jeff DerGurahian and the rest of our team for all the good work that's gone into implementing Vision 2025. And you're seeing that, I think, increasingly reflected in the financial results. I'm really proud of the dedication and resiliency and accomplishments of Team loanDepot. I do think that second quarter results clearly demonstrate the positive progress we're making. And I think with the rising potential of improving market fundamentals and trends heading into 2025, we're going to remain laser-focused on achieving sustainable profitability but at the same time, becoming the innovated and trusted partner for first-time homebuyers throughout their journey of homeownership. At loanDepot, we often talk about home means everything, and our growing teams of professionals deliver a complete suite of products and services that fuel the American dream. So with that, I appreciate everybody's time today and look forward to updating you in the future.

Operator

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

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