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Earnings Call

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CALL PARTICIPANTS	2
PRESENTATION	3
QUESTION AND ANSWER	7

Call Participants

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

Presentation

Operator

Good afternoon, and welcome to loanDepot's Third Quarter 2024 Earnings Call. [Operator Instructions]. I would now like to turn today's 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 our third 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 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 performance and value of our business and facilitating company-to-company operating performance comparisons. 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.loandepot.com. A webcast and a transcript of this call will be posted on our website after the conclusion of this call.

On today's call, we have loanDepot 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.

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 today. LoanDepot returned to profitability in the third quarter through the successful implementation of our Vision 2025 strategic program. Our results were driven by higher origination volumes, margin expansion and the benefit of our process improvement and cost productivity programs.

As our shareholders know well, we announced Vision 2025 in July of 2022 in response to one of the most abrupt and significant contractions in housing and mortgage volumes in a generation. Over the past 3 years, Vision 2025 has been our battle plan to both deal with the realities of a significantly smaller market and positioned the company for long-term success. Achieving Vision 2025 was truly a team effort as we navigated turbulent market conditions over the past 3 years.

Before I talk about our new strategic plan, it's worth noting some of the key accomplishments of our Vision 2025 plan, which had 4 strategic pillars. Pillar 1 focused on transforming the company's origination business and driving purchase transactions with an expanded emphasis on purpose-driven lending and first-time homebuyers. Over the past 3 years, we've added new products to address affordability issues, grew our VA lending operation, expanded our business footprint with homebuilders and enhanced our mellohome offerings.

Pillar 2 centered on investing in profitable growth generating initiatives and launching innovative new solutions that form the foundation of a life cycle relationship with first-time homebuyers and owners. In this area, we launched a portfolio of home equity products, including a home equity line of credit and a stand-alone second mortgage loan. We also introduced our next-generation mellowNow digital underwriting engine and brought our servicing business in-house.

Pillar 3 centered on reducing complexity and simplifying our organizational structure with an emphasis on client engagement, quality, automation and operating leverage. Over the past couple of years, we have revamped our compensation programs to drive revenues and best-in-class quality while supporting the recruitment, training and retention of the best available health. We also reduced a number of organizational and management layers and eliminated unnecessary silos in many parts of our organization.

And finally, Pillar #4 focused on aligning loanDepot's cost structure with market realities while simultaneously investing in our long-term goal of becoming the lowest cost by its quality producer. From the second quarter of 2022, the end of the third quarter of 2024, and -- we reduced annualized nonvolume expenses by over \$730 million. While achieving top quartile loan quality production.

Achieving the objectives outlined in Vision 2025 and -- has been instrumental in successfully navigating this historic downturn in the mortgage market. We successfully reset the organization for the realities of the current market, but it's important to understand that Vision 2025 was far more than just a cost-cutting exercise.

We created new operational capabilities and made significant and strategic investments in our people, our products and our technology platforms that are intended to position the company for differentiated market leadership as the housing market recovers.

As we look forward to a healthier and more normalized housing market, it is now time for the company to look forward to a new horizon and focus on capitalizing on our many opportunities to offer differentiated value proposition to our stakeholders. To this end, I'm pleased to announce the launch of Project North Star, our new strategic blueprint for the next 3 years.

Project North Star builds on the foundational imperatives of Vision 2025, and -- including our focus on durable revenue growth, positive operating leverage, best-in-class productivity and investments in platforms and solutions that support and ultimately transform our customers' homeownership journey.

The 5 strategic pillars of Project North Star are as follows: Pillar #1, to become the leading partner -- a lending partner of choice for homeowners with an emphasis on first-time homebuyers, supporting those clients to the life cycle of their homeownership journey. To do this, we plan to develop and launch a unique AI powered relationship management and engagement platform that allows our customers to optimize their home buying, selling, equity optimization and home management experiences.

Pillar 2 focuses on growing our purchase mortgage reach and capabilities through an expanded geographic footprint and partnerships with key industry participants, including realtors and builders.

Pillar 3 focuses on continuing to invest in at scale our servicing portfolio and maintain best-in-class recapture rates.

Pillar 4 focuses on building out our low touch, automated, data-driven mortgage loan processing workflow to drive operating leverage, quality and to substantially drive turn times down. In this term, we will support a superior customer experience and ultimately, higher revenue as we deliver a consistent durable margins and profitability.

And finally, Pillar 5 is about becoming the mortgage industry's employer of choice, successfully recruiting, developing and retaining the best talent available. We will continue to simplify our organization, reduce management layers and eliminate unnecessary silos to increase innovation and ownership throughout the enterprise.

We embarked on Project North Star, confident in the talent and resilience of the 4,500-plus members of Team loanDepot. We believe our team, coupled with our unique multichannel platform provides the key ingredients needed to become the go-to lending partner for increasingly diverse communities homeowners, including first-time homebuyers and support those clients throughout the life cycle of their homeownership journey.

I will wrap up my prepared remarks today with a few observations on the current outlook for housing and mortgage markets. Over the past couple of years, the housing market has experienced challenges that have resulted in the lowest volume of existing and overall home sales since 1995. We -- the factors that contributed to lower home sales, including the persistent lack of housing stock fueled by chronic underbuilding; the hangover for ultra-low mortgage rates in 2020 and 2021 and -- and an affordability crisis impacting many first-time homebuyers can only be addressed through a concerted public-private cooperation.

Despite these challenges looking forward, the Mortgage Bankers Association recently forecast 2025 mortgage market volumes at \$2.3 trillion, which is up from a forecast of \$1.8 trillion for 2024. The MBA forecast for 2025 assumes a progressive moderation of mortgage rates as well as more homes for sale. Based on this and other internal market intelligence, we believe there is an increasing possibility for upward trend in housing transactions and mortgage market activities led initially by growing household formation trends and supported by demand for home equity linked mortgage products for home improvement, debt consolidation or personal liquidity management.

With the successful completion of Vision 2025 and an exciting new plan ahead in terms of Project North Star, we believe loanDepot is well positioned to capitalize on improving market conditions in 2025 and beyond.

In closing, I'd like to thank every member of Team loanDepot, as well as our other key stakeholders for their ongoing support. Working together toward a common purpose, you've demonstrated your tenacity, commitment and resilience in the face of significant adversity all the while delivering important positive changes and forward momentum for the company.

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

David R. Hayes
Chief Financial Officer

Thanks, Frank, and good afternoon, everyone. We are pleased that the successful completion of the strategic objectives of Vision 2025 has delivered the company's first profitable quarter since the beginning of the market downturn in the first quarter of 2022. The -- the third quarter served as validation of our strategy as we saw a modest improvement in the mortgage market, which, when coupled with the company's positive operating leverage, fueled our return to profitability.

Now as we embark on Project North Star, we transitioned to a company posture that focuses on consistent profitability and shareholder returns by growing stable revenue sources and investing in processes that will result in positive operating leverage. We reported adjusted net income of \$7 million in the third quarter compared to an adjusted net loss of \$29 million in the third quarter of 2023 due primarily to higher adjusted revenues from higher volume and gain on sale margins.

During the third quarter, pull-through weighted rate lock volume was \$6.7 billion, which represented a 19% increase from the prior year's volume of \$5.8 billion, and reflected the impact of lower rates for a portion of the quarter. Rate block volume came in on the high end of the guidance we issued last quarter of \$5 billion to \$7 billion and contributed to adjusted total revenue of \$320 million compared to \$261 million in the third quarter of 2023.

Our multichannel strategy has proven successful in the third quarter by delivering higher year-over-year volume of purchase originations in a supply-constrained market. and a meaningful increase in refinance originations, particularly during the period in the third quarter when long-term interest rates fell. Our pull-through weighted gain on sale margin for the third quarter came in at 329 basis points above our guidance of 280 to 300 basis points and compared to 293 basis points in the prior year.

Our higher gain on sale margin primarily benefited from a channel mix away from JV toward our other channels and wider overall margins across our primary product set.

Our loan origination volume was \$6.7 billion for the quarter, an increase of 9% from the prior year's volume was \$6.1 billion. This was also near the high end of the guidance we issued last quarter of between \$5 billion and \$7 billion. Servicing fee income increased from \$121 million in the third quarter of 2023 and -- to \$124 million in the third quarter of 2024, due in part to higher earnings credits on custodial balances from higher interest rates and higher custodial balances.

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

Our total expenses for the third quarter of 2024 increased by \$6 million or 2% from the prior year quarter. The primary drivers of the increase were higher commission, direct origination expenses, marketing and overtime, reflecting the increase in volume. Our third quarter expenses reflect a net benefit of \$19 million, primarily associated with the expected insurance proceeds related to the settlement of class action litigation connected to the first quarter cybersecurity incident.

Restructuring-related and impairment charges totaled \$2 million, down slightly from the third quarter of 2023. Excluding the impact of the insurance benefit, restructuring and asset impairment charges, the increase in our expenses were primarily related to higher commissions, direct origination expenses, marketing and overtime related expenses to our increased volumes during the quarter as well as higher salary-related expenses, reflecting an increase in head count as we build capacity for expectations of higher volumes going forward offset somewhat by our ongoing productivity initiatives.

Looking ahead to the fourth quarter, we expect pull-through weighted lock volume of between \$5.5 million and \$7.5 billion and origination volume of between \$6 billion and \$8 billion. Volume guidance reflects the seasonal decrease in purchase activity and the impact of funding the higher volume loans locked during the third quarter that remains in our pipeline. We expect our fourth quarter pull-through weighted gain on sale margin to be between 285 and 305 basis points.

We also expect fourth quarter to be negatively impacted by lower servicing revenue related to the second quarter MSR sales as well as the absence of the onetime insurance benefit previously discussed and higher volume-related expenses from closings of loans locked during the third quarter.

Our cost reset focused on creating positive operating leverage and balance sheet management activities have significantly reduced our risk profile and charted the path towards profitability, while allowing us to maintain a strong liquidity position. We ended the quarter with \$483 million in cash. Most notably, our third quarter results demonstrate that loanDepot can quickly accrue the benefits of a higher market volumes.

As we look towards 2025, we anticipate continued market challenges, but we believe the implementation of Project North Star will allow us to capture the benefit of higher market volumes, while we continue to capitalize on our ongoing investments and operational efficiency to achieve sustainable profitability in a wide variety of operating environments.

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 is 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 non-volume-related expenses and kind of hearing your expectations going forward. So you obviously had the benefit from the cyber insurance recovery this quarter. But excluding that, how should we think about the nonvolume expense base going forward? Just any additional plans to hire any additional investments? I just want to make sure we have our expectations properly set.

David R. Hayes

Chief Financial Officer

Yes. This is David Hayes. I think from that perspective, clearly, our volume-related expenses will fluctuate as originations fluctuate. We typically characterize those volume-related expenses as commissions and DOE, but I think you should also think about marketing expense, which is highly tied to volumes, especially in the direct channel. We've continued to be very productive or focused on productivity initiatives on the nonvolume related expenses, so we'd expect those to work some down over the course of remainder of this year and into next year.

But we are investing in revenue-generating initiatives, specifically staffing around our loan officers and our ops team members as well. So we're sort of building capacity up as we expect the eventual recovery of the mortgage market.

The other thing to consider as we go on a go-forward basis, we do see inflationary costs from vendor spend. We saw some of that come into effect in the '23 to '24 from some of our key vendors, and we would expect similar levels of activity going into '25. Those are yet to be determined though.

Taylor DeBey

Raymond James & Associates, Inc., Research Division

Got it. Very helpful. And then just on Project North Star. I think I saw that one of the initiatives was to expand geographically and expand partnerships. So I was just curious if you could elaborate a bit more on that and what geographies are you looking to expand into? And on the partnership side, are you mostly focused on expanding current partnerships or adding new ones?

Jeff Alexander Walsh

President of LDI Mortgage

Yes. This is Jeff Walsh. Geographically, there's a lot of markets in this country where we have opportunity to fill in with our in-market retail team, which we're doing organically. But we're also looking at expansion in our joint venture business with new builders, which we've recently done with Smith Douglas and exploring real estate JVs in the retail channel as well.

So focus kind of in the South and Southeast and kind of the opportunistic markets now, but there are plenty of markets for us to expand to across the U.S.

Operator

Your next question is from the line of Doug Harter with UBS.

Douglas Michael Harter

UBS Investment Bank, Research Division

Hoping you could just expand one of your closing comments. You said you would look to have sustainable profitability in '25 on under a range of scenarios. One, just kind of wanted to make sure that I heard that right. And if you could just expand on that comment a little bit.

Frank D. Martell

CEO, President & Director

Sure, Doug. This is Frank Martell. Thanks for joining the call. So look, I think as you look at the third quarter, as David said, the uptick in volume, which primarily benefited our direct channel was modest in volume, but it proved that kind of what revenue it would take to make money in the company and I think as we look forward to '25, the MBA forecast that currently sits that we get to that, and we're -- we feel pretty good about our chances of making money.

It is a fluid situation. with rates and -- but I think that we believe fundamentally that there's pent-up volume. Certainly, home equity has been an area of a lot of upside for us. And we expect refi to lead the way actually next year, and that's consistent with the forecast that MBA has put out.

So we're hopeful that there's no disruption in the market that would not get forecast off. But if we're making \$2 trillion, \$2.3 trillion market, we'll -- we feel pretty good about our chances. And just to kind of swing around to what David said earlier, I think that we feel there's a lot of work been done on the fixedcost of the company and driving automation in the company. So if we do get volume, we expect to try to drive some operating leverage as well. So we're pretty well positioned for a 2.3 market as we sit right now, and we look forward to that playing out next year.

Douglas Michael Harter

UBS Investment Bank, Research Division

Got it. And as part of Project North Star, you talked about growing the servicing portfolio. Would that be through more retention of it? And kind of how do you think about the financing of those MSRs/cash consumption of retaining more MSRs?

Jeffrey Michael DerGurahian

Executive VP, Chief Investment Officer & Head Economist

Doug, this is Jeff DerGurahian. The growth of the portfolio, I think, is going to come as the market opportunity presents itself, to the extent that we can continue on this path that we've been on and add to the portfolio organically. We'll do that. We'll also opportunistically look at opportunities to acquire MSRs if something attractive is there. I think we'll figure that out over the next several quarters where the best place to attack that growth is.

And in terms of financing it, the lines that we have to finance that are out there, and we'll lever the assets to the extent that we need the cash to grow the origination business and continue to take profitable share.

Operator

[Operator Instructions]. Your next question is from the line of Derek Sommers with Jeffries.

Derek Sommers

Jefferies LLC, Research Division

I was just wondering if you could touch on kind of the recruiting environment, what kind of traffic you're seeing there?

Jeff Alexander Walsh

President of LDI Mortgage

Yes. Thanks. This is Jeff again. We're -- Jeff Walsh. We're seeing positive traction in organic recruitment of loan originators, both in in-market retail and direct lending. It's still a competitive market, where we see offers, multiple offers made to higher end, high-producing loan originators. So is still competitive, but I think we're doing a really good job in winning a lot of really great people over the last quarter, and we're kind of continuing that strategy moving forward of organic growth.

Derek Sommers*Jefferies LLC, Research Division*

Got it. And then just on the kind of Smith Douglas partnership and maybe the builder JVs as a whole. Any kind of incremental color there would be helpful. Or these partnerships serve through the direct channel, kind of how does the expense base kind of compare to a kind of in-market origination? Or just anything incremental would be helpful.

Jeff Alexander Walsh*President of LDI Mortgage*

Yes. Our joint venture business is its own channel. It's run separately. We're really excited about this new venture with Smith Douglas, they are great group over there with a really compelling growth story. And the business model is different than in-market retail as they are typically set up as kind of a broker JV model or a banker JV model where we're obviously sharing in the profitability of the entity. But it is a very, very positive business for us because it's predictable. And obviously, new build has been a really bright spot in the market over the last couple of years versus what we're seeing in resale. So we really like that business and would like to do as much of it as we can.

Operator

At this time, there are no further questions. I will now hand today's call back over to Frank Martell for any closing remarks.

Frank D. Martell*CEO, President & Director*

Thanks, Tamika. Look, on behalf of Dave, Gerhard, Jeff Walsh and Jeff DerGurahian and the rest of our team, I really want to thank everybody for your -- for joining us for the call today.

It's exciting times at loanDepot, I'm really proud of the dedication and resiliency and accomplishments of the team here. Completing Vision 2025 represents a very significant accomplishment for the company. And importantly, we look forward with optimism regarding market leadership and taking share in the market as we focus on realizing the potential the full potential of Project North Star in the coming 3 years. At loanDepot we have a saying, we believe that home means everything, and our growing team of professionals delivers a complete suite of services that we think will fuel the American dream as we go forward. So thanks again, everybody, and I appreciate your time.

Operator

This concludes today's call. Thank you for joining. You may now disconnect your lines.

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