Podcast Transcription Session 31: Aaron Vermut

Peter Renton: Welcome the Lend Academy Podcast, Episode Number 31. This is your host, Peter Renton, founder of Lend Academy.

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Peter: On this edition of the podcast, we have a very special guest, someone that I've been trying to get on the show now for several months, but luckily the stars aligned and we were able to get our calendars all sorted today and I am very pleased to have Aaron Vermut, the CEO of Prosper on the podcast. In this interview, we talk about a little bit about the history of Prosper and about the history of his involvement with Prosper, what those early days were like. We then bring it forward to today and some of the recent developments that have happened. We discussed some of those in-depth and also move on to the future, get some idea about who Prosper is trying to be and what their plans are for the future. Hope you enjoy the show.

Peter: Welcome to the podcast, Aaron.

Aaron Vermut: Thank you, Peter, happy to be here.

Peter: Okay, let's kick it off with letting the listeners know a bit about your background and what you did before you came to Prosper.

Aaron: Absolutely. So I graduated from college in 1995. I went to Washington University in St. Louis, majored in History and German language and literature which was the perfect precursor for what I did next which was...I came out to California and I got a job in technology consulting.

Peter: Right, right.

Aaron: The non-sequeter there was that I actually started as a technical writer for a consulting firm and then transitioned into what's traditionally known as a product role within the technology consulting organization, you know, working through specs and designing systems for large MIS and data warehousing migration. It's really exciting stuff. I did that for three and a half years out in California and also in Switzerland actually for Cambridge Technology Partners.

In 1998 to 2000, I went to Wharton. I got my MBA in Finance and Entrepreneurship and after I graduated from Wharton in 2000, I moved to Washington, D.C. where I got a job with New Enterprise Associates which was a very large early stage venture capital firm that exists both in the East Coast and in Silicon Valley. It's actually one of the oldest venture firms in the country. Then I worked for the Managing General Partner of NEA for three and a half years, on the investment staff making wireless and software infrastructure investment with that team. I was a principal in that organization.

In late 2003, I actually left NEA, moved to California and started my own thing with my father, Steve, who I think many of your listeners are aware of this, he's my partner here at Prosper. We started a company called Merlin Securities, we started the company in 2004 here in California and in New York simultaneously. Our CTO is in New York and we built a broker/dealer servicing small and medium hedge funds with high end technology reporting, back office services and trading. We sort of spent the first part of 2004 building technology and broker/dealer and servicing infrastructure. Peter, as you know, when you start a new business, all that stuff takes a little time to set up. Then we did sort of our first revenue generating stuff here in 2005 and we run that business from 2005 until 2012. 2011 was our last full year of business and by the way, Ron Suber joined us in that endeavor in 2008, April 2008. That's the third leg of the stool of partnership at Prosper.

In April of 2012, we signed a definitive deal to sell that business to Wells Fargo. It actually became what is today the Wells Fargo Prime Services business in Wells Fargo Securities. We closed that deal in August of 2012 then the entire business went over and became part of Wells Fargo where Steve, Ron and I kind of ...you know, we worked for a little while before coming to Prosper.

Peter: Right, right, while you were working at Merlin, obviously you...when did peer-to-peer lending first get on your radar? Was it through Ron or did you discover it independently? How did that happen?

Aaron: : I definitely came to the space relatively late and it was through Ron....when we were running Merlin...I am usually very focused on the business I'm running or I'm working on and I didn't really pick up my head and look around until after the business was sold. In the fall of 2012, when Ron basically said to me...hey, this peer-to-peer lending thing is really interesting. He had been investing on both platforms for a number of years, you know, thousands of loans with just a general peer-to-peer lending enthusiast and he eventually encouraged you and I to take a look. We met some people involved in the business and started getting engaged, probably October, November, December of 2012.

Peter: So what attracted you to....what was the challenge, what was the reason that you decided to really do this kind of takeover of Prosper shall we say?

Aaron: Yeah, it's a really interesting story and it's probably a longer form of a book in here somewhere. When we started looking at Prosper the company was really at a real decision point in its history. Chris Larsen had been gone since March, we were looking at it in October, November the same year. The business had somewhat flat lined and had legal problems in the form of the class action lawsuit, it did not have a coherent strategy in going forward or even a permanent management team. I mean, there was an interim CEO running the company on a couple of days a week basis. So when we looked at it there was definitely....at that moment in time I think there was a round of financing that was trying to come together which had a …frankly, I think it was falling apart and so when we got engaged we started to meet up with Accel and Jim Breyer and John Locke, the guys who were managing the investment for Accel and they basically wanted Steve, Ron and I to become investors in the business. You know, we are not professional investors, we are professional managers and we started taking a look under the hood under the auspices of doing an investment in the company and very quickly we came to the conclusion that this was a very interesting business in a fast growing space with a very large addressable market.

There was an unknown liability surrounding the class action lawsuit, there was unknown technical debt in the company, how much investment have been made in technology, how well did the platform work, how scalable was it and there were just cultural and structural issues in the company that we could try to assess, but would never really get all the way to understand the risks. Within the time a lot of the closed investment of the company really needed to close a deal. But we were very attracted at the same time by the market size, by the business model, by the disruptive nature of what the company was trying to do. Frankly, the opportunity to take something the was fundamentally a great idea, but just not executing well and try to fix it.

So we kind of closed our eyes and held our noses and jumped right in. I mean, there were a lot of things about the company that we just didn't know. We put the money in and got engaged so when we got here in....I guess, two years ago last week, we had to start just going through the contracts and the bills and the customers and the business model and the liabilities related to the class action lawsuit and just start figuring it out. I'll tell you, Peter, that in the beginning we were looking at investment all the way through to the time when the deal closed. There was no certainty that we were going to do it, I mean, we didn't just jump in here enthusiastically saying...this looks like a great opportunity, let's just go take it over and fix it. We were certainly aware of some the significant risks and trying to keep our eyes open about what we were going to have to do over the coming years.

Peter: Right, right, and now...in talking to Ron Suber at length about it, the deal almost didn't come together too from what I gather. It was very much touch and go.

Aaron: Well, there were some contentions between us and the board about the structure of the deal, but also, Ron and I needed some convincing as well. I mean, there was enough....in the parlance of venture capital, there was enough hair on this deal that had made it look pretty risky.

Peter: Right.

Aaron: But at the end of the day, we had a great partner in Sequoia. We feel like we have a pretty good team and we were putting in a limited amount of money into the company so we kind of understood the limited nature of the downside and paired that off, hopefully, with the large nature of the upside if we didn't break the thing when we were trying to fix it. Frankly, we weren't tied up with Wells Fargo and didn't really know what to do with the rest of our careers anyway so it was sort of one of those……look, this is something where there's a large upside for a limited downside, let's take a chance and go for it.

Peter: So then what time...at what point did you realize....okay, great, this is a rocket ship that we've got here and we're going to really launch it. I mean, when did you sort of go from thinking, wow, I hope this is working to oh my God, this is amazing?

Aaron: From day one we knew that we were going to try to go bigger or just break it trying. Some of the key moments for us were...yeah, the first six months were the hardest. When we got here we didn't even know if the business model worked, we didn't know what we'd inherited from a technology standpoint and we certainly needed the deal with the class action lawsuit because it was just a giant wet blanket that was thrown over to the company from many perspectives until we get that settled from retail and institutional and everything, this thing that was out there. The class suit then certified and we were potentially going to trial in October of 2013, but the court mandated that we all get together and try one more time at a negotiated session to try to work things out. So the day we went and did that and the day we went in there, we settled the lawsuit. That was a very big moment for the company and definitely freed us up and started thinking about the future. We certainly didn't want to spend the next five years of our lives tied up in litigation with the certified class. It was a $10 Million settlement over four years. We figured…..wow, that was a large number in the context of where the company was at that time. Either it was going to matter or it wasn't and if we could grow then it wouldn't matter as much. If we couldn't handle it then the company was going to going to go out of business anyway, but it needed that chance to succeed. That was a real big moment for us.

In the first six months and you look at the filing, Peter, you'll see us growing from $9 or 10 Million a month originations to $15 to $21 to $27 to $33 and we got to about $33 Million originations. We are losing more money than we had been losing at $10 M originations which means we had some pretty fundamental problems in the model. We were marketing more, doing more business, losing more money. That's actually not the way it's supposed to work so over the summer of 2013, we made a number of changes to the platform. We rewrote the borrower funnel, we put in new......right when we started at the company , we put in the new credit model that Josh Tonderys, our Chief Risk Officer, had been working on, but we changed our data source from Scorex which is primarily a sub-prime scoring service to FICO 08 so we could better match our customers' expectations for their good credit and what they should get as a rate. It would lower their prices to match what we saw out there in the industry as a whole.

The real big moment for Prosper was in August of 2013 when we released those three things... the new funnel, the new pricing and the new data source. If you look at the fourth quarter of 2013, you actually see originations start to rise again from 30, 35 to 67, I believe, by the end of 2013 and if you look at the filing for the fourth quarter of 2013, you will actually see originations going up. We're still losing money, but loses actually started to come down which is what a healthy business is actually supposed to do. We started making money on a contribution basis on loans that we were marketing. We spend a certain amount on marketing, we do more money in revenue than we spend at marketing and that contribution margin from the loans are to pay for the overhead of the business and we figured, okay, now we actually have a business model that's working here and we can really now execute and grow bigger and achieve scale so that contribution will start paying for the overhead in the business and we can either break even or make money or reinvest in the business or whatever we want to do with it.

Peter: Right, that obviously....those things you put in place there it drove the growth in 2013, the fourth quarter, but by 2014 has....the numbers are obviously in the books now and it was a staggering growth going to like $1.6 Billion from $300 odd million the previous year. When you're asked about this, what are the key drivers of that astounding growth you achieved in 2014?

Aaron The key drivers...there are a number of things that we....we fundamentally rebuilt sort of that partnership borrower acquisition model at Prosper so whereas, I think in late 2013, if you look at our acquisition mix, we were like 80% direct mail/direct response on an acquisition basis and if you look at the mix at the end of 2014, we're about 40% direct mail, 40% partnerships and 20% kind of all the other stuff like SEO and Pay-Per-Click and direct to site. When we started going out and started working with Lending Tree and Credit Karmas and Bank Rates and other partners in building out affiliate programs so that we had a diversity of channels to acquire customers. At the same time, we continued to hone down on the things that we needed to do well in order to increase that contribution margin and make money on the loans when they come in. So streamlined funnel, highly efficient verification process, better customer service....we did that.

In 2014, we expanded our customer service. We have over 130 people in a call center in Texas handling inbound customer service calls. We also opened a facility in Phoenix to handle our underwriting and verification work to about a 20,000 square foot facility. About 50% of all our verification processing now happens in Phoenix which is a much more cost effective way than just trying to do it in downtown San Francisco. Frankly, the talents is there…..I mean, if you think about all the people who lost their jobs at the end of the last cycle who were working in mortgage underwriting from Bank of America and Countrywide and Wells Fargo, all these people, there's all the skills set for exactly what we need to do in terms of underwriting verification, we have that in Phoenix at a cost effective basis, so we started building that out in Phoenix.

We just got better and better at drilling down into aspects of our credit model, acquisition model, verification model so a lot of that growth was basically done on the same number of sort of targeted users and unique visitors to the site, we just learned how to convert those people into loans better so conversion is really a key order on here, conversion, conversion, conversion, in a cost effective manner.

One of the things that really sort of turned the dial for us in the year was we released the fifth generation of our proprietary credit model, we call it PMI-5 Prosper and Marketplace it actually really increased our ability to target borrowers, to identify those good borrowers who have a high likelihood to pay back and to better identify either fraudulent borrowers or potential borrowers or people who are less likely to pay back so to avoid the bad and lend more money to the good and that improved to a 40% increase in our marketing efficiency right there by targeting our customers better. If you look at the quality of loans that we've been issuing over the last year as we grew from, as you said, $359 Million in loans originated in 2013 and to $1.6 Billion in 2014 verified by third parties like PeerCube, the loan quality is actually getting better.

Peter: Right, I've seen that from a variety of sources. Just one other thing about the growth, I mean, obviously you're driving down your acquisition cost per borrower. Is that still...are you still improving on that like did you have goals for Q1 of 2015 to keep driving that cost down? There's got to be a point where it's going to be difficult to drive it down much further.

Aaron: Well, interestingly, we want to drive it down, but not the cost of growth. We want to make sure it is reasonable within the models that we have a good contribution margin and we can reinvest in the business. We don't want to squeeze our partners. We really want to focus on being able to better monetize the traffic that's coming to us rather than try to go back out to our partners and saying……..no, we need to pay you less. We're still investing in those channels, we're investing in our growth.

There's a really great flywheel effect that you get by investing in your partners. If you pay your partners on a success basis and a lot of the work that we do with our partners is they basically make like a revenue share on a loan if they refer somebody, a qualified borrower over to us, but they have to actually pick the loan. The more business we are able to convert at higher dollars, the more revenue you can share with the partner, the partner makes more money. If a partner is making more money off of the relationship they are able to spend more on placement and targeting and advertising for you on the site which means that you actually get more referrals so you get this sort of a flywheel of digital commerce where the more business we are able to do, the happier they are, the more business they send us. I just want to make sure those partners are happy, able to invest in the relationship with us.

It's a balance and there's ....when you're running a business like this there's only sort of three ways to approach marketing. You can really dial back because when you target, Peter, you can basically say…here's where my maximum return is on a marketing spin and you can look at the response rates and you sort of tail off, the deeper you mail and the deeper you market into a segment and so you could say we could go for maximum profit, that's one way. You can go for the less profitable loans where marginal revenue equals zero or marginal profit equals zero of the marginal cost so you have, basically, e-mailed deepest possible without wasting money or you can just go and mail everybody and waste money and try to grab market share. We tend to be that focused on that middle methodology which is we want to mail and we want to market to borrowers as deep as possible so we get that last loan that's profitable, but we don't want to waste money on it which is why it feels running basically a breakeven business. We're investing in channels, we're investing in marketing, we're going after that sort of last loan, but not trying to waste money doing it.

Peter: Right, okay, so let's move over to the other side of your business, the investor side. Obviously, it's no secret that you guys have done an amazing job of pulling in some large institutional investors on to your platform, some of the biggest names in finance are investing in loans on Prosper. I wanted just to talk about the retail investor. Obviously, the demand is insatiable from these institutional investors and the retail investor demand seems like it's not growing dramatically, can you just talk a bit about what your plans are for the retail investors and what you're intending to do to sort of give it bit more of a balance between the institutional and retail?

Aaron: Sure, absolutely. I want to go back a little bit and just talk about.... when we first got here one of the things you have to make sure was really to go out and spend literally millions of dollars on borrower campaigns, the one thing you really want to be sure of when you're trying to start one of these platforms from a standstill is to make sure that you have that investor capacity to fund those loans because if you bring on a bunch of borrowers and they list loans and they don't get funded, you've basically created a really poor customer service experience, the customer experience for the borrowers and generated no revenue wasting a bunch of marketing dollars and have all this fruit die on the vine.

Very early on, we basically brought on these anchor tenants in terms of some of these institutional investors so we can have that core so we would know that we would not spend all this money on marketing campaigns. We could fund the loans and we could continue to learn more about our business versus going back to what we learned in the first six months of being here if we hadn't had some of those institutional guys that we were doing about $9 Million a month with retail at that time when we wanted to grow to 30. It's very hard to grow retail predictably and it's really hard to go on a one-to-one basis on a marketing level with retail. We wanted to make sure that we could prove out the borrower side of the business model first soa lot of the institutional guys were so critical in the very beginning. That being said, we are totally committed to retail here. I know we get a lot of flak for having a lot of institutional investors on the platform. Frankly, definitely they grow faster than retail because they show up with millions of dollars instead of thousands of dollars, but we maintain a very heavy legal compliance accounting function here which is state by state compliance, SEC compliance, public filing, S1s on every loan we fractionalize, bankruptcy remote structure which is the only bankruptcy remote structure in the industry that actually also applies to retail. All of this is an investment in the retail platform and all these investment that we're going to continue to make. We really feel.....like I personally really feel that the growth and the health of the retail side of the business is how we build a hundred-year company here.

If and when that there is a change in cycle, rates change, investment profiles change, the big guys are yield chasers and they could represent fast money. I think some of them will be around for a long time, I think some of them will go away. Certainly dynamic on the platform will change and naturally retail will be so important because retail does have the profile of being stickier, as we call it, and investing through a cycle.

So last year, 2014, was definitely the year of the borrower where we invested in the funnel and the credit model and making sure that the business model works from an economic standpoint.

This year we've hired a dedicated investor services product manager in our product group which is the people who sit between business and engineering to design new products and services. He's actually been with us for over six months designing the future of the investor experience.

So over the next 12 months we have a road map to not only to rebuild what we call the investor funnel which is the process of creating a new investor account. We think it needs a lot of work. It could be a lot easier integrating with services like PayPal for funding, but also to rebuild the tools that investors have access to screen loans, to buy loans, to look at their performance and to gauge how they're doing on the platform. Some examples literally would be making the API work faster, work better. One of the things I'd like to see actually is the ability for someone to come on the platform and to say...just index me, just buy me a representative sample of everything that comes across so I don't have to screen, to do this complicated screen, this criteria screen. So we're rebuilding AQI [Automated Quick Invest], we're rebuilding the web and screening experience, we're rebuilding basically everything. We're also looking at rebuilding the Folio experience although I think we need to do some work just getting it up to par. I mean, I will be the first to acknowledge that the investor side of the house does need that work.

So we have a weekly....what we call scrum where we all sit down and we talk about priorities and development schedules and roll outs for investor services. You'll really see the first fruits of that labor rolling out on the website in the beginning of the second quarter. We're doing the development work now, but I'll also say that from my perspective, the future of the business, the Holy Grail for me with regards to retail participation and broad based retail participation may not be directly related to people who are coming to our site.

Peter: For sure.

Aaron: I think that what we have as a website where investors seek us out, they understand what we're doing, they understand the product and they want to transfer money to us and open an account and start picking loans, it's still a hobbyist or like an expert experience. It's great. That's our bleeding edge, those are the people who represent the core of our business, but if you really want to get out there and get broad based exposure, you really have to create a vehicle that people can just say...hey, I want to have exposure to this asset class and they go into their Schwab or their Fidelity or whatever brokerage account and they buy a ticker and that ticker basically buys them an index at Prosper loan.

Peter: Right. I completely agree. That’s.......

Aaron: We are actually working a third party. This is not something that we would do. We are not an investment platform. We are working with third parties who are exploring, creating sort of closed in funds structures that would literally be like an ETF or a closed end mutual fund that would allow people to just buy a ticker and exchange traded product and get exposure to the asset class. For me, that is when you are really off to the races from a permanent capital retail perspective.

Peter: Yeah, I agree. I think in having individuals open up an account, you need to be more an enthusiast to really do that. I mean, the way that the majority of people in this industry is really going to get the scale that we think it will, people, yeah, people need to be able to select these as products like before 401K Plan at work and be able to say...right, that sounds great or give me some unsecured consumer loans and be done with it. I think that's the key so point taken.

Aaron: Also, when you think about it, Peter, what a wealth manager or RIA is going to say....yeah, you should transfer assets off of our platform (cross talking) to that website and buy loans, go and pick loans in an active way. If we actually had that exchange traded product then the wealth manager could say....hey, leave your money here on our platform, buy this vehicle, this low overhead expense vehicle and have a 5% allocation from your fixed income portfolio to unsecured consumer loans. That is th way it is going to have to be because you're not going to get broad based appeal for people opening up individual accounts.

Peter: Yeah, sure. So I want to switch gears a little and talk about a couple of recent developments that really just happening this month. The first is a change in your reporting. You're going from real time daily updates of your loan numbers to doing it quarterly, 45 days after the end of the quarter. I wanted to get your reasoning for that and the timing of the change and why you decided that was important.

Aaron: Sure, there's multiple aspects to the conversation around data and how we disclose. Thedetails are on the Prosper blog and exactly what we did, but, fundamentally, all the moves that we made is really designed to do two things; to preserve bidders' and customers' access to bidding data so if you're an API user, if you're looking for loans on the website, individual loan criteria is all still there, the way it's always been and investors will also continue to have access to their performance data on a loan by loan basis.

What we've done is we've removed some of the files that give you the whole picture of every loan we're doing by loan ID cross referenced with credit criteria. Why we're doing that is to protect our most valuable asset which is our data asset around underwriting. There has been rumors and there has been actual products that had been released by people who have literally gone out and pulled down our data and either tried to reverse engineer or reverse engineer it to launch their products to get a jumpstart on data.

Peter: Yeah, some of them told me they've done that exact thing for both you guys and Lending Club so.....

Aaron: And, by the way, it's effectively illegal, it's a total violation of the terms of use. Everybody who actually gets access to our data signs a confidentiality agreement. People are doing it anyway, there are bad actors in the industry. Those people are actually making probably a real big mistake by thinking that they can just use technology to reverse engineer a credit model without actually having expertise in-house. This is hard. We have statisticians and mathematicians here that are actually looking at the stuff and tweaking it every day, but, fundamentally, what we're trying to do is we're trying to just protect that asset. It's our proprietary data, it's information about our borrowers and it is our underwriting model and so we're just taking it off the open Internet and protecting it so that we can preserve value in the organization.

And then the other aspect really is on the reporting of the loan buying and stuff. Yeah, very similar to what we've seen others in the industry do, but we want to be and want to get others to focus on quarterly results. We want to have the appropriate time horizon for investment and growth and we don't think that people should be focusing on us on a day by day, month by month basis, there's variations in the business so we're just going to get into that quarterly reporting schedule now.

If anything ever happens with this business in the future regarding going public or an acquisition or anything else...that would happen anyway, and it's just a change in sort of the long standing way that we've reported like literally on a day to day basis. Again, it's to protect us from the short term wins. I mean, we're a private company and we need to have the freedom to experiment and to fail.....to miss a month, to hit a month, but we want to keep hitting our quarters. This is again controlling the reporting data. We report our finances on a quarterly basis anyway and we're just putting the originations on the same team.

Peter: Right, right. Okay, I'm going to get into that IPO question you just threw out there in a second, but before I do, I want to get back to the other big piece of news that just happened and that is your acquisition, the first acquisition in Prosper's history of American Health Care Lending. Can you like I guess…. give us some bit of a back story to how they got on your radar and why you decided to make this acquisition.

Aaron: Yeah, well, this is something we're very excited about, Peter, and I'm glad you asked about it.

We've been working with American Health Care Lending for a while now, they're actually one of our partners. They basically do what is called financing as a service. They are in a large number of doctors' offices around the country and they focus on helping patients arrange financing for elective medical procedures. So if you are at a fertility clinic and that is a subscriber to AHL's service, they will literally hook you up with a Prosper or one of the other providers on their platform and make sure that you get the financing to get that done. Again, we've been partner with them for a while and we see this as a really exciting opportunity for Prosper to expand our capabilities into the point of sale and elective medical space.

If you think about it, right now, our marketing efforts really are directed either to direct mail or partnerships for a direct response direct to consumers so B to C type of contact and AHL....their elective health offering is a B to B to C model. So they're basically going from Prosper to AHL to the doctor's office. The doctors have been trained to make the offer of credit to the customer and the customer can apply when they need the credit. This is the capability of sales, capability that we're interested in owning and continuing to build. We think that the elective health space is the perfect place to start. It is a $20 Billion a year origination market growing at about 20% a year and the thesis that we have here internally is that it's actually going to grow faster than that. There's also an opportunity, a wild card here for increased growth, where if you see more and more Americans with health care plans with high deductibles, $5,000 to $10,000 deductibles, there is room for a Prosper type loan to help them actually pay off even covered procedures.

Peter: Right.

Aaron: So we are acquiring those guys right here in January, the deal is actually closed. It's actually business as usual for them for a while, but this is really part of our strategy for 2015, capabilities building, so we can broaden the reach going forward.

Peter: So practically speaking, these are already a part of you guys. You are already obtaining new borrowers through this channels so I guess nothing's going to change dramatically, I guess, as you integrate this because you're still going to be a channel partner. I presume.......

Aaron: We're going to...yeah, sorry, Peter, we're really going to ....this is capabilities for us. We're not buying growth, we're buying technology, we're buying sales acumen and we're buying a channel so it's a little bit different. You're not going to see like a tack on, a new segment of originations that we were doing before. We are going to integrate the business, we are going to change the business model a little bit into a real competitive point of sales product which will allow us to offer the Prosper loans directly in the doctors' office with potentially competitive rates and competitive terms to the other products that are in the elective medical industry, but we really like elective medicals because it's a space that's ripe for disruption. There are a number of players in the space and it sort of operated without very much competition and very wide spreads over the last number of years and the rates are high. It's very much like the credit card business where the rates are high, there's teaser rates with back interest if you don't pay. We feel like a consumer friendly, high touch customer service experience like what Prosper has to offer could be potentially extremely disruptive to the elective medical procedure.

Peter: Sure and as you said even the broader medical and so many people now have a $,5000 or $10,000 deductible on their plans because it's getting so expensive so I can see this broadening dramatically. I want to go back to....you threw out the IPO comment. There's certainly been a lot of speculations since Lending Club went public a little while ago. I get asked this, I'm sure you get asked this every day just about, what are your plans? Is an IPO on the horizon for this year, for next year? What can you talk about it?

Aaron: Sure, as you know, Peter, it's difficult for me to make forward looking statements with regard to anything like that. I'll tell you we don't currently have a plan for going public. We haven't hired an underwriter or filed an S1 and frankly, the good news for the public is if we ever do file.....because our unique structure we cannot do a confidential filing so it will be telegraphed way ahead of time, but we get a lot of utility out of being a private company. Like I said before, we want to be able to make investments, to succeed or fail and have the variability in our months if we want to experiment with new projects. At the same time, we are getting big, we are growing fast, the macro environment is pretty good. Never say never, but like I said, there's currently no plan in the works right now.

Peter: Okay, I guess that's the best we can get from you on that. Another thing I wanted to talk about briefly was...your previous company was acquired by Wells Fargo who are active in the space, in one capacity or another. I mean, Norwest Ventures was a big investor in Lending Club...I mean, you guys have Wells Fargo cash accounts.....our investor money sits at Wells Fargo. You obviously know this company, I mean, you worked for them for a few months. Where do you think a company like Wells Fargo actually becomes more active in the space? Do you think a company like Wells Fargo would ever acquire you or take a majority interest? I mean, what are your thoughts on the large banks like that?

Aaron: Sure, I have a huge amount of respect for Wells Fargo. I only worked there for about six months though in that perspective, but I don’t know them as well as I probably could, I mean, they're really great people and it’s a quality organization. We do have our corporate banking there. When you open an account at Prosper that's where the money actually is held. They are our bank partner and I do know the individual who was leading the group that purchased Merlin is now the CFO of the entire bank. I've actually sat down and had conversations with him about their view on the world.

I think that big banks, fundamentally, are pretty frustrated. They are operating in a very strict regulatory environment and they spent the last seven/eight years convincing the regulators that they need to underwrite loans in a certain way to a certain level of quality with a certain amount of overhead that they can't just go back and say....hey, we were just kidding, we want to do also strict consumer credit under $100,000 and do all online like Prosper does. I think that they don’t want to deal with the regulatory scrutiny right now given what they're under and I think the opportunity for them relative to the things that actually are the cash cows and make them a lot of money is very small.

There are a number of banks that actually do have term loan products in their offering, but it's kind of like number 19 on a list of 20 things that they want to sell to you and I challenge you to try to find those things on their website so you don't have to apply for it in the branch. Unsecured consumer credit under $100,000 is not an area of focus. I think they perceive the regulatory risk is too high. I think the cost structure for them with the branch model is also too high. We can underwrite our loans for a cost and it's just not in the realm of possibility for banks where they are now given their structure.

So in terms of competitive offering from large banks, you may or may not see it and you may see term loans, but I don't know if you can see a peer-to-peer offering from a large bank. I think the opportunity to actually work with these guys is actually in partnership with some of the regionals, super regionals and some of the community banks as well where they don't have underwriting, they don't have the expertise, the wherewithal to extend credit to their current customer base where we can work with them and try to help them with a lending program of their own.

I don't see Wells Fargo also being able to go to their current shareholders and say....hey, we want to acquire one of these businesses at a whole large valuation and then roll it into their business which is valued by a book multiple. I just don't think that …….

Peter: Right, that makes sense. So, final question and we have gone overtime here. I really want to ask you a little bit about the growth plans when you've really focused on unsecured consumer credit basically from day one. What about moving into other areas, I mean, going down the credit spectrum, maybe moving into small business or auto....what are the plans, what are you thinking about to help grow this business over the next year to three years.

Aaron: Sure, I think one of the things you're going to see at that point of strategic differentiation for Prosper is that we intend, for the foreseeable future, to remain focused on unsecured consumer credit. I fundamentally believe that going into small business lending or mortgages and other types of secured lending or different underwriting models.......each one of those represent a new business with new underwriting criteria, with new data requirements, new areas expertise, new marketing channels. It's basically starting a new company and I think it's fraught with risk.

What we really want to do is we want to focus on exploiting the data asset that we have and that we've just taken steps to protect and being The Player for unsecured consumer credit. That means expanding out from three and five-year loans for debt consolidation which is predominantly what the loans are used for today and getting into new channels and new use cases, for example like elective medical, like home improvement, special occasions, even small business, but I was able to say small business in the way that entrepreneurs would use a Prosper loan to start their business as opposed to their credit card because part of the thesis we have around here is that credit cards are a fantastic transaction medium. They're in your pocket, they work at the point of sale and they're kind of everywhere, they're ubiquitous, but they are bad way to borrow money for more than 30 days and that we really need to get out there and we need to educate people as to what we're doing and create broader use case for the term loan product and that education, understanding and awareness is there then this market. you move from the $800 Billion a year credit card market to the $3.3 Trillion unsecured consumer credit market and you build the capabilities around point of sale finance and transaction finance and be there when people actually want to make a transaction and borrow for that transaction.

That's where the future for Prosper so we'll continue to build out product functionality, product features and capabilities. We're going to be spending this year in brand building so sometime around LendIt, hopefully, we'll see a new brand identity, greater offline channels like television, radio, terrestrial radio will continue in SiriusXM. We're going to hone our message and really the goal is to create a nationally recognized brand at the end of the year. We have a new CMO with deep e-commerce experience in marketing chops to help us do that and we're going to press our expertise and really stay the focused player in the industry on consumer credit. We will likely be deeper in the credit spectrum as we deal with capabilities building. We're going to do that point of sales finance for elective medical staff. We probably have to have a data around people with lower credit than 640 FICO, but it probably won't be an excessively large area the business for us given that it doesn't really represent a huge payoff for us from a business model perspective. It's really just more capabilities building so if you will think about that we were down to 600 FICO, those loans are inherently smaller based on the way....our loans are based on an individual's ability to repay and for the payment to make sense for that person so the loans are inherently smaller, the fees being charged are thereby even smaller. They'll not really make a ton of sense from a marketing perspective and recouping our cost.

With the opposite of a traditional lender in that respect where you see those guys rushing into sub-prime to do more and more because the rates are higher and they can make a ton of money on it, then we make a lion's share of our money on our B, A and AA loans, but we do have to have that broader set of capabilities to penetrate the markets more deeply.

Peter: Right, okay, on that note I think we'll sign off. I really appreciate your time today, Aaron.

Aaron: Thank you, Peter, it's a pleasure.

Peter: Okay, thanks a lot. Bye.

Aaron: Bye.

Peter: Well, there you have it. Certainly interesting that Prosper is choosing to focus just on the consumer credit market. It's certainly a big market and I can see their reasons for doing so. It's certainly a way for them to differentiate themselves in this industry. As much as I would have loved to have heard a secret about any IPO plans...I obviously didn't expect to. I said in my predictions post early this year that I didn't think Prosper would IPO this year. Now that may or may not end up being accurate, but I wouldn't be surprised if they use this year to really consolidate what they've done and really focus on their business. Going through an IPO is a bit of a distraction to the core business of any company. I think we may still not see that until 2016.

Anyway, on that note, I will sign off. Thank you very much for listening and I will catch you next time. Bye.

[closing music]