Welcome to the Lend Academy Podcast Episode No. 45. This is your host, Peter Renton, Founder of Lend Academy.

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Peter Renton: Today on the show, I am delighted to welcome Krista Morgan. She is the CEO of P2Bi. They are a small business lender doing receivables financing and they are someone I have known for actually a long time since way before they started. Krista happens to live in Denver and that's where I'm from and she reached out to me, we had coffee. I think that was probably four years ago when they were still very much in startup mode, nowhere near launching. So I've seen this company grow from an idea all the way through to a successful launch and now they've been in operation for 15 months.

Full disclosure, I am an advisor. I've been an advisor with this company, I think since like 2011 and it hasn't actually required a huge amount of work on my part, but they are someone that I've watched grow and I believe in them. So on this show we talk about her company, we talk about the process for borrowers, what kind of borrowers are doing receivables financing through P2Bi, how they're really disrupting the invoice finance industry and, of course, talking about on the investors' side, what kind of advantages they provide for investors. Hope you enjoy the show!

Welcome to the podcast, Krista.

Krista Morgan: Thank you, Peter, very happy to be here.

Peter: Okay, so let's get started with giving the listeners a bit of background about yourself and how you came to start P2Bi.

Krista: Sure, I mean, like all good finance executives, I got here by way of marketing, so I feel like that was the right career move. I was living in the UK, I lived there for six years and came across peer to peer lending really early on, actually, sitting around my kitchen table and I thought to myself, you know, how come people don't lend to people and as it turns out they did and there was Zopa and I just loved the idea, paid attention to the industry.

Years later, ended up...my Dad and I were just having this conversation about factoring because he had been working at this factoring company and next thing you know we were talking about peer to peer lending. We sort of found our niche in the space that no one had tackled yet and that's really it. And then I moved to Denver and decided to start this crazy company.

Peter: Okay, yeah, so tell all the listeners exactly what it is your company does and what problem you're trying to solve?

Krista: Sure, so we...this actually evolved over time, but at this point what we're solving is the gap really between the group of online lenders that provide up to a half a million dollars of working capital to the banks, which more and more like to do the bigger four or five million deals.

What we're seeing is this…a large number of companies in the middle who still want better technology, who still want a good, fair, transparent lending product and they need a lot of working capital. And so that's the space that we're going after, trying to help the kind of companies that are going into...they've got great natural food products or they have an awesome new widget in Costco, they want a better working capital product and that's what we're doing. So we're providing lines of credit, all backed by receivables and inventory to help these companies keep growing.

Peter: Okay, so then explain...like it's receivables financing, would you call it? Explain exactly...how's that different to factoring?

Krista: So, now, it's actually more of…the product, we are migrating. After a year of being a factoring company, we've actually learned that as you get into the larger deals customers really want some more flexibility and, frankly, it's a real pain to be selling a thousand invoices to a company. So we're actually moving to a hybrid...it's like a factoring meets asset-backed lending line of credit. So you still have a lot of the legal protections of factoring so our investors can still, you know, feel that their money is safe, at the same time, we want to give customers some of the flexibility of a line of credit. It's really today's technology that let's us see into people's bank accounts and accounting systems and even some of their vendor systems that really enables this type of hybrid product.

Peter: So does that mean you are owning the receivables or does the company...or are you just sort of providing a line of credit with...the company still owns their own receivables? How does it work?

Krista: Yeah, so we technically purchase all of their receivables and we get all of the cash into our lock box, but then the customer can log in and basically, we take all those purchase receivables and give them a borrowing base and we say...today, customer, you can borrow $200,000 and then they'll say, great, I want $75,000 and we just effect that transaction and give them the money that they need and all cash in the lock box is automatically paying down the line. Now there's still some invoice verification in there, there's still some of the checks and balances of factoring, but the day to day...we're taking that invoice level transaction out of the day to day of the loan.

Peter: Okay, so they're not saying, here's a million dollars worth of invoices, we want suddenly a check for $800,000 today. That's not what you're offering?

Krista: Well they could do that. It's really just so...what we'll say is, hey, today based on your invoices, you could borrow up to a million dollars, how much would you like?

Peter: Okay, so then they might say, well, we only need $200,000 right now and so then they'll take that, but they know what their maximum line of credit is, right?

Krista: Exactly, exactly, and it can vary based on how big their invoices are, but then we still have a max lending limit that has to be manually increased if they want to borrow more money.

Peter: Okay, but then what if they are a growing the business and they're suddenly…the invoices have gone from $1 million to 1.5 million over the course of say six months, does that mean their line increases automatically or how do you handle that?

Krista: So we have reviews, we have like a credit review process and it happens really fast like in 24 hours and it's actually one of our value propositions. We have a customer that we've worked with for a long time that, when they started...they needed $600,000 when we signed them and they were at $2.2 million in six months. That type of growth is actually perfectly suited to this like crowd lending peer to peer model and it's something that almost no other alternative lender can match, the speed of that growth.

Peter: Okay, so then what kinds of businesses are you seeing coming to you?

Krista: So we have a lot of staffing companies across different industries, so a lot of staffing and services companies, a lot of technology products. We've got a SaaS line of credit specifically designed for SaaS companies based on their MRR, that's been a hugely popular product.

On the receivables and inventory side, we're seeing a lot of natural foods. We actually are just going into the pet product vertical, so many pet product companies are opening up and really any kind of CPG. So you're selling into the big retailers, their payment terms really stink and they'll put big purchase orders out so you really need to be able to get some inventory financing as well.

Peter: Right, so let's just talk about that for a second. The inventory financing that you're doing, is that backed by receivables or is that a completely separate product?

Krista: It runs in the borrowing base. What we're trying to do is also streamline our own operations so by moving to this line of credit structure we can say, okay, we're...for the most part our borrowing base is a function of your receivables. However, on some of our big deals...like we just signed Ronco, which is a big consumer product company out of Austin and they also needed some inventory and the line is so big and the protections that we have in the company are so big that we're able to give them additional capital on top of their A/R for inventory.

Peter: Okay, but you don't do...you wouldn't do a line of credit just based on inventory?

Krista: No, no, so some of those...I know there are some people that really specialize in them in the early stages, that's not our model. There really has to be…usually it's for the bigger deals and they have a lot of A/R and we're supplementing their A/R with inventory.

Peter: Right, okay, so then what about the loan terms, I mean, what is the typical interest rates, the advanced rate that you're doing, the length of the term of the loan...just give us a range of a typical kind of deal.

Krista: Sure, so our lines range...they range in size from about half a million to $4 million, they're one year revolving lines of credit so renewable one year agreements. The typical terms I would say right now, our interest rates are running from about 15% up to kind of 23/24% all in and everything now is based on an outstanding daily balance. So your borrowing base is 80% of the value of your receivables for the most part, but we're still only charging on an outstanding daily balance so we're actually moving to a very simple pricing structure that we think is important because people...it's amazing how hard it is to figure out what you're actually paying.

Peter: Oh, I know, that's whole thing, that's...there's this whole business borrower bill of rights that's been going around that the guys at Fundera who I'm going to have on again actually to talk about at some point…there's just so many...it's apples and oranges and lemons and limes. There's just so many different varieties of loan products for a small business. It's not like a consumer loan, it's like you can get a revolving line of credit, there's factoring, there's term loans, there's MCA, you got so many different options, so I get it, I think it's hard for a small business owner, particularly...the typical small business owner is not a finance expert and I can see...the simpler, the better. I think that's great.

Krista: You know what, though, it is amazing how hard…so we as we've introduced this new product...because we used to charge like a monthly rate on an advance rate so you're actually paying more because you're paying on 100% of the receivables, but you only got 80% of the cash. Now we're going out with just a flat daily rate, you multiply it by 365 and you know what you're paying every day and we've had, amazingly, a ton of push back, people like…hey, this rate is like 20% and we're like yeah, It's 20%, that's what you're paying and they're like, but I have this term sheet that tells me it's 12% and I'm like, great, send me your term sheet. We'll, do the calculation and the term sheet they have is like actually 33%.

Peter: Right, right, exactly.

Krista: ...and it's just...but it's really hard…you're trying to be transparent, but it feels like we're the first ones to be transparent.

Peter: Well, believe me, there's a big movement afoot and I think the small business area is full of opaque loan agreements that are...I am hoping we're moving away from that. I appreciate the fact that you guys are trying to be transparent because I think...to me it's better for business, it causes less friction and it's just the right thing to do.

Krista: Sometimes not the easy thing though.

Peter: Correct, correct, sometimes. So then you got a deal signed up, a line of credit deal, what information are you gathering and what are you sharing?

Krista: Oh gosh, we gather a lot of stuff, everything that you would expect, two years of financials, A/R and A/P, we gather tax returns, both business and personal for 20% owners or greater, we take copies of people's drivers licenses, we do background checks, we do credit checks, we do a lot of tax lien checks to make sure there are no outstanding tax liens and what we really do is we pull together all the documentation, we summarize it in a credit file and we present the summarized credit file to our investors. That said if people want to see the underlying detail, we're willing to share it, we just don't make it public due to data privacy issues. So that's broadly what we're looking at.

Peter: Okay, then how are you protecting the investors, like if...what sort of security interest are you taking?

Krista: In almost all cases, we take UCC-1 liens plus we are buying the receivables, plus we usually do notification and verification of the invoices so we're still doing a lot of those factoring type management processes that give investors additional security and then we also have all the cash coming into the lock box and that's a big thing. You have to send the cash in a lock box not just for what you've sold, but really for everything. And so all of that cash...and it's good for you because it reduces your balance right away so you'll end up paying less, but that's a huge protection for us and then we're just working on like we talked about earlier, bank account integration, making sure...like just trying to protect against fraud in those scenarios.

Peter: Right, right, sure. So let's just talk about fraud and bad debts and that kind of thing. I mean, it sounds like you're collecting a lot of information on the company, but then you're buying invoices that…are you underwriting the final buyer of the invoice as well or...answer that question and then talk about fraud and bad debts and that kind of thing.

Krista: Sure, so what we do, if I was to say our underwriting is 100% call it, you know, 50% is really on the underlying credit of the company. You know we want companies that are growing 50% on the top line that are...they don't have to be cash flow positive, but we have to see a path to that, so a lot of the attention on their balance sheet and their cash position and then it's probably about 30% on the owner so their personal credit. We do like personal guarantees so what's the character of the owner and then the remaining is on the payers themselves, so we do look at it.

What I will say is because we buy...because we're not an auction site, where you're just selling one invoice, we really buy all of your invoices and so we're willing to take your larger customers, but also the smaller ones. In natural foods you get a lot of like independent grocery stores, for example. We will take those because we see the diversification of everything and I'd say about 50% of our portfolio is kind of Fortune 1000.

Peter: Okay, so then as you say you're buying all of the invoices…for that you may have in there companies that don't have very good credit so how has it gone as far as collecting on all of the invoices?

Krista: Well, so far, so good. So far, we have suffered zero losses in our portfolio since May of last year so we're running on about 15 months of sort of very positive track record. We've purchased now just about $100 million in invoices so we have had a default, we have had one customer default where there was an issue...like there was an underlying issue with the invoice, there was subcontractor lien and it just got messy. We ended up collecting, we have a settlement agreement from the owner so that's being paid out over time and that's really it.

We've had a couple of clients like go into what we call a "collection" where the account is not performing very well and we've had to be quite strict with them and manage them out of it, but in all of those scenarios we've collected our money and recouped investor money so it's performed extremely well.

Peter: So given that you own the receivables, I imagine you've got to have some pretty…you own a lot of receivables, you've got to have some pretty efficient collection processes in place. I mean, I've imagined a lot of this is happening just month to month without any friction from you, without any intervention from you, but what do you do when like you see someone's…one invoice is 15 days past due, what's your process?

Krista: So the people who are...we have two people who kind of process accounts receivable all day, everyday, and what they'll do...so we monitor aging reports weekly, so we'll look at the aging reports and say, okay, is there an account here that we're worried about. If one invoice is aging out, we go to the client, we say, hey, we'd like to charge this back. Like this invoice where you…contractually, they have to buy them back after 90 days and usually with receipts coming into the lock box, we will charge that invoice back against those receipts.

So it's very kind of...it's in the normal course of business that an invoice may age out and we charge it back. If there are like a set of invoices that are aging out and we're feeling concerned...you know, first step is we call the client and we just try to understand what's going on, tell us what's happening, how do we figure this out. We have had a customer on a payment plan before where like a percentage of every receipt had to go and pay down this outstanding balance so we work through issues, but very much in the normal course of business. I think as a borrower as long as you're communicating with us, we will work with you and try to find a solution.

Peter: Okay, okay, fair enough. How are you finding your clients? You mentioned a few different verticals, are you going at this one vertical at a time, what are doing to try and bring people into the fold?

Krista: Yes, is the answer, we are going after verticals. So, for example, if you take something like natural foods, we build our own list, we have a sales team, we do outbound calling and e-mailing and we try to get people into the process. I mean, the great thing is that we have a product that no one else really has. In our way we have some really exciting new technology coming out for borrowers that makes their lives a lot easier so we're so confident in that, it makes those outbound conversations go really well.

And I would say as a long term…like I'm also a huge believer in inbound marketing, we create a lot of content, we try to build the P2Bi brand because we actually think that in the lending space that brand is something a lot of people don't do that well and that's the one advantage having a marketing person running a financing company.

Peter: Right, right, so okay let's switch gears on to the investors' side of the marketplace. Who is investing today, you're open to accredited investors, institutional investors, where are you focused?

Krista: Yes, today we've actually been focused on institutional investors. We have a pretty large crowd of accredited retail investors, over like a hundred active investors and that's worked really well for us, but to scale as we start to think about scaling the company, we really needed some more institutional partnerships so we've been having a ton of those conversations, re-working agreements, I mean, as I'm sure you know there's a lot of process and reporting and just sort of legal infrastructure that you need in order to take institutional capital. We're in the process of on-boarding a handful of new funds.

Peter: Okay, so you said you've done $100 million roughly in the last 15 months, like what is it on a monthly basis now? Like if I was a new investor coming along, how long would it take me to deploy like $10 million?

Krista: Today, we think to deploy $10 million it would take at this point about three to six months, given the other capital we have on the platform. So we have kind of on any given day right now about $10 to 12 million outstanding and that's been growing pretty quickly so we expect that number to look like closer to $35 million by next spring. Our goal is to...if we want to hit a billion dollars in lines of credit in three years, we need to grow about 11.5% a month.

Peter: Right, and is that what's been happening? What has been your growth rate?

Krista: Oh gosh, average growth rate has been high. I would say the past couple of months it's slowed down a bit just because we've been...we hired a new sales director so we've revamped our entire sales process and we've been trying to onboard new capital so it slowed our growth because we haven't had the capital to really go out and take on some of the larger deals. Part of our issue is that when you want to sign $2 million deals at a time, you really need to make sure you have enough capital there to do it so that you're credible to those borrowers.

Peter: Right, right, what about...when you're presenting to investors what do you talk about...returns, average returns that an investor can expect?

Krista: We say between 8 to 14%. On average, so far, our crowd has yielded I think netted out 11.66% with the 60-day liquidity.

Peter: Right, that is the thing that's very compelling I think about your product is the fact that you can get double digit returns with 60-day liquidity. There's not many products at all anywhere where you can get that kind of return. As far as how that liquidity works, because you're churning out…you're getting the capital in on a daily basis, so an investor...just so I'm clear, someone puts $2 million to work on your platform and in six months time they say, yeah, I'm done, I want out, do they get their entire principal back within 60 days, is that what you're saying?

Krista: Yeah, we use 60 days as an average, but what would happen is that every…they would ask to divest that capital and then every piece of cash that comes into the lock box they're entitled to a proportional share of that cash based on their ownership percentage of the deal and so we would release that cash to them as it comes in. We actually reconcile it weekly so every week you'd get like an amount of cash into your account and then we expect it to take no longer than 60 days. Some deals pay faster, some deals pay slower, but that's the general guidance for how long it will take.

Peter: Right, okay, when I was on your website yesterday and I saw...it looked like there were ten open deals right now. I'm thinking about diversification from the investor perspective, how long would it take to get diversified across say 50 deals?

Krista: Well, depends how fast we onboard new....you know, at this point we're looking to onboard about five to ten deals a month this quarter is our goal. Some of them are smaller, some of them are bigger, but that's our goal so we have about 35 active lines of credit as of right now.

Peter: Right, but not all of them are open to investors, right?

Krista: Well, not all of them are open, some of them are full and then some of them haven't started like haven't quite started funding yet. We also have balance sheet capital, so some of them have balance sheet capital in them so it just depends on the deal.

Peter: Right, right...are you more investor constrained or borrower constrained would you say today?

Krista: Today, probably it's a bit of both, I would say within the next two weeks it'll be all borrower and really borrower is our big focus as a team.

Peter: So you're about to onboard a couple of big clients then?

Krista: Exactly.

Peter: Right, okay. So then you've kind of got this sort of pretty unique product, when you're talking to...obviously, investors have choices even though...the 60-day liquidity is a great selling point, but, still, investors obviously have choices and borrowers have choices. When you're talking to say borrowers, who are the competitors that you come up against?

Krista: It’s a lot of the old school kind of traditional lenders like LSQ, Porter Capital we come up against like maybe less so, but it's these kind of niche-like factoring companies for the most part. We sometimes get someone like who's had an OnDeck loan or a FundBox loan and is moving over to us, but for the...our rates are usually a lot lower and we're able to lend much larger amounts than those guys. We're not usually competing head-to-head for deals, people are coming to us after they've had their OnDeck loan.

Peter: Right, okay, so then you don't really...there are obviously companies out there offering lines of credit, but it sounds like you're still playing in the factoring space for the most part as far as what your borrowers are considering, when they’re considering you, they're looking at other options on factoring.

Krista: Often, yes. Some people…so with our SaaS product we've seen people compare us with Lighter Capital, some of the revenue-based lending so it probably depends on the profile of the customer, but, yes, I would say in large part if you're talking CPGs, staffing that's very much like where factoring companies play, you know, they love those deals.

Peter: How are you competing against them, like you look at other players in this space, in the online lending space, where there's speed, there's ease of use, there's all kinds of advantages that these newer players have over the traditional players, are you seeing that same advantage in your space?

Krista: Absolutely, absolutely we are, we have a company that's about going to come on at $3 million deal, that is. They have to two full-time people up here managing their line. They're basically with a bank, but like the factoring arm of a bank, and the CEO just came into our office and she was like...it is terrible, like I have two full-time people, I have no idea where my receipts are, I can't figure out how much I'm paying, I can't get the reporting in a timely way like she was just...I mean, two full-time people is a lot to be managing your financing line and she just…and when she looked at us and we said, look this is how it's going to work, she couldn't believe it, like how easy it was going to be.

So I think technology is...that is the thing that really differentiates us, you know, trying to use it in smart ways. We've used every factoring…we've like gone and tested all of the different factoring software in the industry and we recently tested one where...I'm not joking, it only runs on Internet Explorer on Windows.

Peter: Oh, geez.

Krista: We're a Mac shop, so I went and got a Windows license...and this is like the latest and greatest factoring software and I was like, you know...that technology is what their customers are interacting with to get invoices in…like it's not acceptable in this day and age. Someone has got to come in and disrupt it.

Peter: Right, so the disruption that you're doing...I mean, I just want to go back a little bit to the....when you're first underwriting the customer, you talked about the tax returns and the different things, are you using technology to shorten that process? It sounds like you spend a bit of time, what is the lead time from when a company says, yep, we want to go with you till when they get their money?

Krista: So our overall sales cycle...like we just did a big analysis of our data runs at like 57 days, however, the quickest we've done a deal end-to-end is in about I think in about 5 days. So it can go much faster, it's usually that customers don't have the information or you're going back and forth on pricing or whatever it is, we didn't follow up quickly enough so we can already see some really easy wins to get that sales cycle number down and we are working on technology to make it much easier to upload the docs. We keep constantly like revamping our underwriting list to make sure…like do we actually need this document, is this critical or are we just asking for it or is there another way we can get this information.

Peter: Right, right, I had Kathyrn Petralia from Kabbage on just a couple of episodes ago and they are like 100% automated so you can get your money...they're doing much, much smaller numbers than you as far as the line of credit goes, but the way I look at it...I mean, moving towards an automated way is such a win for the small business if they don't have to go and hunt down all of the financial information themselves. So what automation are you putting in on the borrowers' side?

Krista: So we're just about to launch our new...what we're calling our "Lending Hub" and so that will enable customers to like get us documentation in a much more streamlined way so that they're not having to hunt through e-mails to figure out what's actually needed. There's a lot of just dashboards and clarity on what's needed. We're working on financial system integration and we're just working with some of our suppliers to...so for example, you can request like tax returns through the IRS directly and like what would that cost and how would we do that and can we do that in an automated way. But there's no question like we want to move towards making it self-service, making it a lot easier, but, I mean, full automation...it's a tough thing when you're doing million dollar...

Peter: Yeah, that's probably not going to happen ever, certainly not anytime soon…but, I mean, when you're doing $20,000 it's a bit different. So you talked about this getting to a billion dollars in receivables, how are you planning to do that, I mean, how long, what's your growth plan, what do you need to change today to get to that level of scale?

Krista: Well, we need to build an awful lot of technology between now and then to make us more efficient so that...because as we think about scale we really think about decreasing operating cost as a percentage of revenue so how do we do that, how do we build great technology that really makes us more efficient so that's a huge piece. We have four developers, I imagine a year from now we'd be at least double or triple that number. So a lot of technology built, a lot of just sales infrastructure, sales processes, making sure that we are very regimented as a sales team.

We've just started working with SalesLoft, everyone is on cadences, we are very focused at being an extremely efficient sales organization and then continuing to build the team and the culture. You know, we're big believers that we hire really smart people and we let them make us better (laughs) and I think that is something that we're going to have to do if we want to hit a billion dollars in credit lines…so that's the goal, a billion dollars in signed lines of credit by summer of 2018.

Peter: Okay, it will be here before you know it. Before I let you go, I just want to talk about your podcast. I know you're a marketing person and you have your own podcast, why don't you tell the listeners a little bit about that.

Krista: I really appreciate you mentioning that, Peter. Yeah, my friend, Lizelle Van Vuuren, who runs awesome MeetUp group in Denver called "Women Who Startup," she and I wanted to take this women to startup concept and just put a podcast together. We just finished our first season, 10 episodes and it's interviews with awesome female founders and leaders and we just talk about life as entrepreneurs, you know, the pains of angel and VC fund raising, sort of pains of building a team and culture. So it's a lot of entrepreneurial stuff, but just with a female focus, but anyone can listen, we say. (laughs)

Peter: (laughs) Right, well, that sounds great. Good luck with the podcast, good luck with P2Bi, thanks for coming on the show, Krista.

Krista: Thank you, Peter.

Peter: Okay, talk to you later.

So one of the reasons that I was attracted to this company when Krista first approached me many years ago was the whole idea of getting a high yield, we're talking about a double digit yield potentially, with 60-day liquidity. Now that's something that most small business platforms simply cannot offer. I've been an investor from really before they launched, since they were in beta and I've got a small investment there and I continue to invest in new deals because I think this whole concept is very compelling, it’s very compelling for investors and I think once they get to get more of a track record I could see them doing very, very well.

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

(closing music)