LEND ACADEMY

PODCAST TRANSCRIPTION SESSION 56: VINCE PASSIONE

Welcome to the Lend Academy Podcast, Episode No. 56. This is your host, Peter Renton, Founder of Lend Academy.

(music)

Peter Renton: Today on the show, we have the CEO of a company that is quite unique in our industry. I'm delighted to welcome Vince Passione who is the CEO of LendKey. Now, bank partnerships have become all the rage in the last couple of years and it's interesting that now there's so many announcements being made and partnerships being formed. Well Vince and LendKey have been doing this now for many years. Vince has run LendKey since 2009 and they are pretty much exclusively focused on bank partnerships and helping banks sort of expand on their offerings to their local community. I wanted to get him on the show just to really understand his company because it is unique and I learned a great deal actually in this podcast. We go through how their platform works in depth, we talk about all the different banks and credit unions that they're partnering with and also where he sees the industry as it is today. Hope you enjoy the show!

Welcome to the podcast, Vince.

Vince Passione: Thank you, Peter.

Peter: So let's just get started by giving everybody a bit of background about yourself, how has your career kind of led you to LendKey.

Vince: Sure, so started my career in development in IBM, I spent about ten years there and I transitioned from development into sales and marketing and I ended my career at IBM as the Business Unit Executive for IBM covering Citigroup globally. I always tell folks that my client got tired of me selling to them so they eventually hired me so after ten years at IBM, I joined Citigroup as their CTO in charge of the US Consumer Bank. I held that position for about six and a half years and towards the last year and a half of my tenure, I became very involved building something called Citi Financial Interactive and working with a bunch of startup companies to do it, we were incubating this internet bank. So that was my first real close interaction with startup companies that were working with a large institution like Citi.

When I finally took my leave in Citi in 1999, I decided to sort of end my career in large companies and start my entrepreneurial career so I joined forces with the Ricketts family. They were starting an online personal financial management website called OnMoney.com and I became the CEO of that in 1999. We launched that product, think of it as Mint back in 1999...so we launched that and some say we were too early in the market, some say we were too late because 2000 happened and we were successful in selling the business.

I spent some time working in Ameritrade building their institutional client division and eventually, I joined up as the President and Chief Operating Officer of DealerTrack, Inc. which was in the auto finance space and we built a credit portal. Lot of synergies with where we wound up with LendKey. Back in 1999, the auto finance business was dominated by a handful of major money center banks and we had built a very interesting piece of technology that enabled dealers to submit credit applications to multiple financing sources so by providing the dealers with this portal we opened up the opportunity for lenders to very quickly step in without a distribution channel just to start to acquire auto loans. We eventually took that company public in 2005. I left the firm in 2006 and became an angel investor.

I was investigating peer to peer lending platforms back in 2009, came across the predecessor to LendKey which was Fynanz. Back then, what LendKey was doing was pretty much a program to enable wealthy people to fund private student loans. Back in 2007, it was an interesting idea, but in 2008, it was pretty tough. After the market crashed, wealthy people were about 50% less wealthy, about 100% less liquid and the interest rate curve was inverted and we couldn't pay them for the risk.

So, I spent some time with the founder and we agreed to pivot the business and to start to go and create a white label service that would enable, at that time, credit unions to originate private student loans providing them with the instant decisioning, digital origination as well as servicing. We launched in 2009, after I made my investment. That summer we had about 26 clients and then every year we grew ever since, adding new products and services, Today, we have about over 320 clients and service close to a billion dollars worth of unsecured consumer loans for them.

Peter: Okay, so can you just sort of explain exactly how everything works there because you're not a typical platform, you focused on the community banks and credit unions space so are you just providing them a technology solution and a credit and underwriting solution obviously within that, but can you just explain exactly how it all works?

Vince: Sure, so very interesting to see how our evolution occurred. We started off, as I said, Peter, as a white label service that allowed credit unions to originate private student loans, but over the last six years, we went through this natural evolution based on lender demands and we added other products and services. So, today, we sort of sit in that space where there is roughly $3.2 trillion worth of consumer loans and we're offering both private student loans, student refi loans, home improvement loans and personal unsecured loans. The platform is basically five components.

It starts with marketing, we use LendKey.com to drive traffic to some of our clients by aggregating up some of their marketing expenses. We can bring on affiliates and drive traffic from a common credit application and then divert them or lead those volumes to the right local lending institution for them.

The second piece of the platform is the instant decisioning. We provide the ability for our lenders to take their score card, place it on our servers in the cloud and then we give them a credit application experience on their website, so you can imagine the consumer going in and filling out some type of credit application. It might be a (inaudible) where they're using some calculators; it might be a straight up form and the end result of that is an instant decision.

The third component is the digital origination component. What happens post the approval where we then create a white label My Account section so that the borrower once approved will be notified through e-mail that they've been approved after they get the instant decision and they click on a link and their My Account section opens up for that financial institution that they have acquired the loan from and in there will be the instructions, what happens next and will guide them through the fulfillment experience, whether we need to upload documents or electronically verify income. The steps are then outlined to the consumer, they review all their disclosures in that white label My Account section and then finally the end state is that they electronically sign the promissory note. So the output of that origination process is an electronic loan jacket. The lender has an administrative tab where they go in and they can approve loans, the same way as they would approve them on paper, but now they have all that information sitting for them in the electronic loan jacket so obviously they can speed that up.

The fourth part of the business is the servicing piece. The servicing part of the solution is we have built our own servicing platform and we service in the name of our clients. So once again that white label service, so we render the bills electronically to our clients. When they click on the electronic bill it opens them up in the My Account section so they can see where fees, interest and principal are being applied, they can do a change of address, they can change their payment instructions.

And, finally, the last part of the platform is what we like to call Liquidity Management and that's the ability for our lenders to have option to take either the whole loan on their balance sheet…if they choose to, they can participate the loan out in fractions, in syndication to other lenders that they have pre-approved arrangements with that we do in real time or they can actually conduct a whole loan sale and today we partner with Apollo Global Management where our clients can sell their student refi loans in a whole loan arrangement that has been pre-determined between themselves and Apollo. So, if they pull turnkey, now that's white label, that can allow these clients to provide their own underwriting pricing, their own brands, build their own unique customer experience, but yet maintain the balance sheet they choose to or look at options to either diversify or preserve capital.

Peter: Okay, okay, so I want to unpack a couple of things there. First, so you don't fund any of these loans yourself then, you're just merely acting as a middleman. It's the banks that fund it all or Apollo or what have you, is that correct?

Vince: That is correct.

Peter: Yeah, and so what do you say when...you said they can like syndicate a loan out in fractions, can you just unpack that a little bit for us?

Vince: Absolutely. So we have clients who have come to us and said...I'm a local lender and I'm very concerned about geographic risk and we all know in lending the law of large numbers is your friend and having a geographically diverse portfolio of loans can be helpful for certain asset classes...probably the most for that matter, right?

Peter: Yeah.

Vince: So what these lenders have done through our facilitation is they sell with them and they have joined up and created common loan products. So for example, we have 100 lenders who today offer a private student loan called cuScholar and if you go to any of those 100 websites, you will see that loan on their site, same brand, hundred financial institutions all offering it. If the consumer would apply, they would get the same pricing based on having the same credit profile when they apply to any one of these one hundred clients. At the point of origination that consumer can pick the local institution they want to do business with. What they'll then do though is once approved that lending institution will open up the loan and they'll approve it through the administrative tab I told you about.

Once they're done, as soon as they hit approve, because these hundred institutions have already agreed to participate loans out, the loan is broken up into ten pieces. The approving institution holds 10% as the originating lender and then the other nine institutions will all get a message that there's a loan for them to review and it will be the same loan. They're going to get 10% of it, it all goes through the same process so in real time, what's happening here and we think it's really a best practice, is the originating lender is going to hold 10% and have skin in the game. Participating lenders are there at the point of origination and they go through the same exact approval process kit by reviewing the stipulations, reviewing the bureau, ensuring the underwriting is compliant, what they all agreed to and they hit approve.

What LendKey will do is we will then go and collect up the funding, we will fund that borrower whether it's an in-school loan, we will fund it into the school. If it's a re-finance loan, we will pay off the student's loans that the other institutions that they have loans with. When the reverse happens, when the student makes a payment or the borrower makes a payment, we take the payment into our servicing department, we credit the student's account or the borrower's account and then we conduct lender service where we break that payment up and we then distribute it to the ten lenders that happen to be on the rotary of that particular loan. And then we provide all of the financial reporting for it so it's very unique. The participation algorithm is proprietary and we believe we are the only technology company that has a real time loan participation algorithm and platform for these local lenders.

Peter: Yeah, that's fascinating. I haven't heard that before either. So the borrower often will choose their local lender because they like to do business locally. Is that typically...I mean, do they want to go with a large bank? I mean, you give the borrower these choices, how do they decide?

Vince: Yeah, we give them the information about the lender. Sometimes we'll match them with someone who is local and say this seems like the right match for you. Sometimes they might see a brand that they're aware of and select that brand. In more cases than not, they're already a member or customer of one of these credit unions or banks.

Peter: Right.

Vince: So they're seeing an offer from someone they already do business with and they select them. As you can imagine, there's great affinity for some of these brands so they'll select them. What we do is offer the options and then the consumer turns around and makes the selection.

Peter: So as far as...so say you're fractionalizing it out to ten different lenders, what does the borrower see? Do they still like...as far as they're concerned they've still got the loan with the local banker, how does that work?

Vince: This is all behind the scenes. Customer experience is they've obtained the loan from their local lender or the lender they currently do business with and then as far as participations, whether it's happening on the origination side or on the servicing side that is not visible to the borrower. So the nice part about it is that the originating lender maintains the relationship with the borrower and the originating lender keeps their brand in front of the borrower and the originating lender then still has the option to diversify, right? Or, essentially, it might be being done for capital preservation. There might be a small lender who potentially doesn't want to hold as much of this loan from a risk perspective, but they still want to maintain a relationship with that particular consumer.

Peter: Right, so the bank obviously may hold the entire loan, they may end up selling the whole loan, they have that option or they can keep just a portion of it. Basically, there is three options for these small banks.

Vince: That's right, they can balance sheet it, they can participate in fractions or they can do a whole loan sale, but in all cases, they maintain their brand and the relationship with the customer and it is not visible to the customer what's happened. And because we service, we still service on behalf of this institution so from the standpoint of...hey, this loan got sold and suddenly you've got a new servicer, that's not happening here, so we can continue because we have service level agreements with these clients, continue to service the loan on behalf of that institution the way they chose to service it.

Peter: That's big, particularly if you've got a good relationship with your local bank and suddenly they'll sell off the loan and you've got this bank you've never heard of. It happens with mortgages all the time where suddenly you take a loan out from someone and then you find out three months later or a month later sometimes you have to pay somebody else that you've never heard of. So that's a really nice benefit.

Okay then so let's just go through...so student loans are still your primary product, right? I just want to go through all the different products that you're offering today as far as loans.

Vince: Right, so our 320 clients all offer some type of unsecured personal loans. Today we have clients offering a private student loan, we have clients offering a student re-finance loan, we have clients who are offering a home improvement loan. The platform is fairly extensible so the ability to do a personal unsecured loan, the ability to do a direct auto loan, we also have those capabilities. The majority of what we've seen originating on the platform to date has been in the student and education space.

Peter: Right, okay, okay, that makes sense. So then your typical borrower is obviously someone who's either obviously a student or a recent graduate, I imagine, who's either taking out a loan for their education requirements today or they're re-financing so they're pretty young borrowers on average.

Vince: Exactly and I think a lot of our clients have chosen to offer this as the first entry point, obviously getting in very early while they're still in school, but I think what we're seeing is a very big interest in the student re-fi product because you're getting that millennial upon graduation or several years out of school where they're trying to re-finance their student loan debt. As you know, it's been in the paper a lot, the average student who's graduating has somewhere around $35,000 worth of student loan debt. What we have seen is that students are going to or our borrowers are going to our lenders looking to re-finance that debt with the opportunity to save somewhere around $12,500 over the life of that loan. So some are looking for longer term, some are looking for shorter term, but all are looking for the ability to reduce payment, to improve cash flow and to save on the interest expense on the loan over the life of the loan.

In addition, a lot of our lenders, I'd say most of our lenders who offer the student re-finance program have created a very unique product in that they offer an "interest only pay" so today, one of the products they offer, because they're offering both fixed and variable, is a 15-year product where the first four years the borrower only pays interest on the loan. Then you could see how that could be very attractive to someone who graduates from law school, graduates from medical school, is now an associate in a law firm or is a resident in a residency where their future income potential is very high, but in the short term they're dealing with residents' pay or an associates' pay in a law firm, but their student loan debt is very high. So it is a great way for them to right size their payment while they're still seeing that early increase in their income, and as their income starts to escalate so will their payment so we also see a lot of lenders offering that kind of graduated payment in the re-fi space.

Peter: Right, just talk us through some of the rates that you're charging. I mean, I know you said you've got variable and fixed and they're going to be different obviously, but can you give us some idea of the different rates?

Vince: Yeah, it's going to range by lender, it's going to range by product. Imagine now we have a 5, a 10 and 15 year variable.

Peter: Right.

Vince: We have a client offering a 20-year product. They'll range anywhere from 1.9% to upwards of almost 8.9% and it really just depends on trade off with term and whether it's variable or fixed.

Peter: Okay, okay, that makes sense. So I want to talk about all these community banks that you have which you said you've really got a unique niche here. I don't really know anybody that's doing exactly what you guys are doing. So I guess...I'm curious about like how you approach these community banks. Community banks have been under fire, I mean Dodd-Frank has hurt them tremendously and I hear a lot of them are just struggling to move beyond commercial real estate for example. So just talk about the kinds of banks that are coming on your platform and why they're coming on.

Vince: Well, I think you covered it. What you're seeing is that many of these community banks are coming under scrutiny from the regulators to diversify out of these commercial loans, commercial real estate loans. Their one source of diversification is to move over to the consumer side and if you look at someone like WSFS Bank which is a great partner of ours. They're a $4.5 billion community bank based out of Delaware, they are chartered in six states. Of the $4.5 billion at least when we started with them only $215 million of the assets were in consumer assets so they had a vision to diversify onto the consumer side and really just tried to look and see how they attract millennials. So when they looked at options with us, the first product that really made a lot of sense to them was looking at that student refinance product. They started out slow, you know, I think they probably in year one they did $350,000 of this product and then year two maybe $500,000 and this year they did over $11 million in originations. So they are very, very quickly starting to ramp this program, but as you said earlier, it's for a couple of reasons. One is clearly diversification, the other is to obviously diversify to the consumer side. The other is to start to attract that millennial borrower as a customer to their community banks.

I always joke around and say my dad was a Depression Era baby. He watched his father go through the Depression as he did as a child and he watched the banks and he watched his father sort of sit there and struggle with cash and really adopt cash as the solution because the banks failed, right, and my dad in that way too.

When I look at these millennials, I call them the credit crisis babies. They went through 2008 in their teen years, maybe while they were in college listening to their parents say things like I lost my job, I lost my investments. I think that leaves a pretty large sort of impact on someone just like it did on my dad who paid his bills in cash for a very long period of time.

And having come from Citigroup...I think Citigroup is still a phenomenal institution, I don't know that millennials connect with Citi because I think they struggle with what happened through that part of our history, that great recession so I look at some of these local institutions as the farm to table solution. They're local, they're accessible and as much as we say that yes, we've seen this big shift from in-branch to online channel and wanting to deal electronically, I've always seen that consumers will take every channel you will give them because what they're really striving for is speed, transparency and flexibility, but all that comes down to one thing, convenience.

I probably want to turn around and access my financial institution from my mobile device, I also might want to just walk by it one day on my lunch break and step in and drop off something or pick up something so I do think there's this sort of this new focus if you would on being that local institution. When I look at someone like WSFS it's sort of the way I think they're approaching the market in starting off with this student refi program as a form of diversification as well as a way to get access to this younger borrower.

Peter: Right, right, yeah, that makes sense. I just want to talk a little bit about the millennial, the target audience that you have. I mean, they're different to other generations in many ways. So how are you reaching them, how do you target these people and get them on your platform? Are you using sort of the more of the online conveniencing, are you using more of the...you want to do business with the local bank, I mean, how do you market to them?

Vince: Yes so all of the above, I think the one big distinction here is that today, across our platform, when you look at someone like Navy Federal Credit Union. Navy Federal Credit Union is the largest credit union in the United States, they represent over 6.5 million active and retired service personnel and Navy Federal is marketing into their customer base. They're marketing through emails, they're doing statement stuffers, they're doing ads, they're using social media and we assist so the advantage that we have is that we have access to with Navy Federal, probably over 25 million customers who all have an affinity to a brand that's doing business with us and then we assist them.

That's why our marketing channels...we will work with our clients and figure out unique ways for them to run everything from email campaigns, their social media marketing campaigns to how they get out and become known by schools if they are running private student loan programs. We have affiliates that drive traffic to our portal. We use people like Mint, Credit Karma, LendingTree and we also use direct mail where it makes sense as a valuable tool so the benefit that we have is that the organizations that we're doing business with already have many of these consumers as their customers and now what they really are doing is just selling an incremental customer an incremental product which has a marginal cost, right?

Peter: Right

Vince: …since they already know who they are, they have their emails and they have a relationship with them.

Peter: So then are you marketing under the LendKey brand in some instances and in other instances you might be marketing under the bank or credit union brand? Is that how you are doing it?

Vince: So, Peter, think of it this way, we assist our clients when they're looking to upsell and cross sell their existing customer base and we're providing all the same tools to them, we show them how to use e-mail marketing, social media marketing, in-branch marketing, we help them do pre-approved offers of credit to their existing customers and then and what we've been very successful in doing is. We help these clients reach out to new customers and when we are doing it we will market it under the LendKey brand as a portal to help someone find a local institution to offer them a loan as opposed to saying you're going to get the loan from LendKey.

In that case, we act as a marketplace of sorts, where we are now driving traffic through some of those same channels into LendKey and then we allow the consumer to fill out a credit application and you'll see this functionality become more robust over the next few weeks and we call it LendKey network. When the consumer comes in, they fill in a generic credit application, we do a soft pull…because we have over 320 institutions we can take that soft pull, we can bounce it off all of the score cards that we have within our customer base and then we can show that consumer all the potential institutions that would make them an offer and not show them the rack rate, 1.9% to 8.9%, but show them the actual rate that they will get which is very unique.

The second part is since they have all these offers, very similar if you and I went to Kayak and we said I want a round trip ticket to San Francisco and we see all these different websites quoting us, we put up on the left hand side a filter mechanism so the borrower can say I only want to look at fixed rate options, I only want to look at five-year options, I want to shop based on payment and what they'll see then is those offers very similar to what happens on Kayak start to become more customized to exactly what they're filtering on.

Now, finally, when they hit select, typically in many of these marketplaces what will happen is you'll bounce out and you'll be on a totally new website, typically the website of the financial institution that you clicked on. In some cases, I should say most cases, you start over again, the information hasn't been passed. We have created straight through processing since we are also doing not just the marketing, but we are handling the instant decision, we're handling the origination servicing.

The next click moves them over to fulfillment where all their information is already filled out. The only thing we're asking them to do now is to either give us consent to electronically verify information or start to upload documentation from them so we can go to fulfillment for the specific lender that they selected. So that's how we envision our marketplace providing both marketing opportunities as well as fulfillment opportunities and really sort of building on those three tenets we talked about earlier which is transparency, speed and flexibility for the borrower.

Peter: That makes sense, that makes sense. So before I let you go, I just want to ask you about bank partnerships in general. It's interesting, you've been doing this since 2009 and you probably watched as companies like Lending Club start to partner and Prosper and others, OnDeck are doing the thing with Chase and it sounds like you've been doing this for a long time. So what do you make about the big movements just in the last year or two for these marketplace lending platforms to partner with the banks.

Vince: Certainly the last sort of 20 months or so what we've seen is this big focus on partnering with banks and I think the successful marketplace lenders have certainly got the attention of traditional financial institutions and the disruption is something that I think that they all are starting to see and recognize that they have to have a reaction to it. As you know, many of these financial institutions are struggling with a very difficult regulatory environment with Dodd-Frank with legacy systems which makes it very difficult for them to react. It's getting to the point now where their investors are even asking now...what are you going to do about this? In some cases what you'll see and we are starting to see it happen now is they're all faced with this build versus buy decision.

We continue to see our pipeline grow because more and more RFPs are being issued by institutions who are looking for a white label solution, a lending as a service solution as opposed to just buying loans and I think many of our clients if you were to ask…I can either go buy loans from a marketplace lender or I can make loans through someone like a LendKey and that's the decision before them. If I look at the advantages that these traditional financial institutions have aside from the potential challenges on technology is they have the lowest cost of funds in the industry as a depository institution.

Credit unions current cost of funds is probably about 50 basis points, the average community bank is just slightly over 100 basis points. They very easily can be a prime money lender and not struggle with diminishing margins. As we see a rising rate environment occur, we are going to see more and more push now as marketplace lenders who need these relationships if they want to continue to stay in this prime lending space. So I think it's going to be a very interesting year ahead of us as we listen to the industry that more and more financial institutions are starting to look at how they respond to the growth of marketplace lending and they start to come up with their own strategies for offering online lending solutions to their customer base and we hope to be the recipient of many of those contracts in providing that white label service that we've done for our 320 clients today.

Peter: Sure, well sounds like you probably will be. Last question, so where do you go from here? Are you planning on just...you said moving out from that 320 to 500 or 1000 or are you planning…you mentioned auto briefly, are you planning on adding to your product line, where does LendKey go from here?

Vince: I think we grow in sort of two dimensions. The first, I should say three, is continue to grow the base on the platform we have today and the other is continue to add more products and services. The killer application is really a single credit app where the consumer is approved for all possible offers within a financial institution and we want the ability to sit across the table from a traditional bank and say that yes, we can create you a generic credit app, we can do a soft pull and in one interaction with a consumer you can offer them a student re-fi loan, an auto loan and potentially a mortgage.

So adding those additional products and services is where the industry wants us to go and the last piece is continue to add more lenders. It is a network effect, it's what we experienced at

DealerTrack; more lenders you get, more borrowers will be attracted into the marketplace and that makes an awful lot of sense. We're starting to see the size of the institutions and complexity of the institutions grow. As you know, today we have credit unions like Navy, we have banks like WSFS, now we have people like Apollo on the back of our platform, providing some liquidity so we see more of that in 2016 and beyond.

Peter: Okay, fascinating discussion, Vince, I really appreciate you coming on the show today.

Vince: Peter, thanks for having me.

Peter: Okay, bye.

It is really interesting to me that the narrative has changed so dramatically. When I first got into this industry, it was all about disrupting the banks and the fact that we don't need banks and we really want to replace banks. Now, I think the industry has completely adjusted for the most part, not everybody is on board with this vision, but the vision of partnering with banks and I think it really is a way for the traditional banks to increase their efficiency.

I love the LendKey model because you've got local...people often want to do business in their local area. That's one of the weaknesses I think of marketplace lending is that it's online so by its very nature it's national and we sometimes lose that kind of local connection and that's what I see...LendKey, one of their strengths is that they can maintain that and that's the way that I truly believe that bank partnerships are the way forward and this whole online lending space is a way for small banks to really become more relevant or more successful as time goes on. They've shown, the regulators have made it tough, they've had a lot of headwinds in recent years and I think this is one of the few opportunities they have to grow.

Anyway on that note, I will sign off. I very much appreciate you listening and I'll catch you next time. Bye.

(closing music)