



PODCAST TRANSCRIPTION SESSION NO. 206 - RISHI KHOSLA

Welcome to the Lend Academy Podcast, Episode No. 206. This is your host, Peter Renton, Founder of Lend Academy and Co-Founder of the LendIt Fintech Conference.

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Today's show is sponsored by LendIt Fintech Europe 2019, Europe's leading event for innovation and financial services. It's coming up on the 26th and 27th of September in London at the Business Design Centre. We've recently opened registration as well as speaker applications. You can find out more by going to lendit.com/europe

Peter Renton: Today on the show, I'm delighted to welcome Rishi Khosla, he is the CEO and Co-Founder of OakNorth. Now OakNorth only started in 2015, so they're just over four years old, but already they are the most valuable fintech company in the UK, they raised the largest ever funding round for a European fintech and they've been able to do this, they've been able to grow very rapidly, at the same time, in a profitable way.

They're one of the few fintech companies that actually make a profit, but having said that, they are also expanding aggressively internationally and we talk about that in some depth in the show. They're putting a lot of effort into the US market, we talk about the differences between the US and the UK, how they're growing their US presence, how they are approaching their international expansion in a very different way than the way they approached the growth in the UK. It was a fascinating interview, I hope you enjoy the show.

Welcome to the podcast, Rishi!

Rishi Kosla: Thank you.

Peter: Okay, so I like to get these things started by giving the listeners a little bit of background about yourself. I know OakNorth is not your first rodeo so why don't you tell us a little bit about what you did before OakNorth.

Rishi: Sure. In 2002, my business partner and myself set up a company called Copal, it's basically a financial research company, we set it up with a view of servicing major financial institutions, initially the large investment banks, then private equity funds, asset managers, etc. We actually made good on that vision so fast forward 12 years on we were a 3,000 person organization which we built using a total of \$50,000 in terms of capital.

It was very capital efficient in terms of how we got there, our client base included pretty much all the top ten global investment banks, a number of major private equity firms and asset managers and then we sold that business to Moody's Corporation and 3,000 people were distributed around I think it was 12 offices in [inaudible] countries.



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Peter: Okay, so then you sold that. What was the impetus to start OakNorth, what did you see that really led you to attack this which is something that really hadn't been done before in a digital way. So what was the opportunity you saw?

Rishi: Sure, so the real opportunity...the seed of the idea came through a particular experience that we had. Back in 2005, when we were building Copal, we went to a commercial bank for a line of credit because, as I said, we sort of used a total of \$50,000 to build that business so we were balancing pretty finely from a working capital perspective so we went to a commercial bank. They told us very politely where to go and we went to another commercial bank and we had exactly the same experience.

A few months later, we went to an institutional desk at one of the large banks and that institutional desk gave us a credit facility which was for a hundred times the amount we were asking for from the commercial bank (Peter laughs) and they had no issue with it. And we were like, wow, this just shows something is broken somewhere and you could argue that the institutional desk was a little bit too aggressive, but the answer was surely somewhere in between rather than the answer the commercial banks gave us, ie of zero.

So that sort of caused the seed of the idea and as we played out the business of Copal and we were coming out towards exiting it, we kept on coming back to that particular issue we had and saying, you know, is this a structural problem, is it something which applies across markets, is it cycle related, etc. etc.

We became very convicted that, actually, there was a very strong opportunity because this is an underserved segment. It's been underserved for very specific reasons and therefore, actually a very strong opportunity to build a business within and also building a business which fundamentally has a lot of net positives for communities within the markets that we would be playing in.

Because fundamentally, we'll be helping put capital into the hands of companies which are growth companies, small, mid-sized businesses which tend to be the drivers of GDP and employment growth in many countries. So we felt like both from the perspective of solving a real problem, solving a problem which is actually a good problem to solve for countries and communities and also clearly building a good business, it sort of ticked the right boxes.

Peter: Before you launched, I mean, obviously you would have done some market research so you said you went out looking in like 2005, did you find out ten years later that it hadn't changed at all? I'm just curious about the target market you're after, these fast growth companies, they're not really being served by the Funding Circles' of the world because they need more capital than Funding Circle's max, so what are their options today?

Rishi: Their options are to go into a commercial bank and get a very standardized loan package which is fundamentally based on backward looking data from the borrowers, from the value of the data you provide and backward looking analysis is great if you're not a growth company because, you know, your next 12 months looks pretty similar to your last 12 months.



But if you're a growth company, your next 12 months may look nothing like your previous and therefore, actually having a lending institution which is only going to look at your historics so it does not get you very far in terms of meeting your needs so it gets you with a very sub-optimal loan package.

Peter: Okay, so what are we talking about here? Can you tell us the range of loan sizes and the terms, the interest rates sort of thing you're talking about and what's the median?

Rishi: Sure I mean, so in terms of the range of loan sizes we're talking about roughly from half a million up to...depends on which market, let's say plus/minus \$30 million. In the UK it would be plus that, in the US, it would probably be just a little minus that, in some Asian countries it may only be up to \$5/10 million, in terms of where the unmet need is. Average term, roughly three years, average loan size \$5/6 million, those type of numbers so within that type of range.

Peter: Okay, and what's the typical interest rate?

Rishi: The typical interest rate is appropriate for the risk which we're taking on.

Peter: Is there a range, obviously you're not approving everybody, is there a range that you work within?

Rishi: Sure, I mean the range is anywhere from 4% to 8%, that type of range.

Peter: Okay, okay. And so I know that you're not just doing loans, obviously, that's kind of how you've built your business primarily to date, but I know you've really got two divisions of the company. Maybe my first question is, with this sort of software-as-a-service or banking-as-a-service type of product that you have, was that the intention...first, describe the product and was that the intention always from the get-go to have these two divisions?

Rishi: Sure, so the first thing I'd say is we don't actually look at it as two divisions. What we were very clear on is that to provide this type of customized loan packages that we felt were needed within this market segment, you needed to be able to do much more detailed analysis on the particular companies that you were looking to lend to and that detailed analysis looks much more like what you would do on a large corporate loan, i.e. if you were doing a loan of a few hundred million.

And we knew how to do that pretty well from our last business because that's the type of stuff we did day in, day out and we were clear that we needed to bring technology into the equation to be able to apply that same methodology down to smaller ticket sizes. So we actually started by actually saying, we need to build a platform which will enable us to take that corporate approach to be able to provide customized bespoke lending to smaller businesses and mid-sized businesses.

That's where we started and we were very clear that we needed to prove the market opportunity as well as the functionality of that platform in one market and therefore, the bank is very



much...in the UK, where we started actually building that proof and obviously have built a pretty strong loan book here in the UK on the back of it. But as a core theme, it is all about providing customized lending to small and mid-sized companies and globally, we're doing that through obviously providing our platform to existing banks rather than creating our own bank in other markets.

Peter: Right.

Rishi: So we'll continue to obviously build our own bank in the UK and continue to use that to test and evolve our own platform that fundamentally, as I like to say, we think of this as a horizontal play around solving this problem on a global basis, rather than a vertical play of building a bank in one country.

Peter: Right, right, got it. Okay, so then I want to just dig in a little bit into the technology you use because you're making these decisions much more rapidly, I believe, obviously than a traditional bank so how are you using this technology? What's sort of involved in the underwriting process and what have you automated? How does it work?

Rishi: Sure, here's the fun part. So not only are we doing things quicker, but we're doing things quicker on the basis of actually having done significantly more work so if you go back to what I said, most banks in this space actually take a backward looking view based purely on borrower data. Whereas, what we're doing is we're taking the borrower data, we're obviously looking at historic, but then we're using lots of different data sources to be able to create a forward looking view for that particular business. And that's something which other lending institutions in this part of the market, i.e. small and medium-sized businesses, tend not to do.

So we're doing significantly more work in much less time, and ultimately, that's enabled through the platform. So what does the platform do? The platform effectively helps pull in both the borrowers' data, but also locks up said third party data sources and when I say lock, on any particular case, it may be 5, 10, 15, 20, but if I look across the platform, it's thousands of data sources which the platform will go out to across different cases.

So you pull in all of that data and then you use that data, fundamentally, to create benchmarks on a forward looking view so you can have conviction that your forward looking view has been stressed appropriately to be able then to formulate a loan package which is both appropriate for the borrower and more suitable for their business, but at the same time also clearly meets the risk appetite of the lending institution.

Peter: Right.

Rishi: So that at its core is what the platform does.

Peter: So these companies that are coming for a loan, obviously they have their own forward looking projections and I am sure you look at those, but from what I hear you saying, you're saying you create your own based on the data that you've seen so obviously you're not going to



rely just on what they say and you're creating your own forward looking projections, is that how it works?

Rishi: Exactly, so we take obviously what the borrower says, but then we formulate our own perspective.

Peter: Right, right. Okay, so back to the bank for a second, I mean, you've been famously quoted saying you've experienced zero defaults to date. The unfortunate thing about being famously quoted for that is there's only one way to go from there (laughs) because you can't do better than zero.

Rishi: I one hundred percent agree (Peter laughs), and let's be clear that there is only one way to go and it's inevitable that you'll go there, right?

Peter: Right.

Rishi: So I think what we're very clear on is that we will perform, both in the current market environment but also in a downturn, at a level which is significantly better than the market in the segment that we play in. So we clearly, as a lending institution, at some point you're going to have defaults, but we have a very strong conviction that the default rate that we will have and therefore, the loss ratio that we will have will be significantly below market.

Peter: Right, that's fair enough, that's fair enough. So one more question about the bank before we get on to your international expansion. Are you funding all of these loans through deposits in the UK, I mean, I know you're offering some of the best deposit rates. You've got a deal with Monzo now I read about, is that how you're funding the loan book?

Rishi: In the UK, that's exactly right.

Peter: Right. Okay, so then let's move along to...I know you've opened up a US office recently and obviously most of the listeners of this podcast are based in the US, although we do have a substantial international following, so you're opening up in the US and I am curious about the...I get the problem is very, very similar.

I've heard that this segment of the market is very much underserved in this country as well, but isn't the approach going to be very...I mean, every country is going to be different, I mean, the data sources are going to be different, I mean certainly the software is different, the accounting software or whatever, so how do you approach that with taking what the core of what you've built and applying it into a country that has...it's got different infrastructure.

Rishi: So the first thing to note is that we're already live in I think about eight different countries at least, so the challenge of being live in a new country with different data sources, etc. isn't actually a big challenge for us. Some of the countries which we're live in are significantly tougher countries than the US to get data. The US is relatively data rich and, I have to say, data quality is relatively strong.



Peter: Right.

Rishi: So the US, for us, is absolutely a core market that we're looking to delve into. We've already started originating in the US as well as actually licensing our platform so we have clients who are live in the US on our platform today, we're also originating loans for those clients so the client can choose just to take a platform, or they can take the platform and loans as well from us so we're not putting those loans on our own balance sheet.

The amount of demand in the US for the type of lending we're doing, I would say if anything, is stronger than even in the UK and I say that fundamentally because the US is a larger market and we're just seeing larger volumes in a very short period of time than what we had seen on a comparative basis in the UK. So the transportability of the model is very high and actually our ability to execute it as I said, is much simpler in the US than some of the other markets where you have both language, data quality and data availability issues.

Peter: Right, right. So are you just focused on the US banks, is that the market you're going after for this solution?

Rishi: So we're licensing the platform to US banks, but we're also offering the platform and loans to other institutional investors outside banks. So we're both, fundamentally, appealing to banks and non-banks.

Peter: Okay, interesting. And so I haven't heard an announcement so obviously there is nothing public yet, as far as who have signed up for your platform, is that correct?

Rishi: That is correct.

Peter: You can make an announcement right now, if you want. (laughs)

Rishi: I'm sure I can. (both laugh)

Peter: Okay.

Rishi: Thank you for that.

Peter: So then are you like ...when you look at the US market, I mean, do you see this as...obviously the market is much bigger than the UK, we know that, but where are these people being served in the US right now? Is it still the same, are they going along to banks right now and having the same experience that a similar company in the UK would have?

Rishi: Exactly right. Regional banks and having the same experience.

Peter: Right, right, okay. So then the platform, the website anyway is oaknorth.ai and ai, it doesn't stand for artificial intelligence from what I gather it stands for analytical intelligence. Is that the platform that you're going out globally with for this offering?



Rishi: Exactly right, the reason is very specifically that we call it analytical intelligence, but clearly it is a play on artificial intelligence which obviously is already embedded within the platform, but fundamentally, it's an analytical platform so that's why...the origins of the name. Actually, we used an algorithm to come up with the name (Peter laughs) just for the fun of it.

Peter: Okay.

Rishi: So, yeah that is absolutely the platform which we're referring to.

Peter: Okay, so what geographies are you live in today and what geographies are you expanding into?

Rishi: So in terms of where we're live, obviously the US, obviously the UK, Germany, Austria, the Netherlands, Italy, Singapore, Taiwan, China; that's where we're live. And where are we expanding to, I mean, you know, I think that's already a reasonable amount of breadth, I think what we're looking to do is gain increased depth within each market. Yeah, I think we've got, again, our estimate of total loan stock in this space is around \$7 trillion and we think the market is under penetrated so, you know, I think we've got a reasonable way to go.

Peter: Right, right, for sure. And the fact is there really is no global brand doing this right now. I mean, it feels like...

Rishi: Except for one.

Peter: (laughs) Right, right, there is one up and coming global brand, yes indeed. So your intention then is not to get a banking license in any of these countries, is that correct, and why not do that, why not get a banking license?

Rishi: That's correct. Why not, because we fundamentally believe that working with existing lenders in existing markets is a much more scalable way for us to actually take our platform and propagate it across markets, rather than trying to build our own regulatory infrastructure in each of these countries and then dealing with, you know, the challenges of running multiple regulated entities.

And clearly, from a capital perspective, the amount of capital it would take to run a bank in each of these different markets would require us maybe tens of billions and, therefore, it's just not the most efficient way to either bring in capital, use capital, also not the most efficient way to [inaudible].

Peter: Right, right. So this sort of SME growth business segment is obviously huge, but I noticed recently that you've also expanded your product offering in the UK to mortgages for the entrepreneurs, the business owners of these companies. So tell us a little bit about that product, was that driven by your customers, or why launch that product?



Rishi: If you look at what we've done within the core, it is very much about how do you create a tech platform to be able to provide customized lending into a segment which isn't used to receiving customized lending.

Now when you look at what we're doing in the mortgages space, we're not doing standard mortgages. We're doing complex mortgages where we need to be able to look beyond the types of basic parameters that a standard clearing bank would look at. Therefore, the approach which we take has (inaudible) and the underwriting is actually very similar for these types of assets as well as we do in our core.

Now clearly the end customer, instead of being a business in this scenario is a company, but it's clearly one in the same in the way that a lot of these clients are going to be business owners and therefore, we're servicing them on their personal requirements, rather than on their commercial requirements. So we felt like it very much leverages the core of our approach and our platform, number one.

Number two, although it's not technically the same client segment, it's technically the same client.

Peter: Right.

Rishi: Right, so therefore, it's actually very much in keeping with the mission that we have.

Peter: So is that something that you intend to roll out across the other markets eventually?

Rishi: Exactly right.

Peter: Okay, so then like I'm just curious then, you're live in the US and how many people do you have in your US office now?

Rishi: Plus/minus 20.

Peter: Okay, do you think that's going to be your...what's the plan for growing that? I was in your office just last month in London and it's quite a sizable workforce there. Are you intending for the US to grow into that kind of size?

Rishi: Yeah, very much so, very much so.

Peter: Okay. So then talking about the funding round, there was a lot of noise or a lot of a...not noise, but publicity, shall we say, around the funding round that you did. It was the largest ever funding round for a European fintech, \$440 million from SoftBank. I'm curious...obviously SoftBank, they're relatively active in the fintech space, but how are they helping you, or are they helping you beyond just providing capital?



Rishi: Sure, so a couple of things. First of all, you're right about the \$440 million round, SoftBank was the primary investor, but Clermont Group was the secondary investor so it was a combination of the two of them.

To answer your question on SoftBank, SoftBank are helping us and actually I have to say that they're proving to be a very strong partner for us and they're helping us in a multitude of ways. One is removing the constraints from your thinking about capital so effectively saying capital isn't a constraint; how fast can you go, how large can you go whilst still obviously maintaining some level of prudence one needs to to make sure we don't go off the rails, right, that's number one.

Number two, they are directly helping in terms of bringing in talent and identifying actually where we may need talent as we scale which is proving very useful.

The third aspect is, you know, they know a few banks who could be clients and they're being helpful in that regard so fundamentally, strategically, channel acquisition and actually from a client perspective, on all areas they are being helpful and therefore for us are proving to be a very strong partner.

Peter: Right, right. We're almost out of time, but I want to get a couple of more questions in. You mentioned China and...China is notoriously difficult to crack. I spend a lot of time in China personally with our event, we have a conference in Shanghai. How are you approaching that market, I mean, do you have like....are you partnering with a local business, are you setting up from scratch? How are you attacking the Chinese market?

Rishi: So the first thing to note is in our previous business we did operate in China, we had about 300 people in Beijing.

Peter: Okay.

Rishi: So we've operated there and that was an independent operation, i.e. standalone, and therefore operating in China isn't new to us. We have a small team in China today and we intend to, again, build that, not necessarily at a very high growth rate today, but build it and put all the right foundations in place.

The market which we're obviously looking at scaling quickly is the US market and what we want to do is take our time in creating the right foundations in China because we do understand how much tougher it is to actually build and penetrate so that's our approach to China.

Peter: Right, okay. So you know, I'm thinking as you're talking, you've got a lot on your plate. Like this is the last question then, so tell us how you spend your time? Do you spend half your time focused on the US market, are you focusing on building the team, maintaining the culture; how do you spend your time?



Rishi: All of the above so obviously the US is a key focus. I am the CEO of the regulated bank in the UK so clearly, that continues to be my main focus, but bringing in the right talent across the business in the right places is fundamentally the only way that one can scale. Therefore, that's inevitably a meaningful focus for us and then, you know, there's 24 hours in a day and seven days in a week so you can actually stretch the week pretty effectively.

Peter: Okay, well on that note, we'll have to leave it there, Rishi, I wish you all the best. You've built a fantastic business in a short amount of time and I can see that you're only just getting started. Thanks for coming on the show.

Rishi: Thank you so much, appreciate it.

Peter: Okay, see you.

Rishi: Bye.

Peter: This whole banking-as-a-service segment is truly fascinating to me. It's one that is really still in its infancy. While we've seen some companies in the consumer lending space, even in the small business space move beyond their own offering and offering it to other companies in the space, we've never seen anyone like OakNorth that are just going out across the globe fairly aggressively, taking their core technology, not just expanding it to one other country, but to multiple other countries at the same time.

If they can pull this off and they certainly have the resources to do it, they're extremely well funded so if they can execute this, they will be the dominant brand in this space and it's going to be fascinating to see how all this plays out.

Rishi is actually going to be a keynote speaker at our LendIt Fintech Europe event in September so you can find out more and listen to him at that event.

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

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