

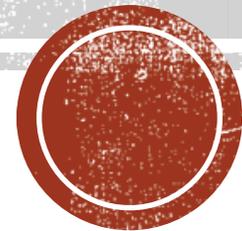
ALTERNATIVE ONLINE LENDERS

An Overview of the Changing Small Business Lending Landscape

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OVERVIEW

- **How has technology affected the small business lending landscape?**
- **Why are small business borrowers turning to online lending solutions?**
- **How can innovations in small business lending better serve small business borrowers and how have CDFIs taken advantage of new technology?**

HOW HAS TECHNOLOGY AFFECTED THE SMALL BUSINESS LENDING LANDSCAPE?

FINTECH AND THE DISINTERMEDIATION OF TRADITIONAL FINANCIAL INSTITUTIONS

Unbundling of a Bank



Source: CBI Insights <https://www.cbinsights.com/research/disrupting-banking-fintech-startups/>

CURRENT SMALL BUSINESS ALTERNATIVE ONLINE LENDING LANDSCAPE

- Alternative online lenders are non-bank lenders with business models that incorporate internet and emerging data technology to improve the borrower/applicant experience, loan decisioning, and loan funding
- The largest US small business alternative online lenders are CAN Capital and OnDeck
- Current market size of small business alternative lenders is unknown but estimated to be small vs total US small business loan market
- Growth is projected to be huge
 - PwC estimates \$150 billion by 2025
 - Financial Times estimates \$25 billion by 2019

CURRENT SMALL BUSINESS ALTERNATIVE ONLINE LENDING LANDSCAPE

- Online innovation has delivered unprecedented speed and ease of use for borrowers, and has made loan application, underwriting and decision for lenders inexpensive
 - Applications take little time to complete
 - Application and underwriting is automated with algorithms that seamlessly access applicant credit histories and extensive borrower data
 - Lenders offer fast turnaround times
 - Search Engine Optimization and Ad Tracking used extensively by lenders

DIVERSE AND NUANCED LANDSCAPE

- **Online Balance Sheet**
- **Lender/Borrower Online Marketplaces**
- **Peer to Peer Platforms**
- **Digital Payment Provider Backed Credit**

THE EMERGING ALTERNATIVE LENDERS

ONLINE BALANCE SHEET LENDERS

- Loan decisions are made by proprietary underwriting systems that rely on cash flow data, credit scores, social media data, industry geography, and other firm specific data
- APRs average 25-80%, average terms of 6-18 months
- Products offered include traditional loans, cash advances, and lines of credit

CAN CAPITAL

OnDeck



Kabbage

BlueVine

IOU Central

THE EMERGING ALTERNATIVE LENDERS

LENDER/BORROWER ONLINE MARKETPLACE

- Online platforms that match borrowers to lenders that are part of their marketplace
- Wide variety of APRs, wide variety of terms
- Often refer to banks, traditional financial institutions, and online alternative lenders



THE EMERGING ALTERNATIVE LENDERS

MARKETPLACE (Peer-to-Peer) PLATFORMS¹

- Connect small business borrowers with capital from individual and institutional investors
- APRs average 10-30%, average terms of 36 – 60 months



1. As the industry has evolved, alternative online lenders have increasingly been referred to as marketplace lenders, a term that helps emphasize the growing institutional investor base of the sector. So while peer-to-peer lenders initially allowed individual borrowers to connect with individual lenders, individual lenders increasingly are being replaced by institutional investors who are turning to online marketplace lenders for investment opportunities. Because some balance sheet lenders are now originating small business loans for institutional investors to purchase, balance sheet lenders are also often referred to as marketplace lenders. In the Treasury Department's recent Request for Information, they defined online marketplace lending as "the segment of the financial services industry that uses investment capital and data-driven online platforms to lend either directly or indirectly to small businesses and consumers."

THE EMERGING ALTERNATIVE LENDERS

DIGITAL PAYMENT PROVIDER BACKED CREDIT PRODUCTS

- Paypal Working Capital, Square Capital, Amazon Pay
- Only available to select businesses already processing payments using the payment system
- Fixed, pre-determined percentage of business' daily sales deducted – borrower determines the percentage of sales towards repayment
- A single loan fee based on amount of loan is charged



WHY ARE SMALL BUSINESS BORROWERS TURNING TO ONLINE LENDING SOLUTIONS?

WHY ONLINE LENDERS?

Small-business owners may turn to online alternative lenders for a variety of reasons.

- Simplified application process
- Rapid approvals and disbursement of funds
- Reduced bank lending to small business borrowers
- Impaired credit may make getting a bank loan challenging
- Perception that banks are less likely to lend to small firms now

Very limited data are available on and relatively little is known about firms that tend to use online lenders

FRS 2015 SMALL BUSINESS CREDIT SURVEY

Characteristics of SBCS Credit Applicants

Firms that applied with an online lender N=209 ⁶		Firms that applied with a traditional lender N=1204 ⁷
83%	ARE SMALL FIRMS Share of applicants with annual revenues below \$1M	61%
48%	ARE YOUNG FIRMS Share of applicants in existence 5 or fewer years	36%
54%	ARE FIRMS WITH GROWING REVENUES Share of applicants reporting an increase in revenues in the past 12 months	58%
38%	ARE PROFITABLE FIRMS Share of applicants operating at a profit	58%
25%	ARE FIRMS WITH CREDIT CHALLENGES Share of applicants reporting credit availability is a significant challenge	12%
36%	ARE MINORITY-OWNED FIRMS Share of applicants that are minority-owned firms	14%

Source: [Click, Submit: New Insights on the Online Lender Applicants from the Small Business Credit Survey](#), Federal Reserve Bank of Cleveland.

Note: Online lender applicants are defined as those firms that applied for financing at one or more online lenders, including firms that applied at both online and traditional lenders.

**HOW CAN INNOVATIONS IN SMALL BUSINESS
LENDING BETTER SERVE SMALL BUSINESS
BORROWERS AND HOW HAVE CDFIS TAKEN
ADVANTAGE OF NEW TECHNOLOGY?**

POSSIBLE BENEFITS TO CDFIs

- Expands product offerings that can retain and grow customer base
- Enable CDFIs to provide customers increasingly preferred online services
- Provides access to innovative technology and automated lending processes
- May allow for geographic diversification of portfolio

POSSIBLE BENEFITS TO SMALL BUSINESS BORROWERS

- Lenders' lower operating costs could lead to lower borrowing costs
- Use of industry data and benchmarks could expand pool of qualified borrowers
- Increased credit availability in underserved communities in rural or LMI areas

PARTNERSHIPS

- **CRF SPARK**

A loan origination software package for small business lenders

- **Mirador**

Platform helping lenders optimize their small business loan origination process

- **Pathway Lending**

CDFI developing a online loan application platform to integrate with their existing CRM software

PARTNERSHIPS

- **OFN Venturize**

- Educational website developed to help small business owners learn more about lending options and products

- **Opportunity Fund/Lending Club Partnership**

- Lending partnership focused on serving underserved California based small business borrowers

- **TILT Forward Initiative – AEO**

- Technology based solutions for mission-focused lending

Project Cue

TILT Forward Network

DreamFund

Reimagine TA

QUESTIONS?

THANK YOU!

- **Marysol McGee**

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