PODCAST TRANSCRIPTION SESSION NO. 162 / SASHA ORLOFF

Welcome to the Lend Academy podcast, Episode No. 162. This is your host, Peter Renton, Founder of Lend Academy and Co-Founder of LendIt Fintech.

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Today's show is sponsored by LendIt Fintech USA 2019, the world's leading event in financial services innovation. It's coming up on April 8th and 9th, 2019 at Moscone West in San Francisco. We've recently opened registration as well as speaker applications. You can find out more by going to lendit.com/usa.

Peter Renton: Today on the show, I am delighted to welcome back Sasha Orloff, he is the CEO and Co-Founder of LendUp. LendUp focuses on the subprime consumer or the non-prime consumer, if you will, and they provide a short term loan product and a credit card for this population. They actually have broader goals than just those two products which we get into in some depth.

We talk about the non-prime consumer and how they're doing, how traditional financial institutions are not serving these people, what needs to change for them to move the needle for this population. We talk about the regulators and what needs to happen there, we talk about the new study they did with Experian where they're able to take more data and show an increase in credit score for LendUp customers, and we talk about financial education and much more.

Anyway, I'm sitting here in my LendUp t-shirt, I promised Sasha I would tell him that I'm wearing it in celebration of recording this podcast show today. Anyway, it was a fascinating interview, I hope you enjoy the show.

Welcome back to the podcast, Sasha.

Sasha Orloff: Great to be here.

Peter: Okay, so I know we chatted, it was about just under three years ago, so a lot of people know about you and you have a fairly high profile in the fintech community, but for those who don't, maybe just give a little bit of a brief description about LendUp and what your mission is.

Sasha: Yeah, so what we're doing at LendUp is building the financial services destination for the half of America that's been shut out. This is the emerging middle class that don't receive the benefit of a lot of the fintech innovation that we're seeing and are structurally locked out of most banking systems, especially credit, because of low credit scores or volatile income.

Peter: Okay, so obviously your name is LendUp and lending has been the core part of what you do, but you mentioned it wasn't going to be just about lending, have you broadened your mission here?

Sasha: (laughs) Yeah, so there's two fun parts to that answer.

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The first is the frustration of just buying a domain name when you are a startup and LendUp was really the core of what the business was going to drive and be and it was six letters, two words and it was a domain that was available and there's a really funny story behind all of that that I'm sure your listeners are not interested in, but it was fun anyway, I'll tell you sometime over a beer.

Then there is the reality of the business so I think there's two versions of LendUp. There is the LendUp that people know about from the press or from coming to your conference and listening to me on stage or various other channels and then there's the LendUp behind the scenes that we haven't really talked about a lot.

The vision was always about helping people improve their financial health and that is along the categories of saving, spending, borrowing and planning and so all of our vision is to help improve peoples' financial health, but credit was the place where the industry makes money, it's the hardest to do and there was the biggest opportunity.

So while we started with thinking about what was one of the worst financial products on the market which is payday loans and reinventing that and making it better, the next was transitioning to installment loans and helping graduate people to better products at lower rates and longer terms and then credit cards. We just started incubating secured cards and that will obviously be putting us on a path to helping people also save money and use their savings to improve their credit score.

All of this comes with like one fundamental challenge that we're trying to solve which is, 56% of our country today have a subprime credit score and if you have a subprime credit score, you're going to pay $250,000 more over your life in additional interest and fees and that's a problem that's solvable with technology, product innovation and the right team.

Peter: Right, right. I've heard it said quite frequently that it's actually really expensive to be poor, it's much cheaper to have wealth and that's part of it because of all of the fees and everything. So I want to just talk about…you've been in this business now for several years so I'm curious about the state of your core audience, the sort of non-prime consumer. Are they doing any better today than they were when you started?

Sasha: I think there's quite a bit of this population that is still fundamentally ignored. So we're talking about the state of today, $250,000 in additional interest and fees, over half of America and when we start translating this into who our customers are, you think of it as your Lyft or Uber driver that took you to work, your Starbucks barista that gave you coffee this morning, the Amazon delivery driver that is delivering your packages while you're at home, the real estate agent, the small entrepreneur, that construction worker; it's everyday working America.

One of the sort of trends that we're seeing now is with the rise of the gig economy and automation of payroll system that our country is becoming less stable, not more, and that makes it even more challenging for the traditional banking system to serve them effectively. But that's where technology and mobile phones and rethinking products can actually help improve

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borrower's lives and we've seen this by increasing peoples' credit scores by hundreds of thousands of points, saving them hundreds of millions of dollars of unnecessary fees and delivering millions and millions of credit education courses. So we're making a good dent for how short we've lived and existed as a company.

Peter: So I want to pick up on one point there, the education courses. I know, I've been to your website, I've seen some of the videos that you guys do because one of the challenges I always find and this is not just the non-prime population, it's the prime population as well, a lot of people are just not interested in finance, they're just not interested in learning. They want to be financially secure and financially healthy, but they're not really interested in learning so how are you able to engage this population and help them learn?

Sasha: I think you're saying that financial education isn't fun and exciting (Peter laughs), I wholeheartedly disagree.

Peter: I'm sure it can be.

Sasha: We're dealing with the reality that people are busy and they have busy lives, their jobs are demanding and requiring, their families are demanding and requiring, and so how do we fit this in. What the industry has traditionally done is they've separated financial education and literacy into other aspects in arm's length and separately, a lot of the banking system and the financial system now wins when customers lose.

Peter: Right.

Sasha: And so when you cake these two things together by building all of our own technology, we can actually gamify good behaviors so we can use alerts, reminders, nudges and challenges to incentivize people to exhibit the key behaviors that will benefit them and benefit us….on time repayment, learning more about how the financial system works and keeping a budget and maintaining credit balances low so that they're available when the unforeseen circumstances happen.

And so that's the approach we have taken here at LendUp which is creating a business model where we only win when the customer wins and gamifying the experience so that we're optimizing for peoples' long term financial health.

Peter: Okay, so is your target customer then, I'm thinking about how you would gamify something to be very different to a 50-something than a 20-something year old. What is the core sort of audience that you're going after or are you trying to do it for all audiences?

Sasha: Well let me give you two examples.

So we just completed this study on our loan structure/product structure with one of the major credit bureaus and I think the results are published on our blog and what it showed was the

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creation of the product structure can actually have a material positive impact on somebody's credit score.

So I'll give you three very specific examples.

By having the ability for consumers to have payment plans and continue to make positive payment history which is the number one factor in your credit score, 85% of our customers would have higher credit scores, 18% would have significantly higher credit scores. The percentage of people who have subprime credit scores through our product structure drops from 79 to 65% and the percent of thin file customers, the sort of people that are invisible to the traditional credit bureaus drops from 11 to 4%.

So when we start thinking about the implications of how you can gamify and create these product structures, you can get the same amount of returns to the business, actually higher returns and you can do it in a way which really makes the customer win. On the credit card side, you can think about a lot of the industry is motivated by having people rack up high balances that they revolve and make interest on.

And that’s also the second biggest factor in your credit score is the availability of credit that you have so we create challenges and nudges to actually help people maintain a budget and pay more than their minimum due or their full balance. Just against the way the industry thinks and makes money, but tangibly helps the customer build their credit score right now.

Peter: I completely agree. One of the things that I think the banks have got to realize is that if some of your main profit centers are when your customer is suffering that is something that is...that has to have a lifecycle in today's age where things are more transparent. I think a lot of the fintech platforms that I speak with...it's all about an alignment with the customer and so you don't sort of celebrate when someone makes an overdraft or has a late fee or something.

I feel like that is something that has to change and I think it is great that companies like you are doing that. But I want to go back, the report you're talking about I actually listened to a podcast with yourself and Jo Ann Barefoot and Alex Lintner from Experian talking about this research. I think it's super interesting to me. Can you just give us an example?

You just mentioned how 86% increase their credit score and I can’t remember all of the other percentages you mentioned, but what specific data points are you talking about? Is this rent, is this utility bills, is it cell phone bills, I mean I know these are the sort of things that are still not in a traditional credit score which I think is crazy. That's a whole topic for another podcast, but what are the data points that allow this population that you're serving to increase their score?

Sasha: I think you're right on point. There are so much data sources and payment records that are just not visible in the traditional credit bureaus and so we wanted to take something that would have been very non-controversial which is actual loans, actual trade lines and simulate what a credit score would look like. So we took our own credit scores and payment records on

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loans and use those to simulate the score with the help of Alex and his incredible team over there and we showed these positive results.

But it starts to open up what is really the more interesting question which was what are the data sources that are not available in the major credit bureaus that can have meaningful impact on helping people improve their credit score, improving financial inclusion and giving people credit for the things that they're doing all the time. But because a bank can't work with them, whether it’s lack of credit card, mortgage, car loan, a home loan, a home refinancing loan, they're just not on the major bureaus and so this is the start of what we hope is a large movement of using data to improve financial inclusion.

Peter: So are you reporting the payment behavior of your customers to the major bureaus today?

Sasha: We report…so on our loans product there are four different levels and it's different availability by state and local laws, but for the most part generically, there's silver, gold, platinum and prime and so we worked hard with the bureaus to accept our platinum and our prime levels, but we’re still working with them on approving the silver and the gold levels of our ladder. The credit cards are all reported as with almost all credit cards that would.

Now we are keen on encouraging results with the acquisitions of like Clarity Services and so you start to see when you have people like Experian acquiring Clarity that they're starting to take some of this other tradeline data and putting it alongside the major bureaus. Now it's separate, but it's now more readily available. I think those are all really exciting.

Peter: Right, right. So the Experian piece, was that taking your one payment product and putting that into their system? When you talked about the 86%...I'm just trying to be completely clear about what the lift was. Was that just on the platinum and gold, whatever it was, or what was the actual piece that created that lift?

Sasha: So it came down to two key takeaways.

The first is that more reported data, including the short-term data supplemented with the data that we already report, would have an even more positive effect on consumers.

The second was looking at structure of our product so in a lot of the non-bank lending, especially those geared towards sort of short-term lending or subprime lending, you see these product structures that have these kind of teaser rates or have these debt traps that spiral out of control.

Now LendUp doesn't do any of that. You can't borrow again until you repay your loan in full, there's no accruing interest or fees or rollovers. And so by having payment flexibility, meaning when people are struggling you give them options on how to make successful payments. That also showed a tremendous impact on helping people improve their credit scores. When you think about it in the prime world, there's a lot of flexibility. If you can't make your credit card

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payment the day of your credit card payment or your mortgage payment, the day of your mortgage payment, it's not instantly turned into this rollover/refinancing situation that's reported as delinquent, you usually get options on how to bring your account current.

So we're just bringing a lot of the same best in class practices to a market that just hasn't seen it before and what the results are, turns out that you can dramatically improve people's credit scores by doing it.

Peter: Right, right. Okay, I want to talk about your credit card. When we last spoke in 2015, you had just launched your credit card so you've obviously had quite a bit of history with that now, can you tell us how that's been going, the sort of traction you're getting and what is different with that product than your other loan products?

Sasha: The credit card shares a lot of the learnings that we've had from our millions and millions of loans that we've done on the platform. It's a completely different product, it solves a different problem for a lot of the borrower, which is sort of everyday cash flow and payments capabilities and credit rebuilding so we decided that we were going to take a little bit of a long term approach to not just launching a credit card, but actually redefining how a credit card could work for the consumer.

And what happens is you get three things.

One, we've attracted an incredible team of people from the credit card industry who have always dreamed of building better models, building better product features and functionality from a de novo platform so I think that's exciting. We've really staffed up the team.

Second is we've seen incredible growth so as soon as we sort of took the covers off we actually had to shut down our website and put up a waitlist because the demand far exceeded our financial ability to maintain them or our banks financial ability to maintain them. So hundreds of thousands of people on the waitlist that we're eagerly starting to make roads to unlock.

The third is by really being thoughtful about the user experience. So knowing that it's a profitable product really trying to make sure that we're really solving a customer problem with the result what ended up happening was we're the highest rated card in the non-prime segment on Credit Karma.

So we've actually been recognized as the cardholders' choice with a near perfect score of 4.7 out of 5 in an industry that typically sees ratings of 2 sometimes down to 1 and so it's been a really exciting launch.

Peter: That's interesting to me. What are the typical credit limits on these cards and what makes them so popular?

Sasha: I think that what makes them popular are three things.

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One, it’s just transparent so its cheaper than they can get, but it’s transparently cheaper. There aren't these weird hidden fees like a fee to apply or a fee to call customer service or a fee to make a payment. It’s a straightforward, transparent, normal credit card, grace period and all.

The second piece is it’s built natively for mobile and so the experiences are designed not as a website that's been shrunk down to a mobile app. It’s actually designed to have features and functionality native to mobile that make a really good user experience from alerts, reminders, nudges, budgeting, free credit score, education, all of the things that you would expect that don't even yet exist in prime credit cards.

I think the third piece is you can see by using our card that it’s actually teaching you about how to improve your credit score. It doesn't guarantee that you're going to improve your credit score, but it gives you your free credit score. It gives you a lot more flexibility on making on-time payments, it gives you a lot more education about keeping your balances low which is the opposite of what most credit card companies, or all credit card companies, how they think about. And so you just get this really great positive feedback because it’s there to help you succeed, not for you to fail.

Peter: Right, what is the range of credit limits that you're offering?

Sasha: Yeah sorry, the rates range from 19% to 29% APR, zero to $60 annual fee, but those are depending upon risk and credit lines from $300 to $2,500.

Peter: Okay, interesting. Are these like Visa cards, Mastercards, you must be partnering with a bank to issue these, I presume.

Sasha: Yeah, we have multiple bank partners that were just sort of very motivated and interested in building products for this customer segment so we worked with them to design products and come into market and they’re a nationally based Visa credit card.

Peter: Okay, cool. So then I want to switch gears a little bit and talk about regulation and I feel like...when you talk to people in Washington, they have a very negative view of the space you operate in. I mean, I know you're fully aware of that, but there's a lot of…anyone who's charging...if you extrapolate out APRs or whatever, it can be quite challenging for them to understand the good you're doing. So tell us about what are you doing to engage regulators and are you making inroads there?

Sasha: Yeah, so this is something that I think I'm seeing improvement in the relationships between banks, regulators and fintech which is really important because the current situation of our regulation is what's causing this dichotomy, this exclusion out of the financial system. I don't think anybody believes this is intentional, but the reality is 56% of our country have a subprime credit score and if you have a subprime credit score the banking system doesn't work well for you.

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And so the divide and the problem is, the divide between the banking sector and the non-banking sector traditionally has been really, really big for the subprime market so we're not talking about great innovation like SoFi and Affirm and LendingClub and those types of players that are refinancing out debt for cheaper rates. We're talking about access and availability for everyday working Americans.

The divide has been so great and so where we really fit in is this bridge between these two worlds; helping people get from low credit scores to high credit scores and while we don't guarantee it we do everything in our technological power to design for it so that requires quite a few things. It requires investment in hiring people from the regulatory world, we have state examiners, people from the CFPB, Treasury, Federal Reserve on our staff so it helps them sort of understand and helps us understand their perspective and them understanding our perspective.

We have a very active government affairs led by Jotaka Eaddy in Washington DC who really spends a lot of time helping bridge discussions with regulators and advocates and key constituents and partners so that we're actually engaging in dialogue on both sides about how do we upgrade these laws that were written in the 70s, the 80s and even 2008 to help make banking more inclusive.

And then the third is we have to actually proactively engage and take our experiences and help it in the community, whether that's sharing best practices along compliance, regulation, product growth, controls, oversight, working with people like FinRegLab, applying for and opining on the OCC's Fintech Charter and the CFPB's sort of RFP with Project Catalyst.

So we think about this in three different approaches that it's our responsibility to help drive the conversation because we have such a huge opportunity for financial inclusion and you typically don't get that perspective so loud and clear in DC, San Francisco and New York. We're trying to kind of bridge that narrative.

Peter: Right, because sometimes I think when I read what the regulators are saying, I sometimes feel like they want everyone to have like a prime credit score. They want everyone to get prime credit, they want people to get 10% on a 3-year loan, that's what they want and they don't want this 56% of the population or whatever, they say yep, you need to charge them the same.

I sometimes think there's sort of this mismatch between what the regulators want and what is reality. I see all these talks about usury rates and all that sort of thing that they want everyone to have access to credit and they want everyone to have access to credit at like 10% and I feel like...obviously that's just not economically possible. Do you feel like, is the conversation changing yet, I mean, I haven't seen much evidence of that yet, but maybe, maybe I haven't been listening closely enough.

Sasha: We all want the same thing, we want our entire country to be prime, we want people to have readily available credit to buy homes, start small businesses, have reliable cars to get to

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work. Credit creates advancement in wealth, credit creates availability and access and mobility that enable the American dream.

Now the problem that we're facing today is over half of our country have a subprime credit score and the subprime credit score is a predictor of likelihood of default and so in order to make even just a break-even business...let's pretend that we had one bank and it was evenly controlled across the entire country and everybody was able to be priced perfectly, people would have to price differently, otherwise you're punishing responsible borrowers and rewarding bad borrowers.

Now the solution is you have to give people that first stepping stone to build and establish your credit score and we have to have a regulatory framework that doesn't just enable that, it encourages that. And so it is entirely possible, it is entirely within our control, financial inclusion is totally possible, financial exclusion is a choice that we're making. And so this is something and the only way to solve it is by letting people have that first step towards credit building. It's like your first job; your first job out of college doesn't pay Jamie Dimon's salary (Peter laughs), but we're America and everybody can get to Jamie Dimon's salary, realistically, theoretically....

Peter: Theoretically.

Sasha: ...you have to get that first job.

Peter: Right.

Sasha: That first job is not being CEO of the world's largest bank, it's being a teller and then working your way up to a manager, and then working your way up to district manager, and then working your way up and learning about operations and credit management and all of the different aspects of a business and showing success.

But if we're in a society that says we are not going to let 56% of our country take that first job even if it's not a high paying job, that's effectively what we're saying today. And so we need to change the dialogue and we believe that we're in a position and you, with your podcast and your platform, to be able to help shift that narrative and show people that financial inclusion is something that's solvable with technology, with data, with education and with a regulatory framework that encourages it.

Peter: Right, right. I've been preaching that as well, I feel like the promise of fintech isn't to save people $100 a month on their student loan or whatever it is, the promise which...I'm not saying that's not a noble cause, it is, that does help a vast number of people, but the real promise, I always say is to really use the technology to expand access and bring people who have been unbanked or underbanked into the system. I'm not going to rest until we've made inroads there and I feel like we've still got a lot to go.

Anyway, we're almost out of time, but there's a couple of more questions I really want to get to and firstly, you look around your space and obviously you've got the storefront lenders, the

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pawn shops and the payday lenders that are still in existence somehow. When you look around the space that you operate in...obviously there are some unscrupulous players, there are companies that are out there that aren't as mission-driven as what you guys are, but what would you like to see? Maybe how are you different from the unscrupulous players and what would you like to see to sort of rout them all out or to make it impossible for them to do business?

Sasha: Well I mean, if you have an extra billion or $2 billion, I'm sure we can figure out something to do with it. (Peter laughs). There is I think equal culpability from the banking sector down to the payday sector of creating products and structures or maintaining legacy products and structures that are set up where the lender or the bank win when the customer loses.

The three most notable talked about examples are endless overdraft fees and reordering transactions to optimize for banks to collect as much overdraft fees as possible; reverse amortization loans with no income verification that put us into the Great Recession; payday lenders where the marketed convenience of a rollover creates an endless cycle of debt for people. So we all have culpability as a financial sector to the problems that we're facing today. So your question is how do we solve it.

I think what we're seeing is what fintech is really driving, the thing I'm most excited about, is they're driving new experiences that are much more transparent than ever before and customers recognize and value that and you see fintech overtaking banking as the largest private lender/personal lender around and you're going to start to see that in every industry that people that are solely focused on creating amazing experiences are going to win because customers now are having choices.

Peter: Right.

Sasha: I think, two, the regulatory environment of rethinking some of this old regulation is a discussion we haven't had in a long time. We've been adding so much regulation that I think we're now talking about what regulation makes sense and what doesn't. We haven't had that dialogue in a long time.

And third is, I think we're rethinking the notion of what a bank means and so if there can be a fintech charter or we can start reissuing new bank charters and ILCs, you're going to start to see the word bank can have a more broad meaning than I think it does when you think about the brick and mortar place on your corner that has 365 mediocre versions of everything that you want.

Peter: (laughs) Okay. So I want to move over to the other side of the balance sheet and I'd like to get an idea about, you know, how you're funding your loans today, the bank partners you're working with. Where's the capital coming from today for you to fund all of your loans?

Sasha: Yeah, we have warehouse lines in place on the cards and separately on the loans businesses and so those are there. Our credit performance has been, for six years, just incredibly steady, we invest very heavily on the credit side. We have not had a shortage of

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people saying, can we fund your portfolio, can we fund your portfolio so that side there, there's been a lot of structure and a lot of interest and we're very well funded there.

Peter: Right. Okay, finally then, what are you working on today that you think is most exciting for LendUp?

Sasha: The thing that I'm most excited about is we're really at an exciting stage of the company right now. We have proven that we can build industry defining products, both internally and as rated by the customer.

The second thing is we've proven that this can be profitable and I think we've earned enough trust now in the market to show that we're really committed to building the consumer. So if you have product market fit and profit market fit, it starts to unlock some really exciting conversations.

So we have nothing to announce at this moment, but we promise we will let you and your listeners know that we some major partnerships that are in the works right now that I think will rethink how both the private market and the banking industry think about becoming relevant to their customer base.

Peter: Okay, well I look forward to hearing about that. Anyway, it's always a pleasure talking with you, Sasha, thanks for coming on the show today.

Sasha: You as well Peter, good chat.

Peter: Okay, see you.

Sasha: Bye.

Peter: You know, I'm reminded of something that Scott Sanborn said sometime ago, the CEO of LendingClub, he said that credit is just a data problem. What companies like LendUp are doing, they are solving the data problem for a very difficult population to serve and they are doing this in a way that is really making a win-win environment. They are proving that you can do this at scale and actually build a profitable business.

So I feel like, as I said before, fintech needs to serve more than just prime consumers, it needs to serve the entire gamut, from the new immigrant to the person right out of college to the people who are really just entering the credit system for the first time and it needs to serve all of those people equally and I feel like we are nowhere near that now. I hope in the next few years we will make progress; I feel like progress is slowly being made, but I'd like to see it move faster as would Sasha, I'm sure.

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

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