PODCAST TRANSCRIPTION SESSION NO. 185 / JEFFREY MEILER

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Peter Renton: Today on the show, I'm delighted to welcome Jeffrey Meiler, he is the CEO and Founder of Marlette Funding, also known these days as Best Egg which is their consumer facing brand. So I wanted to get Jeffrey on the show because we've never had him on before and Marlette has become one of the true leaders in the online lending space.

As you'll see in this episode, they've really done things that no other platform has done and they have built themselves a very strong brand in the industry. So we talk about their loan performance, we talk about profitability, we talk about Jeffrey's perspective on the entire online lending space, we talk about the investor side of the business and what's in store for 2019. It was a fascinating interview, hope you enjoy the show.

Welcome to the podcast, Jeffrey.

Jeffrey Meiler: Hey, thank you, Peter.

Peter: So I like to get these things started by giving the listeners a little bit of background and some context. You've had a pretty interesting career to date, Jeffrey, so why don't you go through and give us some of the highlights.

Jeffrey: Sure, I'd be happy to. My background, and importantly the background of my colleagues at Marlette, is a bit unique in the online lending space. Myself, my leadership team and actually the overwhelming majority of the folks at Marlette have backgrounds in consumer finance and banking so in the context of the online lending industry, we're a bit more fin than tech-weighted from an experience standpoint.

Now I specifically have 25 years of consumer finance and banking experience with seven years actually spent in the UK and Europe, but the majority of the time in the US with the focus really on unsecured consumer lending. In fact, as you may know, many of us at Marlette worked together in the US credit card industry. If you look at my leadership team, six of the nine people have known and worked with me for over 14 years. If you look at the broader strategy staff, about 60% of us have worked together previously.

Peter: Wow!

Jeffrey: Yeah, it's pretty unique.

Peter: So was that primarily at Barclaycard or is that what the majority...

Jeffrey: Yes, it is. Let me give you more color to that. What is really unique is, yes, it's at one issuer and what is special and has been unique for us is the nature of our shared experience. We collectively, had the experience of building a US card business from a billion dollars to $12 billion from a portfolio standpoint in five years, making it a top ten card issuer and the team, the team that is at Marlette, built the prospect database, the credit models, the value propositions that enabled the success of that credit card business. As you can imagine, that was great context for what we've done at Marlette.

Peter: Yeah, right, for sure, for sure. So then let's go back just a few years to the founding of Marlette. What was it that you saw and why did you decide to start an online lender?

Jeffrey: Hey, that's a great question. We incorporated in August of 2013 and then launched in the middle of March in 2014 and there were really two things that really informed our thinking about starting Marlette. The first was we clearly saw that consumers were not being served and appreciated the size of the total addressable market. That was the first thing.

The second thing was we saw an opportunity to take a different approach than the current incumbents, more fin than tech, more focus on credit and capital markets than on growth in isolation, better alignment and attention across the capital stack and more focus on building a resilient personal loan business that reflected our recession tested team's experience in the credit card industry.

Peter: Okay, okay. So then before we move on, I've got a strange question for you. You know, I noticed that your email address changed recently from Marlette Funding to bestegg.com. What is your company name, what are you going by these days?

Jeffrey: Great question. The company is still named Marlette Funding, but our lending platform and what consumers recognize is Best Egg and we found, to your good point, that many of our corporate relationships were not connecting these two brands. So over the past two years, we've made a concerted effort to increase awareness and the connection between the two brands and that's, hence, why we made the email addy change to try to connect the two brands so that there isn't that confusion out there, but a fair question.

Peter: So the Marlette brand isn't going away, you're just sort of aligning more with the Best Egg brand?

Jeffrey: I would preclude us embracing more and more, as time went on, the Best Egg brand.

Peter: Okay, where did that name come from? What's the origin of Best Egg?

Jeffrey: Sure, sure. So the origin was really part and parcel of the thinking about the customer that we wanted to serve and when we really analyzed who we were going to be working with, who we were going to be helping here, it was typically a consumer that is 46 years old, is an individual that has liabilities that exceed assets and they're carrying, typically, $15,000 plus in credit card debt and they're looking to make a change. The theme for a lot of these people as we talk to these consumers was the desire, the aspiration to have a nest egg. So it was a bit of a play on words, well, you know, you don't have a nest egg, get a loan from Best Egg...

Peter: Right.

Jeffrey: ...and start on your path.

Peter: Got it, that makes sense, that makes sense. So then you've talked a little but about this, but I want to delve into it a little bit more. Like the background at Barclaycard, you know, Barclaycard obviously...Barclays is a very well established, dare I say old, British bank that goes back centuries, how'd your time there influence what you've been doing over the last...particularly when it comes to how you sort of built a successful company. How have your learnings at Barclaycard helped you do that?

Jeffrey: I think that's a great question and to your point, Barclays is a couple hundred year old institution and to have folks come from there and go and do a startup, it isn't necessarily the logical expectation, but the thing that was unique was Barclays had purchased a startup in the US, something called Juniper, and that was the entity that I referenced earlier that the team grew rapidly. So really Marlette is leveraging that specific experience.

It also, though from a 200-year old bank perspective, I think there are some things we borrowed from there also. I think the compliance discipline, the credit practices were things that we took from Barclays and embedded in Marlette very early on and both of those specific things had a level of maturity that exceeded the maturity of the company itself.

Peter: Right, got it, okay. So then now when you look at the competitive landscape today and you see there's more personal loan offerings for consumers than there probably has ever been, certainly in the last couple of decades, I'm just curious about when you're looking at the landscape and you've obviously got all of the other online lenders today, you've got banks coming in as well, how are you differentiating Best Egg from the other offerings that are out there?

Jeffrey: Hey, that's a super relevant question. As you know, Peter, the most successful players in the online lending space are those that deliver a fast frictionless customer experience and we spend an inordinate amount of time, energy in focusing on that.

In the context of 2018 specifically, we introduced new funnels from a customer standpoint, one that is focused on a better experience for those people using a desktop and one is focused specifically on those customers that are using a mobile device. Those efforts in 2018 resulted in us having a net promoter score of 68, an A+ rating with the Better Business Bureau and a 9.5 out of 10 TrustScore from TrustPilot. I think that that's going to be the key, that focus on the customer is going to be the key to differentiate and win in this space and I think that segmentation and personalization is something that, specifically in 2019, we're going to make a lot of strides in.

Peter: Okay, we'll delve into that a little bit more in just a bit, but I want to talk a little bit about your 2018 and the scale you guys are at. I know you just recently crossed another milestone so tell us, how big is your loan book today?

Jeffrey: So to your point about milestones, as we came to the close of 2018, we crossed the $7 billion mark, so in less than five years we have originated $7 billion. As far as the outstanding book, the outstanding portfolio is about half of the total originations so circa $3.5 billion.

Peter: Okay, so then when you look back at 2018 then, we are recording this in the middle of January, so you might not have closed out your books yet, but I'm sure you've got a very good idea of how it went. Tell us a little bit about...I'm interested in profitability, in growth and that kind of thing.

Jeffrey: Happy to share and to your point it’s unaudited financial results at this point, but happy to share those. So 2018, is the second consecutive year that the company has achieved GAAP profit in the double digit millions and year-on-year we had about a 60% increase in profits. Q4 specifically, Q4 of 2018 marked the seventh straight quarter that net income has been positive on a GAAP basis. Now turning to loan originations, 2018 was robust for us also, originations increased 27% year-on-year.

Peter: Okay, okay, that's a pretty impressive performance. I want to get back to the profitability, it’s great you’ve got seven consecutive quarters of profitability. You know, when we look at many other companies in this space and it's definitely been a knock on the space for the last few years where there has been a lot of venture capital money being thrown at the online lending space and profitability has proven elusive for many players.

Obviously we don't have publicly available books for everybody, but there are for a few players so I'm curious, what's your take on that? Obviously, you monitor your competition closely, I'm sure, why is it so hard for many companies to make money?

Jeffrey: Hey, that's another good question. I think new business paradigms that are challenging well entrenched incumbents, in this case the banks, always struggle to be profitable. Now, specifically, if we look at the online lending industry, I think that near term profitability is also linked to where you are positioned on the fintech continuum.

Before 2016, I think it was generally more acceptable for the incumbents to pursue growth versus profitability in isolation. This is more commonly accepted in the tech space. For example, how many years did Amazon lose money.

Peter: Right.

Jeffrey: IPO was in 1997 and in 2009, they were still in the red. What happens in our industry is in 2016, it became abundantly clear that tech was important in delivering a frictionless customer experience, but credit performance, access to capital and profitability were more important and the pendulum had swung to fin versus tech.

Peter: Right, right.

Jeffrey: And I think those players that were more skewed to fin, like Marlette, had an easier time migrating to profitability and acclimating to the new consensus sentiment about the nature of the online lending industry.

Peter: So is that something that you consciously made the decision of? Obviously, we know 2016 was a difficult year for many companies in this space. I wouldn't say funding dried up completely, but it certainly was a lot more difficult. So was that a conscious decision back then to say, right, we need to batten down the hatches and focus on profitability?

Jeffrey: Yes I would say, in general, we were always skewed, from an orientation standpoint, to be more fin than tech, but post 2016, it became clear that we couldn't wait to get to profitability and at the end of the first quarter of 2017, the last quarter that we lost money, we narrowed the commercial agenda and became a lot more focused on profitability.

Peter: Got it, okay. So let's talk a little bit about credit performance. You've already mentioned that several times and I want to know what color you can give us on the credit performance of your loan book.

Jeffrey: So I, as you would expect, would say we have really a unique performance from a credit perspective. We have been really, really consistent in what we've delivered for investors and for the company. I really think it comes down to this orientation that is more fin-grounded than tech-grounded and let me explain what I mean by that.

For us, on a quarterly basis, job one was always to originate loans that would serve us well and our investors through a recession and we specifically, on a quarterly basis, target a specific loss coverage ratio and because we target that, we have more predictable and consistent results. In contrast, in contrast, others in the space, especially pre-2017, thought of themselves as a marketplace.

Job number one was balancing supply and demand for their loans. When demand for loans was high, interest rates to consumers went down and underwriting softened. That approach leads to more volatility and less consistency and I think that, in a large part, that's been the biggest difference. It starts philosophically for how we see the nature of the business that we're in.

Peter: Yeah, that makes sense, that makes sense. So I'm curious about how you view...when you look at your business overall, you have really maintained a focus on one product to date, the personal loan, and you've seen others who have branched out into different verticals or just sort of adjacent products, shall we say, and I'm curious about how you view that. Are you comfortable being a monoline business for the foreseeable future, or how do you think about adding a new product vertical to your business?

Jeffrey: Yeah, another great question. Yeah, to date we have been totally focused on building a profitable resilient personal loan business. Having accomplished that though, in 2019 we will start to take steps to broaden our product pallet and leverage the platform and the infrastructure that we have built. As you would expect, the first steps are likely, you know, close cousins to the personal loan business, but see over the medium term that we'll go further afield from that, but absolutely, Peter, I think that the time has come for Marlette to diversify.

Peter: Well you know you guys seem to have a lot of experience in the credit card business. I wouldn't guess, of course, what your next product would be, but certainly I know that you guys must have...that would be a logical step.

Jeffrey: I can't comment, but to your point we love credit cards.

Peter: I know, I know. Right, okay. Anyway, so it's interesting that you guys are based in Wilmington, Delaware. I don't know if there's any other fintech companies in Wilmington, Delaware, there certainly aren't many. I don't know of any other in the online lending business. Now Delaware is obviously a very...a lot of places have their official headquarters there for various reasons that the government has set up…the state government of Delaware has really promoted that, but I'm curious about...do you think that Wilmington, Delaware, being located there is an advantage or a disadvantage to you when it comes to attracting talent to Marlette?

Jeffrey: We think it's a huge advantage to be in Wilmington and to your point, I don't know if people broadly appreciate that this greater Wilmington area has the greatest number of people probably in the United States with unsecured credit experience and being in the middle of that has been super helpful for us in scaling the business. I referenced earlier that, you know, 60% of the strategy staff worked with us previously. Even outside of that, the people we've hired have experience in unsecured credit.

Now having said that, we are a fintech player and believe in hiring the right and best people and have tools that enable us to have people work remotely also, if that's something that is important to them, but being in Wilmington has really enabled us to flourish.

Peter: Interesting, interesting. I imagine that all of the unsecured credit people is because the credit card companies set up shop there, is that one of the primary reasons?

Jeffrey: Yes, in Wilmington there's essentially two industries, pharma and credit cards, financial services and to your point, a number of players are headquartered in the area.

Peter: Right, right, for sure. Okay, so I want to switch to the other side of your business, the investor side, and I'm curious about the investor mix today and what kinds of investors are buying loans and is that changing at all?

Jeffrey: Yes, that has changed greatly over the five year period that we've been in business. In the very early days, we were funded 100% from hedge fund money, that's not the case today. I wouldn't quote specific mix percentages, but would say that as we've built a track record and shown consistency, we've been successful in migrating, over time, to buyers, loan buyers, whole loan buyers, with lower and lower costs of capital and that has been really helpful and fruitful and has been, you know, a part of our migration to profitability.

Peter: Right, that makes sense. So then on that, we did have a couple of years ago, we had your Head of Capital Markets, Karan and Josh Tonderys on the show and we talked quite a lot about securitization and I won't go into too much depth, but maybe...I will link to that show in the show notes, but you have become quite a prolific securitization issuer, your deals seem to attract a lot of attention so maybe you could just give us an update on that and do you plan to sort of keep this similar rhythm in 2019 that you've established?

Jeffrey: Yeah Karan, who you referenced, has done a great job in developing our securitization program and our deals have been well received. In 2018 specifically, we did $1.7 billion in transactions bringing the total Marlette issuance to date to $2.9 billion. Furthermore, in 2018, a number of the tranches from 2016, 2017 and 2018 received rating upgrades from Kroll. As we look to 2019, market conditions permitting, we'll continue to be a serial issuer of securitizations.

Peter: Right, right, okay. We're running out of time, but last question on 2019, the future, you've already touched on some of these things, but I'm curious about what you're excited about when you look ahead to this year. What are some of the things that you want to accomplish?

Jeffrey: To your point, Peter, we've touched on some of this, but as we enter 2019, it's really going to be about capitalizing on the robust and balanced performance that sets the stage for continued growth and product expansion. As you would expect, we closely monitor all conditions that may impact the business and are prepared to recalibrate, if necessary, but right now, right now, we remain optimistic that we can continue to expand our business at pace, both within personal loans and outside of personal loans.

Peter: Okay, well on that note, we will leave it there. I really appreciate you coming on the show today, Jeffrey, and best of luck to you in 2019.

Jaffrey: Hey, thank you, Peter.

Peter: Okay, see you.

You know, the online lending industry is certainly maturing and I think Jeffrey sort of brings on some of those points there where, you know, they're a profitable business, seven quarters in a row, I think that's extremely important. Gone are the days if you look back to 2015 when money was just being thrown around, anyone could raise capital and there was certainly no focus on profitability or very little focus on profitability back then.

Today, this feels like a different time, 2019, you know, if you're not profitable, or at least have a really easy or strong pathway to profitability, you are in serious trouble. I think companies like Marlette are showing the way where you can make money in this industry, even as a monoline company. They have proven that it's certainly doable and I think the rest of the industry needs to take note of that. I'd like to think that by the end of 2019, the vast majority of companies in the industry will be profitable.

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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