The Politics Of Online Lending

by Steve Brown

These days the Internet is revolutionizing all aspects of our lives including the way we dress, eat, drive and now maybe even the way we vote. Consider curmudgeon Bernie Sanders who is running on the democratic ticket as a "socialist." To raise money, he is using the Internet to capture small donations. The average contribution is a reportedly modest $31 per sympathizer, but more than 400,000 small donors have kept his machine running. The online site gives the senator a way to raise money so he can press on with public events in crucial states.

This inexpensive yet efficient collection tool is not restricted to politics, however. It also finds its way into banking in the form of online lending. While we have talked about this subject before, we do so again to point out how formidable this group of competitors will eventually be to bankers.

On paper, the proposal is attractive after all. It doesn't require any more outdated branches, there is no waiting and high technology algorithms analyze a borrower's financial picture so loans can be approved quickly. Small business may have to wait for a few days, due to the more complex state of their finances, but the answer seems quick when compared to a more rigorous approach used in the regulated world of banking.

This must be the case because when you calculate the total costs for one year and then convert it to an annualized rate you find small business borrowing rates range from 8% to as high as 99%. That is wild when you consider that just by doing a bit more paperwork a small business can borrow for as little as 4% or so.

What is interesting is that many of these platforms do not actually lend money. Instead, they are merely software platforms that connect borrowers with investors. Through those platforms, institutional investors (hedge funds and other large players) reportedly provide about 80% of funding while smaller investors provide the remainder.

The whole process is structured to be simple and while it makes an end run on the bank lending process it also needs the banking system at this point to make the payments. For example, the process typically goes that someone applies online and clicks through to electronically sign loan documents, those loans are then automatically shown to investors who then fund the loans. Once that is done the bank account is linked to for direct deposit and then on a monthly or even weekly basis funds are debited out of the account to make payments on the loan. From end to end consumer borrowers can get loans in as little as 1 day to as many as 3. For small business loans things run about 10 days all the way through the process.

There is still much to transpire in the online lending platform arena as regulators now ramp up to get involved. No one is too sure where it will all end up, but certainly the streamlined approach of online lending is here to stay. As such, community bankers will have to adapt--particularly when competing for smaller loans.

There are plenty of big name players moving around the online lending space, but that doesn't mean this part of the business is anywhere near being done. Certainly, some of the smaller loans of $1,000 could be funded by smaller contributors, perhaps just like Bernie is doing with his political campaign.

BANK NEWS

M&A Activity

Entegra Bank ($984mm, NC) will acquire OldTown Bank ($113mm, NC) for about $13.5mm in cash or roughly 1.16x tangible book.

Google Compare

Google has announced it will allow borrowers to comparison shop for the best mortgage deal through a partnership it has formed with Zillow and LendingTree. Borrowers put in their zip code, price of home, down payment and how long they expect to live in the house and Google then searches and returns with information on up to 300 mortgages from 75+ lenders.

Job Cuts

HSBC is cutting 2,000 jobs in its commercial bank unit over the next 3Ys as it seeks to reduce costs.

Small Business

A survey of small business owners by the NFIB finds 53% say they have hired or tried to hire new staff but 45% say they could not hire staff due to a lack of qualified applicants.

Unintended Consequence

The RMA reports 83% of community bank member survey respondents say they have seen rules and regulations meant for the largest banks trickling down and impacting them.

Board Materials

A PwC survey of corporate directors finds directors "somewhat" or "very much" wish their materials: better highlighted risks related to the issue being discussed (69%), included more management insights (67%), were shorter and more summarized (51%), were provided with more lead time (46%), included fewer acronyms and industry jargon (40%), and were better scrutinized to remove information that is no longer relevant (35%).

Millennial Living

A survey by Bank of America finds millennials say they choose where they want to live based on the following: desire to be near family (42%), work, job, or career opportunities (41%), where they grew up (28%), financial reasons (28%) and relationship, partner or spouse (24%).

Growth Opportunity

A Bank Director survey of where bankers see their greatest loan growth opportunities finds: commercial real estate (85%), C&I (56%), residential mortgages (45%), construction (39%), SBA (24%) and other consumer loans (13%).

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