Fact Versus Fiction: FinTech Lenders

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Vice President, Consumer Lending
TransUnion
In this session, we’ll review:

• An overview of the personal loan market

• FinTech consumer profile
  o How different are the demographics and geographical distribution of FinTech consumers?
  o How does the debt wallet of FinTech consumers compare to those of other consumers?

• FinTech lender strategy and performance
  o How are FinTechs different than other financial institutions in terms of origination strategy?
  o Do FinTech loans perform differently than other financial institution loans?
  o Can we measure returns on FinTech loan performance compared to other financial institutions?
An overview of the personal loan market
Personal loan total balances have grown by double digits annually since 2014, driven in part by increasing average balances.
We continue to see growth in originations and consumers with a personal loan

Quarterly unsecured personal loan originations and consumers with a balance

Originations (M)

# of consumers with a balance (M)

Q1 2018 YOY: 24.5%

Source: TransUnion consumer credit database
Personal loan adoption is low relative to card and auto loans

Share of population segments with open personal loans on file as of Q2 2018

<table>
<thead>
<tr>
<th>VantageScore® 3.0 risk ranges</th>
<th>% of total population in each band</th>
</tr>
</thead>
<tbody>
<tr>
<td>Subprime (300–600)</td>
<td>6%</td>
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<tr>
<td>Near prime (601–660)</td>
<td>30%</td>
</tr>
<tr>
<td>Prime (661–720)</td>
<td>62%</td>
</tr>
<tr>
<td>Prime plus (721–780)</td>
<td>6%</td>
</tr>
<tr>
<td>Super prime (781–850)</td>
<td>6%</td>
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</tbody>
</table>

Source: TransUnion consumer credit database
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FinTechs have grown share rapidly in the personal loan industry

Personal loan balances ($) originated by lender type (Year-end)

Source: TransUnion consumer credit database
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But FinTech performance has led to some concern — and some lively debate — in the market.

New growth plan for online lenders: layoffs
Source: Wall Street Journal

The FinTech threat: Part bubble, part trouble for big banks
Source: The Globe and Mail

As trouble piles up, online lenders pull back
Source: Los Angeles Times

Investment in marketplace lenders has crashed since the start of 2016
Source: Bloomberg

Marketplace lending may threaten U.S. financial stability
Source: Reuters
Growth and share shift in the personal loan market have led to many questions that we’ll address in this session.

<table>
<thead>
<tr>
<th>Dimensions</th>
<th>Business questions: FinTechs compared to other personal loan lenders</th>
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</thead>
</table>
| Consumer demographics | • How are FinTech consumers different?  
                         (Age, number of trades, wallet profile, Aggregate Excess Payment) |
| Origination strategy | • How are FinTechs different in terms of origination strategy?  
                         (Risk, term, amount, and pricing) |
| Credit performance  | • Do FinTech loans perform differently? |
| Risk returns        | • How do FinTech loans measure in terms of risk-adjusted returns? |
Consumer demographics
We analyzed over 60 million personal loans originated in 2014, 2015, 2016, 2017 and 2018Q1

Performance metrics at $t$

- Consumer profile:
  - Origination VantageScore®
  - 3.0 score, age, number of trades, wallet profile, Aggregate Excess Payment
- Loan profile: Amount originated, estimated interest rate

Performance metrics between $t$ to $t + 12$ months

- 60+ DPD (balance-level)
- Monthly ending balances
FinTech consumers are similar to those of other lenders in their age groups

Source: TransUnion consumer credit database

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FinTechs and banks have similar proportions of thin-file customers

Number of open trades on file at personal loan origination

<table>
<thead>
<tr>
<th>Lender type</th>
<th>0-2</th>
<th>3-5</th>
<th>6-10</th>
<th>10+</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank</td>
<td>13%</td>
<td>18%</td>
<td>32%</td>
<td>14%</td>
</tr>
<tr>
<td>Credit union</td>
<td></td>
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<td></td>
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<tr>
<td>Traditional finance company</td>
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<tr>
<td>FinTech</td>
<td></td>
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</table>

Source: TransUnion consumer credit database

Note: personal originations 2014-2018 Q1
FinTech consumers are as credit-active as bank and credit union consumers

Share of consumers with each credit product at personal loan origination

Source: TransUnion consumer credit database

Note: personal originations 2014-2018 Q1
TransUnion’s Aggregate Excess Payment algorithm exhibits a shift in excess payments being made, due to multiple drivers.

<table>
<thead>
<tr>
<th>Risk tier</th>
<th>2016Q2</th>
<th>2017Q2</th>
<th>2018Q2</th>
<th>2018 YOY growth</th>
</tr>
</thead>
<tbody>
<tr>
<td>Super prime</td>
<td>$1,846</td>
<td>$1,891</td>
<td>$1,931</td>
<td>2.1%</td>
</tr>
<tr>
<td>Prime plus</td>
<td>$1,645</td>
<td>$1,657</td>
<td>$1,641</td>
<td>-1.0%</td>
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<tr>
<td>Prime</td>
<td>$1,178</td>
<td>$1,198</td>
<td>$1,182</td>
<td>-1.3%</td>
</tr>
<tr>
<td>Near prime</td>
<td>$762</td>
<td>$776</td>
<td>$754</td>
<td>-2.8%</td>
</tr>
<tr>
<td>Subprime</td>
<td>$167</td>
<td>$161</td>
<td>$160</td>
<td>-0.6%</td>
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</tbody>
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VantageScore® 3.0 risk ranges
Subprime = 300–600; Near prime = 601–660; Prime = 661–720; Prime plus = 721–780; Super prime = 781-850

Source: TransUnion consumer credit database
Prime and above FinTech customers have the highest levels of Aggregate Excess Payment at loan origination

Median 1-year AEP at personal loan origination

- **Subprime**
- **Near prime**
- **Prime**
- **Prime plus**
- **Super prime**

**Credit product**

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<th>Bank</th>
<th>Credit union</th>
<th>Traditional finance company</th>
<th>FinTech</th>
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<tr>
<td>Subprime</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
</tr>
<tr>
<td>Near prime</td>
<td>$200</td>
<td>$400</td>
<td>$600</td>
<td>$800</td>
</tr>
<tr>
<td>Prime</td>
<td>$400</td>
<td>$600</td>
<td>$800</td>
<td>$1,000</td>
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<td>Prime plus</td>
<td>$600</td>
<td>$800</td>
<td>$1,000</td>
<td>$1,200</td>
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Source: TransUnion consumer credit database

Note: personal originations 2014-2018 Q1
Origination strategy
FinTech focus is gradually shifting towards lower risk consumers

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Source: TransUnion consumer credit database
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FinTechs issue the largest loans across the risk spectrum above 570

Average new loan amount (Q1 2014 – Q1 2018 originations)

- Subprime
- Near prime
- Prime
- Prime plus
- Super prime

Source: TransUnion consumer credit database

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FinTechs have more risk appetite than banks, but are more conservative than traditional finance companies.
FinTechs have the most robust, risk-based pricing

![Graph showing originated implied interest rate* (Q1 2014 – Q1 2018 originations)]

VantageScore® 3.0 risk ranges
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*Interest rate is calculated using originating balance, term, and payment due at origination;

Source: TransUnion consumer credit database

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Credit performance
FinTech loans experience higher delinquencies, specifically within lower credit tiers

60+ DPD balance-level delinquency rate at 12 MOB (Q1 2014 – Q2 2017 originations)

Source: TransUnion consumer credit database

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Risk returns
We estimated lenders’ risk-return measure using a straightforward approach

We estimated lenders’ risk-return measure using a straightforward approach

Annual interest income earned

Subtract

60+ DPD balances during 12 MOB (current status not observed since last DQ)

At t+12 months
Interest income earned = $10.8M

First 12 MOB
60+ DPD Balances = $5.1M

Yr. 1 Interest Income Earned Net of Delinquent Balances = $10.8M − $5.1M = $5.7M
Yr. 1 Risk-Return Measure = $5.7M/$100M = 5.7%

Note:
Costs associated with funding, branch, operating expenses, collections, and technology not included

For illustration purposes only

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FinTechs generate effective portfolio risk-return ratios that exceed those of banks and credit unions

Year one on book effective portfolio risk-return

Bank: 6.8%
Credit union: 6.2%
Traditional finance company: 8.9%
FinTech: 8.5%

Source: TransUnion consumer credit database
After an initial ramp-up, FinTech risk-return performance has stabilized

Year one on book effective portfolio risk-return for FinTechs

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Thank you!

Questions? Contact me at:

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