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Lending Startups Hone Their Focus

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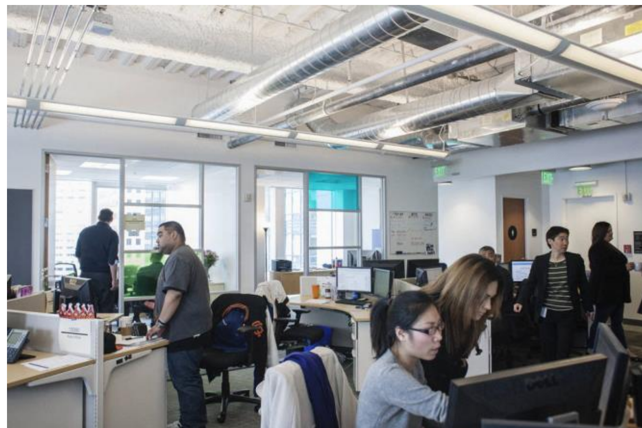

Prosper Marketplace's San Francisco offices. The strength of large-scale fintech startups, such as Prosper and others, is forcing newcomers to the sector to target more-specific lending niches. *PHOTO: TALIA HERMAN FOR THE WALL STREET JOURNAL*

By **TELIS DEMOS**
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Silicon Valley once threw money at startups that aimed to disrupt broad swaths of finance. Now it is rewarding those that have sharpened their focus.

While overall venture funding into lending startups is slowing, some platforms still are raising money by taking aim at narrower or less-traditional borrowing niches than the first generation of financial-technology firms.

Faced with a glut of online lenders and cooling interest from investors in some loans, a newer crop of fintech startups is focusing on areas including loans for real-estate projects, people with poor credit ratings, car buyers and, at the extreme, people getting married.

Venture funding for U.S. lending startups dropped to $298 million in the first quarter from $832 million in the last three months of 2015, according to Dow Jones VentureSource. The largest commitment in that shrinking pool was $150 million for Flurish Inc., whose LendUp platform focuses on borrowers with limited or poor credit history, according to VentureSource. Nine of the 11 fundraisings in U.S. lending were for earlier-stage companies, a change from recent quarters, when late-stage startups did more fundraisings.

"You have a lot of established players in areas like credit-card refinancing," said Joshua Jersey, chief executive of Promise Financial, which focuses on loans for weddings. "It's a strategic imperative of younger platforms to have a narrower focus."

Mr. Jersey is seeking financing to expand lending by his company, which teams up with roughly 100 wedding venues and other vendors to offer loans at the point of purchase.

The shift in emphasis highlights the difficulties of breaking into an online lending industry whose early entrants are well financed and becoming more deeply entrenched. It also shows that startups are wrestling with how to balance the technology industry's growth-at-all-costs mentality with the financial industry's need for prudence.

"There's an awful pressure to grow fast and scale up quickly coming from Silicon Valley," said Oren Bass, a former lawyer and Goldman Sachs Group Inc. executive who founded online lender Pave Inc. "That's not the game when it comes to finance. You live and die by your underwriting."

Pave started in 2012 seeking to create income-sharing agreements with borrowers. It narrowed its focus last year to consumers who lack credit history, such as expatriates or people just out of college. It tries to gauge borrowers' income potential by focusing on their education and skills, partnering with education firms like General Assembly, which teaches people skills like how to code or analyze data.

This month, it closed $8 million in an early-stage financing from Maxfield Capital, a venture-capital fund.

Startups, such as Pave, lean on complex data analysis to find borrowers who are a better credit risk than traditional indicators such as a FICO score would suggest.

Applied Data Finance, which last year secured backing of fund managers Colchis Capital Management and Victory Park Capital and raised additional equity funding, will start making loans available in 23 states this month. Its loans, under the brand Personify Financial, are aimed at borrowers with FICO scores between 550 and 650.

"We're focused on data science," said co-CEO Krishna Gopinathan,who previously founded Global Analytics, a technology firm that analyzes credit risk. "We think the risk of many borrowers is overstated by other lenders."

Lending startups that target a relatively wealthier customer base are facing several hurdles, including the presence of large-scale rivals such as LendingClub Corp., Prosper Marketplace Inc., and Social Finance Inc. that dominate market share in consumer lending.
Investors also have been concerned about the poor performance of initial public offerings for lenders including LendingClub, and how tighter access to capital to fund is threatening growth for those platforms.

The result has been a broader pullback from sector by venture capitalists. Venture fundraisings for U.S. lenders reached a record $1.3 billion in the third quarter last year, according to VentureSource.

Fund managers who were previously focused on consumer loans are looking to diversify.

"We want our portfolio to be very diverse, geographically and by borrower types," said Don Davis, portfolio manager at Prime Meridian Capital Management.

Prime Meridian manages over $140 million worth of assets invested in online consumer and small-business loans, and in February launched a fund that will invest in commercial, multifamily, and single-family home project loans.

Among the first loans it will be buying are from Sharestates, an online platform that funds commercial and residential projects, that this month said it partnered with institutions including Prime Meridian, which committed $45 million, and Colony American Finance, a lender to real-estate investors, to fund $300 million in new loans.

LendingHome, which lends to people and firms buying houses as investments, said that it completed a private securitization in March and also is launching a retail investment platform. It said it grew its originations sixfold in 2015 from the prior year, with $550 million funded since launching in 2014.