1Q15 Prepared Remarks

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This presentation includes certain non-GAAP financial measures. These non-GAAP financial measures are in addition to, and not a substitute for or superior to, financial measures prepared in accordance with GAAP. See the end of our press release filed today on Form 8-K reporting our 2015 first quarter results for a reconciliation of the non-GAAP measures used in these remarks to their most directly comparable GAAP measures.

James Samford – Head of Investor Relations

Good afternoon, and welcome to Lending Club's first quarter of 2015 earnings conference call. Joining me today to talk about our results are Renaud Laplanche, Founder and CEO; and Carrie Dolan, CFO.

Renaud Laplanche – Founder and Chief Executive Officer
Introduction
Thank you, James. I'd like to welcome everyone to our first quarter conference call.

This was another great quarter with 109% operating revenue growth year over year to $81 million and the momentum we are seeing gives us the confidence to raise both our revenue and EBITDA outlook for the year.

I'll begin today's call with a brief introduction of Lending Club; then I'll dig into our first quarter results and our progress towards our 2015 goals. I will then turn the call over to Carrie, who will go into more detail about our financial results, provide guidance for Q2, and update our full year outlook. At that point we'll turn the call over to the operator for your questions.
Let's get started.

LC Overview
Last quarter we provided a detailed overview of the business as it was our first quarter as a public company. Today, we do not plan to go as deep on how the business model works; however, I would like to touch on a few key areas before talking about the quarter.

- Lending Club is an online marketplace serving two constituents: borrowers and investors.
- Investors invest capital and assume credit risk, borrowers make monthly payments of principal and interest, and our marketplace underwrites, prices and services the loans.
- Our marketplace operates at a lower cost than the traditional banking system, and we pass on the cost savings to borrowers in the form of lower interest rates and investors in the form of attractive risk adjusted returns.
- Traditional banks have an operating expense ratio of 5% to 7%. The same measure at Lending Club, assuming no growth in originations, is roughly 2%.
- There are two sources of cost reduction: first there are costs that we do not incur at all such as the cost of building and maintaining a branch network and the cost of collecting and guaranteeing deposits, including capital reserve requirements and FDIC insurance. Instead of collecting deposits, we offer investments to investors, therefore not creating the same asset-liability mismatch as the traditional banking system.
- Then there are costs that we do incur but at lower amounts as we use our innovative business model and technology platform to drive costs down. Automation, continuous process and system improvements, and flow optimization give us the ability to constantly drive down our operating costs.
- We also use technology to deliver a better customer experience by automating tasks that our users would otherwise accomplish manually, constantly improving user flows and making our products available at the time and place that is most convenient to them.
- While we have continued to more than double originations and revenue year over year, we have been disciplined about growing only as fast as we believe is responsible and compatible with solid risk management and a great user experience that contribute to building and maintaining our brand and our reputation.

I would like now to take the opportunity of this call to share a couple data points about our borrowers and investors:

- We added a slide to the Investor Presentation this quarter that provides you more insight into our borrower demographics. In 2009, as you might expect, the early adopters were predominantly millennials. Over half of our borrowers were under the age of 35. Today, our borrowers are mainstream consumers looking for responsible and affordable credit, with over 75% of our borrower base being over the age of 35. We believe this expansion of our user base demonstrates the broad based appeal of our brand and our products.
- Another one-time disclosure relates to Net Promoter Scores, or NPS, a standardized measure of the likelihood of our borrowers to recommend our products. For the past four quarters the Net Promoter Score of our borrowers, as measured within 2 weeks after the loan has issued, has remained at record high levels with a reading of 78, showing a very high level of customer satisfaction.
- On the investor side, we saw a strong influx of individual investors in Q1, with self-directed retail investors representing 24% of investments, individual investors investing through a fund or managed account representing 51%, and institutional investors representing 25%. We believe the significant influx in individual investors' capital was caused in part by the increased brand awareness and credibility coming from our public offering in December and in part by seasonality as we typically see capital inflows from individual investors increasing as they reshuffle their portfolio around tax season.

Now let's dig into a few of the first quarter highlights.

Q1 Brief Highlights

Originations

Starting with originations…

- Loan originations in the first quarter increased 107% year over year to $1.64 billion, compared to $791 million in the same period last year. Nearly $9.3 billion in consumer and small business loans have now been issued since we launched eight years ago, including $5.2 billion just in the last year.

- Our marketplace remains neither supply nor demand constrained. We intend to stay disciplined about our growth rate with an emphasis on solid risk management and the continued improvement of the great user experience we have been delivering on both sides of the platform, as well as continuing to build on the trust and confidence we've established in the Lending Club brand. That being said, we always look for opportunities to safely and efficiently deliver faster growth. In the first quarter we had such an opportunity, with many marketing channels outperforming our expectations, both in terms of volume and cost efficiency.

Revenues

Operating revenue in the first quarter was $81 million, up 109% year over year.

Adjusted EBITDA

Adjusted EBITDA in the first quarter was $10.6 million or 13.1% of revenue. We are continuing to invest heavily in engineering and product development to continue to automate processes and build new products and features that continue to fuel our growth, increase our operating efficiency and deliver a great user experience. In particular, we plan to double our engineering headcount this year, which we expect to grow at twice the pace of our operations headcount.

Other Highlights from the Quarter

Now I'd like to discuss our progress towards our 2015 priorities and other highlights from the quarter.

- First, an update on our marketing channels

- In our core business we are continuing to activate our existing marketing channels at a higher level and continue to see a tremendous amount of growth opportunities, and at the same time we are establishing new channels that provide us with diversification and flexibility. While there are always small competitors entering the market, causing short-term inefficiency in some of the most visible channels that are most readily available to them, we have built sufficient diversification and have enough excess borrower demand that we can afford to lower our spend or entirely shut down any particular channel with very limited or no impact on our ability to deliver fast, efficient growth.
- Some of our new channels rely on partnerships to funnel borrower demand: such as the exclusive marketing agreement with Home Advisor ahead of the peak season for home improvements, an appropriate channel for our new double A grade super prime loan product. In small business lending we are now the exclusive non-SBA term loan provider for Sam's Club's millions of small business members, and we've signed a new exclusive partnership with Newtek, the nation's largest non-bank SBA lender, to offer non-SBA loans to Newtek's existing and prospective business clients. In many instances our dominant position in the industry puts us in a situation to secure exclusive or priority access to these channels.
- While any one of these partnerships might not have a material impact on our results this year, we believe that in aggregate they will continue to provide us with diverse, exclusive, cost-efficient distribution channels and will contribute to fueling our growth in the years to come.
- In the same spirit, we also entered into an important partnership with Citi to provide affordable credit to moderate and low income families across the country. While the amount of origination expected to come from this program is relatively small at $150 million, we believe this partnership is important insofar as it is the first time a top 5 US bank is relying on a marketplace model to originate loans. We believe this program will set a precedent that will be followed by other large US banks and will help further our goal of transforming the banking system into an online marketplace, with the banks becoming marketplace participants and benefiting from that transformation.
- As we mentioned last quarter, we continue to explore new channels including direct response radio for both consumer and small business loans in 4 small local test markets. We are also planning to start a small TV test later this month.

- In Education and Patient Finance,
  - We completed the rebranding of the elective medical financing part of Springstone as Lending Club Patient Solutions, released an entirely new loan application funnel, made progress toward building a sales team, and the issuing bank for these loans rolled out a new credit model.

- Let me now say a few words about the competitive environment:

  - We have launched co-branded programs with several members of the Banc Alliance network in the last few weeks and are seeing promising results. This relationship with Banc Alliance, and the relationships with Citi, Union Bank, and various other regional and community banks demonstrate the increasing desire by the industry to partner, rather than compete, with us. Partnering provides the banks with a means to efficiently and effectively leverage marketplace lending without the complexity, investments and risks of venturing on their own.

- We have also seen a number of small lending marketplaces emerging in the last few quarters. As I mentioned earlier, while there are many new platforms, most of them have deliberately chosen to focus on market segments the Lending Club platform is not currently active in, and therefore pose no immediate competitive threat. As to the small number of platforms that present a competing offering, we have seen some short term inefficiency in some of the most visible channels, but again with our channel diversification and excess borrower demand, we can lower our spend or shut down any particular channel with very limited or no impact on our ability to deliver fast, efficient growth. In addition, we believe that our platform's scale, and the amount of data gathered over the last 8 years, have enabled us to optimize processes, credit models, application funnels and loan pricing to a degree that any new competitor will find it difficult to rationally compete against.
- We have continued to expand our lead and grow faster - in absolute dollar amount of additional quarterly originations - than any other player in the space, every quarter over the last several years. Remarkably, we have even grown faster in percentage terms than the second largest platform over the last 2 quarters, with the Lending Club platform growing originations at 21% and 16% sequentially, quarter over quarter, and the second largest marketplace growing originations at 10% quarter over quarter in the same period, despite their growing off a considerably smaller base.

- Now turning to a different topic entirely: our new office space.
  - We secured a 10-year lease for an additional 112,000 square feet on Market Street next to our headquarters in San Francisco, comprising 8 floors to be delivered to us progressively from June this year through June 2017 to accommodate our planned headcount growth over the period.
  - We made a deliberate decision to add office space in San Francisco, rather than moving our operations to a lower-cost location. In contrast to a traditional call center environment, most of our operations staff is college educated. In addition to their operational role, they essentially function as "process engineers" who are constantly looking for ways to use technology to make processes more efficient and deliver a better customer experience. Their colocation and tight collaboration with product and engineering creates the best environment to efficiently and consistently create technology-enabled operations improvements, and to drive automation.

- This leads me to operations efficiency, the last topic I'd like to discuss today:
  - At Lending Club, we consider banking as an engineering problem: as a set of processes that can be optimized, simplified and made more efficient with better technology. Our investments in engineering, process improvements and task automation are generating significant gains in operational efficiency. These gains were particularly evident this quarter with our origination and servicing expense as percent of origination coming down significantly year over year and sequentially. The portion of the improvement due to efficiency gains, as measured by our headcount per loans issued and serviced, was close to 10% (or 8 bps of origination) year over year.

- Now let me turn the call over to Carrie to go into more detail about our financial results, our guidance for the second quarter, and an update on our full year outlook.

Carrie Dolan – Chief Financial officer

Intro

Thanks, Renaud. I'd also like to reiterate how pleased we are with the company's results this quarter.

I will first review our financial results and then review our second quarter and annual guidance before taking your questions.

All year over year comments are comparisons to the first quarter in the prior year.

Originations / Revenue

- As Renaud shared, total Originations in the first quarter grew to a record $1.64 billion, an increase of 107% compared to the same period last year.
- This origination growth drove equally strong revenue growth. Operating Revenue in the first quarter was $81.0 million, up 109% year over year.
- As a quick reminder, the majority of our revenue is earned in 2 ways:
  - First, transaction fees are earned up front when a loan is originated. These fees totaled $72.5 million, up 105% year over year and represented roughly 89% of operating revenues in the first quarter.
  - Second, servicing and management fees from investors are recurring in nature and are earned over the life of the investments. During the first quarter, these fees totaled $7.6 million, up 165% from last year.
- First quarter revenue performance came in ahead of our expectations as a result of several drivers.
  1. First, momentum picked up during the quarter with high borrower conversion rates, particularly in our standard program with broad-based benefit from the interest rate reductions that were made possible by the diversity and fast growth of our investor base.
  2. Given these favorable acquisition trends, that somewhat offset expected seasonal headwinds, we decided to take advantage of the positive momentum and activate more than we had communicated to you on our last call.
  3. In addition, our investor mix provided upside as we had a higher proportion of retail investors and a higher proportion of demand from investors paying marginally higher servicing fees. This investor mix change added approximately $1.2 million to revenues this quarter. The impact of this shows up in several revenue lines, including gain on sale, which is part of "other revenue".

  Revenue yield, which is operating revenue as a percent of originations, was 4.96%, up 7 basis points year over year. Higher mix of Servicing, Management fees and other revenues accounted for 11 bps of the increase, including 6 bps coming from collection fees, which were introduced in the 4th quarter of 2014. These increases were partially offset by a 4 basis point decline in transaction fees due to a higher mix of Small Business and Education and Patient Finance, including a greater mix of the recently launched true-no interest product, which has inherently lower revenue yield.

Expenses / Contribution Margin

- Now turning to expenses.
- We divide expenses into 2 major buckets: those that directly drive revenue and are part of our contribution margin, and those that support our infrastructure and long term growth.
- As we review expenses in this section, please note that these amounts exclude stock based compensation, depreciation, amortization, and acquisition-related expenses.
- The contribution margin expenses that directly generate revenue include: Sales and Marketing, and Origination and Servicing.

- Sales and Marketing expenses consist primarily of those related to borrower and investor acquisition, and are generally variable and track origination volume. They vary quarter to quarter with seasonality, channel mix, channel testing, and additional marketing efforts designed to support new product launches.
- In the first quarter, Sales and Marketing expenses were $33.4 million, up from $17.1 million a year ago. As a % of originations, sales and marketing expenses declined from 2.16% to 2.04% year over year. The improvement was due in part to channel efficiency and improved conversion rates, partially offset by the impact from expanding our acquisition channels for Small Business and Education and Patient Finance, which included the creation of a Patient Solutions sales force. Also during the quarter, we reclassified our personal loan sales team costs from the Origination and Servicing line into Sales and Marketing line. Excluding this reclassification, our sales and marketing expenses as a % of originations would have been 1.99%.
- Relative to the 4th quarter, sales and marketing expenses as a % of originations increased 24 bps. Excluding the reclassification, expenses increased 19 bps. On an adjusted basis, roughly half of the sequential quarter over quarter increase was driven by normal seasonal trends, while the other half was from the expansion of acquisition channels for Small Business and Education and Patient Finance.
- Our Origination and Servicing expense consists primarily of personnel related expenses for credit, collections, customer support, and payment processing teams and vendor costs associated with facilitating and servicing loans such as issuing bank, and credit agency fees.
- In the first quarter, Origination and Servicing expenses were $12.0 million, up from $7.0 million last year. As a % of originations, these expenses declined from 89 basis points to 73 basis points year over year. Excluding the 5 bps reclassification, Origination and Servicing expenses would have been 78 basis points.
- Both Sales and Marketing and Origination and Servicing expenses are netted against our operating revenue to derive contribution income and a Contribution Margin, which focuses on the efficiency of how we drive our revenue.
- On a dollar basis, our contribution income in the first quarter was $35.7 million, up 145% year over year.
- As a percent of operating revenues, our contribution margin was 44.1% in the first quarter, up 640 basis points from the prior year.
- As a % of originations, our contribution margin grew 34 basis points from 1.84% to 2.18% year over year. 7 basis points of the improvement was from higher revenue yield while the remaining 28 basis points came from improving expense efficiency.

Operating Expenses / EBITDA

- The second set of expenses that are outside of our contribution margin but are included in our EBITDA margin are costs that support our infrastructure and long term growth. Specifically, these are engineering and product development and other G&A costs.
- Engineering and product development expenses include personnel related costs along with non-capitalized hardware and software costs.
- We have maintained our aggressive pace of building our engineering team to develop new products that will fuel future growth, and build up scalability and security ahead of growth. As a result, engineering and product development expense increased to $8.2 million in the first quarter, up 95% year over year.
- As a % of operating revenues, Engineering and product development expenses were 10.1% in the first quarter of 2015, down slightly from 10.8% last year.
- Our engineering costs in the first quarter were a bit below plan as the bulk of our hiring occurred a little later in the quarter due in large part to new hires waiting to join until after bonus season.
- Other G&A includes personnel related expenses for our support organizations such as legal, finance, internal audit, accounting, risk management and human resources, along with facilities expense.

- Year over year, these expenses increased to $16.9 million in the first quarter, up 98% as we continue to invest aggressively in these support teams to further de-risk future growth.
- As a % of operating revenues, other G&A expenses were 20.8% in the first quarter of 2015, down from 22.0% last year.
- To derive our adjusted EBITDA, we subtract these operating expenses from our contribution income.
- In this quarter, adjusted EBITDA was $10.6 million or 13.1% of revenue compared to $1.9 million or 4.8% of revenue in the first quarter last year.
- Adjusted EBITDA came in ahead of our Q1 guidance range on higher revenues, which included the positive revenue benefit related to our investor mix and our marketing efficiency, both of which flowed directly into our EBITDA margins.

Adjusted EPS / GAAP

- Adjusted net income, which is GAAP net income excluding stock based compensation, depreciation, and acquisition related expenses, was $7.7 million or 2 cents per diluted share during the first quarter versus $875 thousand, or break-even per diluted share in the year-ago period.

- Finally, our GAAP net loss this quarter was $6.4 million compared to a loss of $7.3 million a year ago. The difference between GAAP and Adjusted net income is largely due to stock based comp which increased $4.6 million year over year to $11.6 million. Stock based compensation as a % of operating revenue declined from 18.2% last year to 14.3% this quarter.

Balance Sheet

- Now turning to the balance sheet.
- As we have discussed, in contrast to the traditional banking system, capital to invest in loans is provided from loan sales and securities issued to investors rather than from banking deposits. A key differentiator for our marketplace model is that, as a matter of business model, we do not assume credit risk or use our own balance sheet to invest in loans, and the loan sales and securities issued to investors perfectly match the term of the loans.
- When reviewing our balance sheet, you will see both the loans as an asset and the corresponding notes or certificates as the offsetting liability. The changes in value of these loans, notes and certificates generally offset one another and do not impact our equity.
- At the end of March, total balance sheet assets reached $4.3 billion. Of this, $3.2 billion is in loans, $874 million is in cash and cash equivalents and the remaining $223 million in other assets.
- Our servicing portfolio, which includes both loans on the balance sheet and sold loans, increased to $5.6 billion in the first quarter, up from $4.7 billion in the fourth quarter of 2014 and $2.8 billion in Q1 last year.

Guidance

With that, let me give you our thoughts about the second quarter and for fiscal year 2015.

- Given the strong momentum we continue to see on many fronts, we remain encouraged that our strategy of fast yet disciplined growth is paying off, and feel confident raising our full year revenue guidance.
- We expect operating revenue to be in the range of $90 to $92 million in the second quarter. We are raising our full year range to between $385 and $392 million, up from the range of $370 to $380 million provided during our fourth quarter earnings call.
- Our long run focus is to optimize our contribution and adjusted EBITDA margins, and eventually net income; however, over the short term horizon, we intend to continue to invest in new channels, product development, engineering, process automation, and the buildup of support and risk management functions.

- We expect Adjusted EBITDA in the range of $8.5 to $10.5 million in the second quarter. We are also raising the full year range to between $40 and $46 million, up from the prior full year guidance range of $33 to $42 million.

- I would like to provide some additional color on share count and our upcoming lockup expiration. We ended the first quarter with approximately 372 million shares, which adjusts to approximately 410 million shares on a fully diluted basis. While our 180 day lockup period ends on June 9th; current employees and directors will not be free to trade on this date as our second quarter earnings blackout period will be in effect at that time. As a result, we estimate today that approximately 150 million shares outstanding and covered by the lock-up will be eligible for sale at lockup expiration and approximately 182 million shares will become eligible for sale after our second quarter earnings release in early August in accordance with our standard blackout policy.