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“Alternative” Lending – Should Banks Jump in or Hold Off?

19 May 2016 By: Jacob Jegher

There has been a fair amount of controversy and press in recent weeks around alternative lending, and it raises questions about the viability of the space, the role of alternative providers and how/if banks should consider approaching the space. Throw in the threat of regulation and alternative lending can quickly become a scary space. However, banks are already exploring alternative lending and some have entered into partnerships with providers. What will this space look like moving forward? Should banks jump in or hold off?

Javelin has spent a fair bit of time researching this space, and we have just released a report on small business alternative lending. *‘Build, Buy, or Partner’ and Beyond: How Alternative Lending Is Reshaping Small Business Banking*, examines how alternative lenders are poised to disrupt and analyzes how/if banks can build, buy or partner in order to best serve their customers.

No matter what happens in the near-term and what the industry eventually looks like, **alternative lending is here to stay**. That’s because players like OnDeck, Kabbage, and many others have revealed significant gaps in how banks serve small business customers. The challenges faced by a few providers don’t represent the market opportunity. Alternative lenders have carved out a market based on smarter credit decisioning, speedier access to funds, a sleek user experience, and contextual marketing. Banks have taken notice, with a number of partnerships beginning to form that will define how the credit needs of this growing segment are met in the future. **Should we even be calling this “alternative” lending anymore?**

Despite banks still owning the largest share of the lending market, awareness and acceptance of alternative lending is growing. Small businesses that otherwise would not be considered creditworthy by banks are finding avenues for funding in the new alternative lending industry. This year, 7% of small businesses with credit needs are currently using alternative loan products. We expect this to double in the next year.

Whereas some banks have partnered in order to respond to small business needs, others are deciding to go at it on their own. Wells Fargo recently announced FastFlex, a $10,000 - $35,000 small business loan that can be funded within a single business day. This shows that more consideration is being placed on creating products in-house, as bankers weigh the benefits of a partnership—like speedier time to market—with the risks, which include reputational and cost considerations. Javelin believes that other banks will follow suit, in an attempt to compete with alternative providers and respond to the needs of small business customers. How banks chose to follow suit will depend on numerous factors, but it is up to each bank to explore the build/buy/partner/ignore equation. Access to credit is a crucial part of the banking relationship, especially for small business owners and prospective entrepreneurs. Banks that are unable to meet those needs are under threat of losing lucrative customers.
