Peer-to-peer lending – a case study

This section provides a fictional case study applied to peer-to-peer lending

Isabella's Pastry Shop

Setting the scene

Isabella is a pastry chef whose sales have been steadily increasing and she has recently moved to bigger premises, including a small restaurant that now accounts for 30% of her turnover. However, this has put a significant strain on her staff and capacity. To double her capacity she needs to buy a new machine for processing dough and additional ovens. This would allow her to double her capacity. The combined cost of these new machines is €50 000, which is what she set out to find. Isabella went to ask for a loan at her local bank, where she already has a €10 000 overdraft facility and is paying off the final year of a €30 000 loan (for the initial investment). However the bank would only offer her a loan of just €30 000 at a 14.5% interest rate, rather than the 11.5% she previously had in place. She decided to search on the internet for alternatives and came across peer-to-peer lending.

Preparation: day 1 – day 10

Isabella spent some time researching everything she could find about the concept of peer-to-peer lending, paying particular attention to how it worked, which sites offered it and under what conditions/ price and the rules the sites set. She collected and read blogs/articles about peer-to-peer lending and looked at other borrowers similar to hers and the deals they had. At the end of that week she felt she understood it and knew enough to apply. To find out more about lender behaviour, Isabella registered with a couple of peer-to-peer lending platforms and lent €100 of her own money in tiny sums to other businesses like hers. It allowed her to get a better idea of what it is like to be a lender and what people will most likely focus on. With this knowledge, she spent the time putting together the financial records and other disclosure requirements.

The fundraising period: day 11 – day 20

Once everything was finished and thoroughly checked, Isabella submitted her documents to the platform. The credit assessment team from the platform followed up with her for some additional financial information, including additional filed and management accounts, and they looked at this information alongside the credit models used by the platform. Soon afterwards, Isabella heard that her business had passed the credit assessment. Now that it had been approved, the business could be listed on the marketplace for investors to bid on. Some of the lenders decided to get in touch with Isabella via the live Q&A tool. They asked her questions to get a bit more detail on how she intended to use the money and the profitability of the business over the last couple of years. Happy with Isabella's answers, her €50 000 loan was fully funded by lenders within a couple of days of being listed. She had the choice of either taking the average rate offered upon reaching the target, but decided to keep her loan on the marketplace for the full seven day auction. Over the remaining days, Isabella watched the interest rate come down as more investors bid to lend to her.

After the bid

Once the auction finished, the platform got in touch with Isabella to confirm the final average rate of 10.3% that had been offered. This was in line with the average for her rating category (B) and was below even her original borrowing cost from a bank (11.5%). Isabella drew down the loan and the funds were in her bank within three working days. Isabella paid back the loan and the interest on a monthly basis over a five-year period. This was managed by a direct debit to the platform, which then managed repayments back to the investors' accounts.