

In-Class Exercise: P2P Lending Business Models

Exercise 1: Structured Debate — “Is Funding Circle a Marketplace or a Lender?”

Format: Split into two teams. Each team prepares arguments for its assigned position, then presents. After both sides speak, the class votes — but first, read the debrief questions.

Team A — “Funding Circle Is a Marketplace”

Anchoring evidence: Funding Circle was founded as a SME-loan auction platform, its core software stack matches investor bids with borrower listings, a substantial share of origination flows to external institutional buyers, and its fee logic historically centred on placement fees rather than net-interest income.

Team A: Funding Circle Is a Marketplace

Argument I

Argument II

Argument III

 Concession *Strongest argument AGAINST your position:*

 Closing *How you address the concession:*

Team B — “Funding Circle Is a Lender”

Anchoring evidence: Funding Circle warehouses loans through structured vehicles, participates in government-guaranteed lending programmes, maintains a capital cushion sized to balance-sheet exposure, and reports net-interest income as a meaningful revenue line distinct from placement fees.

Team B: Funding Circle Is a Lender

Argument I

Argument II

Argument III

 Concession *Strongest argument AGAINST your position:*

 Closing *How you address the concession:*

Debrief Questions

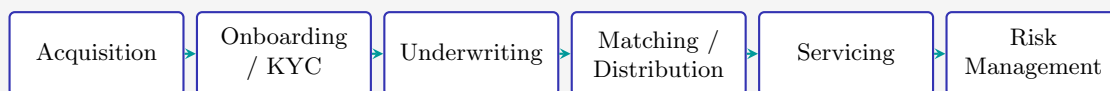
Q1: Does the answer — marketplace or lender — matter for how regulators should supervise Funding Circle? Why or why not?

Q2: Could the answer genuinely be “both”, and if so, what does that imply for investors trying to value the firm?

Q3: Name another firm (in any sector) whose original business model has drifted toward the incumbent’s model over time. What tensions did that drift create?

Exercise 2: Lending Value-Chain Mapping

Scenario: The traditional consumer-lending value chain can be broken into six links. Marketplace lenders attack individual links with specialised solutions. Your task: for each link, identify a platform, describe the friction it removes, and predict the long-term outcome.



Value Chain Link	Platform Attacking It	Friction moved	Re-	Replaces or Improves?	Bank Loses or Adapts?
Acquisition					
Onboarding / KYC					
Underwriting					
Matching / Distribution					
Servicing					
Risk Management					

Synthesis Question

Q1: Which link in the lending value chain is *most vulnerable* to marketplace-lender disruption? Which is *most resistant*? Defend your reasoning with reference to switching costs, regulatory barriers, data advantages, and the balance-sheet-creep paradox.

Facilitator Solutions

Sample answers for instructor reference. These are illustrative; student reasoning may diverge and still be valid.

Exercise 1: Debate Sample Answers

Team A (Funding Circle Is a Marketplace) — sample arguments

Argument I. The platform's founding architecture is an auction matching engine: investors post demand, borrowers post listings, the software clears a spread between them. That matching logic is the defining value-creation mechanism of a two-sided platform, not a lender. The platform's earliest investors were retail, and the earliest revenue was a placement fee — revenue that scales with transaction volume rather than with the size of a loan book.

Argument II. Even today a substantial share of origination flows to external institutional buyers through whole-loan sales and structured pass-through vehicles. That external-distribution channel keeps the platform's risk profile closer to a broker than to a depository lender: the loan exits the platform's books rather than sitting on them.

Argument III. The platform exhibits classic two-sided network effects: more committed investor capital shortens time-to-fund, which attracts more borrowers, which deepens the investor pool. That reinforcing loop is the economic hallmark of a marketplace. A pure lender, by contrast, captures no network externality from growing its book.

Concession. The strongest argument against Team A is that warehousing activity, government-guaranteed programme participation, and a sizable capital cushion all look like the balance sheet of a lender, not a marketplace.

Closing. The balance-sheet activity is a bridging mechanism for arrival-rate mismatch between the two sides of a real marketplace, not evidence that the marketplace is secondary. The economic centre of gravity remains the matching engine; the balance sheet is a supporting layer.

Team B (Funding Circle Is a Lender) — sample arguments

Argument I. Warehousing loans on the platform's own books creates exactly the credit risk that defines a lender. The firm sets aside capital against that risk, manages provisioning, and reports net-interest income as a revenue line. Those activities do not belong to a marketplace.

Argument II. Participation in government-guaranteed lending programmes requires the platform to originate and hold loans under the same regulatory framework as a bank participant. The compliance obligations, capital treatment, and operational controls are indistinguishable from a lender's. Regulators do not grant these programmes to pure marketplaces.

Argument III. The firm's capital cushion is sized to balance-sheet exposure, not to placement-fee volume. That sizing logic is the defining property of a regulated lender. A marketplace would not carry a cushion calibrated to loan-book size because it would not have a loan book.

Concession. The strongest argument against Team B is that the auction matching engine and retail-investor placement channel remain real, functioning parts of the business, with genuine network effects and real marketplace revenue.

Closing. Regulatory classification follows economic substance. When a firm takes credit risk onto its own books and manages a capital cushion calibrated to that exposure, it is a lender — regardless of how it acquired those loans.

Debrief Q1 — Regulatory supervision

Whether a regulator should treat Funding Circle as a marketplace or a lender depends on the risks it creates, not on the label it prefers. A pure marketplace generates mostly conduct-of-business and investor-protection concerns; a lender adds prudential concerns — capital adequacy, provisioning discipline, liquidity, concentration risk. If the platform warehouses loans and runs a capital cushion, prudential supervision is warranted in addition to conduct rules. Applying only marketplace oversight to a firm that takes credit risk would leave the prudential risks unaddressed, which is the outcome supervisors try hardest to avoid.

Debrief Q2 — “Both” as an answer

The answer genuinely can be “both”: Funding Circle operates a matching-engine marketplace on top of a balance-sheet lender on top of a compliance function built for both. That duality matters for valuation because the two layers earn money on different clocks and at different multiples: placement fees scale with volume and attract platform-style valuation multiples, while net-interest income scales with book size and attracts lender-style multiples. Investors who apply a single multiple to the whole firm will systematically mis-price it; investors who apply sum-of-the-parts logic can triangulate more accurately.

Debrief Q3 — Cross-sector drift example

A clean parallel is early e-commerce marketplaces that began as pure listings platforms and eventually moved into first-party inventory — the platform warehouses the stock, takes inventory risk, and competes with its own third-party sellers. The tension this creates is acute: the marketplace message still promises a neutral venue, while the first-party book forces the platform into direct competition with the sellers it relies on. The parallel to Funding Circle is structural: the balance-sheet layer promises to absorb arrival-rate friction for the marketplace, but once it exists it redefines what the firm is.

Exercise 2: Value-Chain Mapping Sample Answers

Value Chain Link	Platform Tackling It	At-	Friction Removed	Replaces or Improves?	Bank Loses or Adapts?
Acquisition	LendingClub (comparison funnels)		Branch-dependent intake for consumer loans	Replaces	Bank Loses
Onboarding / KYC	Prosper (digital document KYC)		Branch visit for identity and income verification	Improves	Bank Adapts
Underwriting	Auxmoney (thin-file model)		Rejection of applicants that shallow bureaux cannot score	Improves	Bank Adapts
Matching / Distribution	Funding Circle (SME auction)		Relationship-officer bottleneck on SME term loans	Replaces	Bank Loses
Servicing	Mintos (originator-reporting layer)		Cross-jurisdiction servicing opacity for retail investors	Improves	Bank Adapts
Risk Management	Platform scoring engines generally		Manual rule-based review with limited data integration	Improves	Bank Adapts

Synthesis Question Sample Answer

The most vulnerable link is Matching / Distribution. Switching costs at the matching layer are low: a borrower can submit the same application to multiple platforms in the time it takes to pour coffee, and an investor can reallocate capital between platforms with a few clicks. Cross-side network effects and data-driven pricing compound this — each new user who joins a dominant platform raises its scoring accuracy, which widens its advantage over thinner competitors. The most resistant link is Risk Management at the prudential layer. Regulatory barriers (capital-adequacy rules, concentration limits, stress-test regimes) and the data moat built from years of repayment history entrench incumbents whose books are already large. A platform that attacks Matching can grow quickly but eventually hits the balance-sheet-creep paradox: to scale the product, it has to warehouse loans, which pulls it into the prudential regime where its incumbent-disadvantage resets. A platform that attacks Risk Management directly faces that regime from day one without the marketplace revenue cushion. Either path is hard; the Matching path starts easier and gets harder, while the Risk path starts harder and stays hard.