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SoFi Technologies

SoFi Q1 2023 Earnings Call

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SoFi Technologies, Inc.; CEO & Director
Christopher Lapointe
SoFi Technologies, Inc.; CFO

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PRESENTATION:

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Operator^ Good morning. And thank you for attending today's SoFi First Quarter 2023 Earnings Call. (Operator Instructions) At this time, I would now like to turn the conference over to our host, Maura Cyr, from SoFi Investor Relations. Maura, please proceed.

Maura Cyr^ Thank you and good morning. Welcome to SoFi's first quarter 2023 earnings conference call. Joining me today to talk about our results and recent events are Anthony Noto, CEO, and Chris Lapointe, CFO.

You can find the presentation accompanying our earnings release on the Investor Relations section of our website. Our remarks today will include forward-looking statements that are based on our current expectations and forecasts and involve risks and uncertainties.

These statements include but are not limited to our competitive advantages on strategy, macroeconomic conditions and outlook, future products and services, and future business and financial performance. Our actual results may differ materially from those contemplated by these forward-looking statements.

Factors that could cause these results to differ materially are described in today's press release and our most recent Form 10-K as filed with the Securities and Exchange Commission as well as our subsequent filings made with the SEC, including our upcoming Form 10-Q.

Any forward-looking statements that we make on this call are based on assumptions as of today. We undertake no obligation to update these statements as a result of new information or future events. And now, I'd like to turn the call over to Anthony.

Anthony Noto^ Thank you, Maura, and good morning, everyone. The first quarter at SoFi was an incredible beginning to what is already turning out to be yet another eventful year in the macro environment. Amid all the volatility, we delivered another quarter of record revenue and adjusted EBITDA with strong overall operating results, reinforcing the strength of our strategy and our ability to execute with excellence.

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A few key achievements from the first quarter include: our eighth consecutive quarter of record adjusted net revenue of $460 million, up 43% year-over-year, with record revenue in Lending and Financial Services as well as continued strength in Tech Platform; our third consecutive quarter of record adjusted EBITDA at nearly $76 million, representing a 48% incremental margin and a 16% margin overall; an incremental GAAP net income margin of 54%, resulting in a loss of just $34 million.

Deposits increased by $2.7 billion sequentially, marking another record quarter and now exceed $10 billion in total deposits. Importantly, more than 90% of our consumer deposits are from sticky direct deposit members and 97% of our deposits are insured. Our cash and cash equivalents on the balance sheet increased by $1.1 billion to $2.5 billion since year-end, reinforcing our strong liquidity position.

Once again, we are achieving several financial inflection points. Adjusted EBITDA of $76 million is now greater than stock-based compensation at $64 million, which actually declined. And this is another critical step towards GAAP net income profitability. We achieved positive variable profit in the Financial Services segment and remain on track for positive contribution profit by year-end.

Additionally, lending net interest income revenue, or NIM revenue, of $201 million exceeded lending noninterest income of $136 million for the second consecutive quarter, and importantly, our NIM revenue is meaningfully greater than our lending segment directly attributable expenses of $115 million.

These trends increase the visibility and reinforce our goal of achieving positive GAAP net income in Q4 2023. Along those lines, we had another quarter of positive GAAP net income for SoFi Bank at $73 million, reflecting a 20% margin and a 23% return on average tangible equity on our way to expected 30% returns within the bank over the long term.

Lastly, the quality of our bank operating and liquidity metrics remain robust and have improved since year-end. We saw new record levels of unaided brand awareness in the quarter and continued strong cross-buy trends, which helped drive strong year-over-year growth in members and products with decreasing marketing spend intensity.

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The 433,000 new members in Q1 '23 brings total members to nearly 5.7 million, up 46% year-over-year. We also added 660,000 new products in Q1, ending with nearly 8.6 million total products, also up 46% year-over-year. Of these new adds, Financial Services products totaled 7.1 million at quarter end and grew by 51% year-over-year, while Lending products of 1.4 million were up 24% year-over-year.

Sales and marketing expenditures as a percent of revenue declined nearly 100 basis points from last quarter and nearly 475 basis points from a year ago. The strength of our results once again underscores how our full suite of differentiated products and services provides the foundation for a uniquely diversified business that is able to endure through market cycles as well as exogenous factors.

We talk often about our ability to act nimbly in a rapidly changing environment. There were several examples once again this last quarter, but I'd like to take a moment to highlight one that really exemplifies nimble execution to truly help our members at the most critical time.

As the recent bank crisis developed, our team was able to bring our deposits FDIC insurance capabilities from offering $250,000 to $2 million within a week, providing comfort and safety to our members and enabling 97% of our deposits to now be insured versus 92% before the increase.

Now I'd like to spend time touching on segment level results as well as the structural advantage of our product strategy and having a bank charter. In Lending, we generated a record $325 million of adjusted net revenue, up 33% versus the prior year period. Our personal loan performance more than offset the continued headwinds in demand for student loan refinancing and the less robust performance of home loans.

Student loan refi continues to be impacted as federal borrowers still await clarity on the end of the moratoria and federal student loan payments. Home loans face macro headwinds from rising rates while we continue the process of integrating Wyndham Capital Mortgage, which we acquired at the beginning of Q2 2023.

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The personal loans business maintained its strength in Q1, hitting record originations of nearly $3 billion, up 46% from $2 billion in Q1 2022. This product continues to deliver even as we maintain our stringent credit standards and pass on rate increases to our borrowers. While these origination levels themselves are impressive, the strength of our balance sheet and diversification of our funding sources provide new options to fund origination growth while driving efficiencies with cost savings.

These advantages are a direct result of SoFi Bank. Having more balance sheet flexibility allows us to capture more net interest income and optimize returns, which provides more stable earnings in any macro environment, but it's especially important in times of excess volatility.

As of the end of Q1 2023, 44% of our loans were funded by deposits, and our $2.7 billion of new deposits raised in the quarter helped fund our $3.6 billion of total originations in the most cost-effective way. Our lending capacity remains robust with over $20 billion in total capacity to fund loans and meet our liquidity needs with $10 billion of deposits, which have grown by $2 billion a quarter, $3 billion of equity capital and $8.6 billion of warehouse capacity.

Lastly, the bank contributes to strong growth in SoFi Money members, high-quality deposits and great levels of engagement. This has led to a higher average account balances even as average spend has increased.

More than 50% of newly funded SoFi Money accounts are setting up direct deposit by day 30, and this has had a significant impact on spending. Q1 annualized spend was 2x 2022 spend, and Q1 spend per average funded account was up 15% quarter-over-quarter. SoFi Money members have increased over 48% year-over-year to 2.4 million accounts. Given the quality of these members with a median FICO score of 749 for our direct deposit portfolio, we see ample opportunity for cross-buy.

This is a great segue into Financial Services more broadly, where net revenue more than tripled year-over-year to $81 million and grew 25% from $65 million in Q4 '22. Contribution loss of $24 million improved $19 million versus the previous quarter, and we achieved very able profitability for the first time in this segment even as we maintained elevated marketing expenses in the first quarter.

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We've continued to achieve strong member and product growth by iterating our products to ensure they are differentiated on four key factors: fast, selection, content, convenience and continue to invest and make them work better when used together.

So far in Q2, we continue to iterate on these products. Last week, we raised our savings rate again to 4.2%. And just this morning, we announced SoFi Travel in partnership with Expedia, which will include member discounts and 3% cashback rewards on bookings made with the SoFi Credit Card. SoFi Travel is a digital destination that represents our first nonfinancial product effort to help our members spend better in the next phase in SoFi's mission to help our members achieve financial independence.

We finished Q1 with 7.1 million Financial Services products, up 51% year-over-year and 5x total lending products of 1.4 million. The increased scale in financial services helps drive cross-buy and marketing efficiencies.

Financial Services sales and marketing spend as a percentage of net revenue was 51% versus 16% in Q1 of last year. We continue to scale our top-of-the-funnel products given the attractive monetization opportunities by capitalizing on our improved brand awareness and network effects. We saw this increased efficiency even with the fact that these products have a 12- to 18-month payback period.

For Technology Platform, full segment revenue of nearly $78 million saw a growth of 28% year-over-year with a 19% margin at the segment level or 28% if you exclude Technisys. Galileo's overall diversified growth strategy includes growth in new verticals, new products and new geographies with a focus on larger customers that have large installed bases.

In Q1, Galileo signed five new clients and made big strides in the strategy with 80% of newly signed clients having existing customers or portfolios along with our growing pipeline of joint opportunities selling Galileo and Technisys offerings to an expanded customer base. Technisys recently signed one new client in Mexico and has entered into a proof-of-concept stage with a large U.S. legacy financial institution. With that, let me turn it over to Chris for a review of the financials for the quarter.

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Christopher Lapointe^ Thanks, Anthony. We started the year with a great quarter, which saw strong growth trends across the entire business. We achieved record revenue and adjusted EBITDA despite operating in a rapidly evolving macro backdrop. I'm going to walk you through some key financial highlights for the quarter and then share some color on our financial outlook.

Unless otherwise stated, I'll be referring to adjusted results for the first quarter of 2023 versus first quarter of 2022. Our GAAP consolidated income statement and all reconciliations can be found in today's earnings release and the subsequent 10-Q filing, which will be made available next week.

For the quarter, top line growth remained strong as we delivered record adjusted net revenue of $460 million, up 43% year-over-year and 4% sequentially from the fourth quarter's record of $443 million, and above our Q1 guidance of $430 million to $440 million.

Adjusted EBITDA was $76 million at a 16% margin, also above the high end of our most recent guidance of $40 million to $45 million and ahead of the prior quarter record. This represented 14 points of year-over-year margin improvement, demonstrating the strong operating leverage of the business as it scales.

Year-over-year margin improvement has been driven by significant operating leverage across our sales and marketing, G&A and ops functional expense lines. Overall, this resulted in a 48% incremental adjusted EBITDA margin year-over-year.

Our GAAP net losses were $34 million this quarter, which is a $76 million improvement year-over-year and a $6 million improvement sequentially. Our incremental GAAP net income margin was 54% for the quarter. In addition to our adjusted EBITDA margin expansion, we saw meaningful leverage against stock-based compensation as a percentage of net revenue at 14% in Q1 2023 down from 16% in the fourth quarter and 24% in the prior year quarter. This represents further progress toward our expectation of GAAP net income profitability in Q4 2023.

Now on to the segment level performance, where we saw strong year-over-year growth across all three segments. In Lending, first quarter adjusted net revenue grew 33%

year-over-year to $325 million. Results were driven by 113% year-over-year growth in our net interest income, while noninterest income was down 17%.

Growth in net interest income was driven by a 99% year-over-year increase in average interest-earning assets and a 318 basis point year-over-year increase in average yields resulting in an average net interest margin of 5.5% for the quarter. This represents roughly 110 basis points of year-over-year NIM expansion.

Q1 originations grew 7% year-over-year to $3.6 billion and were driven by record volumes in our personal loans business, which grew 46% year-over-year to nearly $3 million. However, student loan originations were down 47% year-over-year and home loans by 71% year-over-year as the extension of the federal student loan moratorium and macro factors continue to provide headwinds to these businesses.

We achieved this top line growth while maintaining our stringent credit standards and disciplined focus on quality. Our personal loan borrowers weighted average income is $164,000 with a weighted average FICO score of 747. Our student loan borrowers weighted average income is $173,000 with a weighted average FICO of 769.

This continued focus on quality has led to strong credit performance. Our on-balance sheet delinquency rates and charge-off rates remain healthy and are still below pre-COVID levels.

Our on-balance sheet 90-day personal loan delinquency rate was 38 basis points in Q1 '23, while our annualized personal loan charge-off rate was 2.97%. Considering the weighted average life of the personal loans on our balance sheet, our portfolio life of loan losses are forecasted to be 4.5%, which is below our risk tolerance.

Our on-balance sheet 90-day student loan delinquency rate was 12 basis points in Q1 '23, while our annualized student loan charge-off rate was 0.34%. As we've expressed in the past, it is reasonable to expect credit metrics to revert over time to more normalized pre-pandemic levels but continue to expect very healthy performance relative to broader industry levels.

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The Lending business delivered $210 million of contribution profit at a 65% margin, up from $133 million a year ago and a 54% margin. This improvement was driven by a mix shift to higher-margin personal loans revenue as well as sales and marketing and ops efficiencies and fixed cost leverage across the entire segment.

Shifting to Tech Platform, where we delivered net revenue of $78 million in the quarter, up 28% year-over-year, while Galileo revenue was up 3% year-over-year. Overall, annual revenue growth was driven primarily by Galileo account growth to 126 million in total. We also signed five new clients in Galileo and one in Technisys, and we finished the task of moving every client to the cloud with 100% of transactions now migrated.

Sequentially, revenue and contribution profit declined in the segment due to seasonality in transaction volumes, along with timing implications from shifting focus to larger potential partners with larger existing businesses, B2B customers, and a more durable customer base, which has longer sales cycles. The segment delivered a contribution profit of $15 million representing a 19% margin and 28% if you were to exclude Technisys.

Moving on to Financial Services, where net revenue of $81 million increased 244% year-over-year with new all-time high revenue for SoFi Money and continued strong contributions from SoFi Credit Card, SoFi Invest and Lending-as-a-Service. Overall, monetization continues to improve with annualized revenue per product increasing for the fourth consecutive quarter to $45, 2x the $20 in the prior year and up 15% sequentially from $40.

We reached 7.1 million Financial Services products in the quarter, which is up 51% year-over-year, and we continue to see strong product adds with 584,000 new products in the segment. We hit 2.4 million products in SoFi Money, $2.2 million in SoFi Invest and $2.2 million in Relay.

Contribution losses were $24 million for the quarter, which improved by over 50% year-over-year and 44% sequentially as we start to see operating leverage in the segment. Importantly, we achieved positive variable profit in the Financial Services segment for the first time, which reinforces our expectation of positive contribution profits by the end of 2023.

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Switching to our balance sheet, where we remain very well capitalized with ample cash and excess liquidity. Last year's opening of SoFi Bank further reinforces our strong balance sheet and provides us with more flexibility and access to a lower cost of capital relative to alternative sources of funding.

In Q1, assets grew by $3.4 billion as a result of a $1.1 billion increase in cash and cash equivalents, highlighting our strong liquidity position and access to cash as well as adding loans to the balance sheet given the strong growth we continue to see in personal loan originations.

On the liability side of the balance sheet, we saw tremendous growth in deposits as they grew to over $10 billion, up $2.7 million sequentially versus $2.3 million in each of the prior two quarters. Because of this, we exited the quarter with just $3.5 billion drawn on our $8.6 billion of warehouse facilities. In addition, last week, we extended our corporate revolver for another five years and upsized it to $645 million.

This further highlights our strong liquidity position, particularly in this market. Our available for sale securities portfolio remains quite modest at $175 million market value with $6 million in cumulative unrealized losses versus $195 million at year-end 2022. This portfolio consists primarily of short-duration government-backed securities.

Let me finish up with guidance. Throughout the last 12 months, we have demonstrated the benefit of having a diversified set of revenue streams, multiple cost-efficient sources of capital and a keen focus on underwriting high-quality credits. We expect those benefits to persist going forward even in light of the existing macro backdrop. For Q2, we expect to deliver adjusted net revenue of $470 million to $480 million and adjusted EBITDA of $50 million to $60 million.

For the full year of 2023, we are raising guidance and now expect to deliver adjusted net revenue of $1.955 billion to $2.02 billion, up from our prior guidance of $1.925 billion to $2 billion, and we now expect full year 2023 adjusted EBITDA to be $268 million to $288 million, up from our prior guidance of $260 million to $280 million. This represents a 30% incremental EBITDA margin for the full year.

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Overall, we couldn't be more proud of our Q1 results and continued progress. Having delivered over $460 million of adjusted net revenue and $76 million of adjusted EBITDA, we continue to make great progress against our long-term growth objectives in the quarter and remain very well capitalized to continue pursuing our ultimate goal of making SoFi a top financial institution. With that, let's begin the Q&A.

Operator^ (Operator Instructions) Our first question comes from the line of Mihir Bhatia with Bank of America.

Mihir Bhatia^ Maybe to start, Chris, if you could just provide the loan sales and gain on sale margins this quarter with and without hedging if possible, please. And just talk also about the larger strategy, is there any change as you've grown deposits to hold loans for longer? Or is it still very much a buy and distribute model?

Christopher Lapointe^ Yes. No problem. So I'll hit on each of the products, starting with our home loans business. So in home loans, we ended up selling $78 million of principal at 104.7% execution level. Inclusive of hedges, it was about 100 basis points less than that. In our personal loans business, we did not do any whole loan sales in period. Our last one was in Q4 at 104.4% execution. But we did execute a $440 million consumer loan ABS transaction with spreads that outperformed our expectations, and we were able to price at 90 basis points over SOFR.

The deal was 8x oversubscribed with over 28 orders, which allowed us to tighten spreads meaningfully by 80 basis points relative to the deal that we did back in Q4 that had comparable collateral. The market obviously continues to search for shorter duration securities backed by higher credit collateral. And then in student loan refinancing, we did not do any whole loan sales in period. Our last one was in Q3 at 104.4% execution.

What I would say in terms of your second question, Mihir, as we've discussed in the past, we are extremely well capitalized at this point, having raised $3.6 billion in 2021. We have access to $8.6 billion in warehouse lines, $3.5 billion of which is drawn currently.

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And our bank deposit base of $10 billion is growing really quickly with the vast majority of our deposits, more than 90% of them coming from direct deposit members. In addition to that, we've been able to successfully access the ABS markets each of the last two quarters, which have brought attractive fixed financing options for all of our loans. Given this flexibility, we're always going to maximize returns on the loans that we originate as well as the overall firm ROE.

And that's going to take different forms given the environment that we're operating in at any given point in time. This quarter, similar to last quarter, we had the flexibility to hold loans for a longer period of time, particularly given the growth that we saw in deposits of $2.7 billion, which resulted in really strong net interest income, but that could certainly change in future quarters, but we have a lot of options and flexibility today.

Operator^ Our next question comes from the line of Jeff Adelson with Morgan Stanley.

Jeffrey Adelson^ I was just wondering if you could dig in a little bit more on the loan growth expectation from here. You've been doubling the loans every quarter year-on-year. And I understand you have a lot of capital at this point. But is there a point at which you feel like you need to start selling your loans again?

And then, I guess, on the actual loan sales side, what are your -- what gives you confidence that the loans you're marking on your balance sheet today, if you were to start going back to the market again, what gives you confidence that you can kind of hold on to those marks you have on the balance sheet?

Anthony Noto^ Thanks, Jeff. First, what I'd say is that our overall strategy as it relates to loans and when we sell them versus hold them is really driven by liquidity and our ability to optimize return on equity. It's the same strategy we've had since 2018. Our ability to execute has only become more and more strong and robust so that we have maximum optionality.

I would love to remind everyone that if you think about our liquidity stack and our funding stack, we have $3 billion of equity -- our own equity capital that we can fund with; $8 billion of warehouse facility, and then as we reported today, $10 billion of

deposits. That source of funding allows us to be very nimble in what we decide to hold versus what we decide to sell.

It also allows us to be very nimble as it relates to loan purchases of SoFi loans and other opportunities that we have is optionality, on deals over time. So in essence, there's no one answer to your question. It's about maximizing ROE and making sure we have the right liquidity and making sure we have the right capital ratios as a bank. I'll let Chris talk about the way we think about the value of the loans in the marketplace.

Christopher Lapointe^ Yes, absolutely. And in terms of why we get confident in the sense that we would be able to sell the loans at where they're currently marked, every single quarter, we work with a third-party valuation firm that marks to market each and every one of our loans on an individual basis to account for changes in every single factor that impacts loans.

So that's things like the weighted average coupon, default rates, prepayment speeds, benchmark rates, spreads as well as where secondary bonds and residuals are trading. So you see that mark-to-market take place every single quarter, and that flows through the revenue line of our P&L.

Operator^ Our next question comes from the line of Kevin Barker with Piper Sandler.

Kevin Barker^ I wanted to follow up on the acquisition you announced a couple of months ago on Wyndham Capital. You mentioned that it's going to be accretive within the next six months. And I believe they did about $2 billion of originations last year according to some press reports.

Could you just give us an idea of like how big do you expect the mortgage platform to be? And then what does the accretive within six months guidance imply? Did you have to do a significant amount of further integration within the SoFi platform? Or is a lot of that already existing within Wyndham?

Anthony Noto^ Thank you. First, let me approach the question about home loans from a strategic standpoint. As many of you know, we want to be a one-stop digital provider

for all our financial needs during all the major decisions of your financial life and all the days in between.

In order to do that, we have to be there when you make large decisions like how you pay for college, like how you may pay for grad school and medical school or buying a home. We've taken approach over the last five years where we prefer to vertically integrate with our technology. It gives us lower cost. We can innovate at a much faster rate. We can make better real-time decisions, more personalization. The mortgage industry, as you know, is very cyclical.

And it can really be challenging if you take actions at the height of the market from an acquisition standpoint or other investment standpoints. We've worked hard over the last three years to find a technology and a platform that we could buy at a great price, a small dollar amount that could be integrated pretty quickly and allow us to accomplish the objectives that I mentioned from vertical integration.

We couldn't have been happier to find Wyndham. We think it's a phenomenal team. It's a long and durable company, just the way that Galileo and Technisys was around for decades, and it was founder-led and Jeff will continue to stay with us at SoFi. The integration will be done throughout the year. It's not significant in size in terms of the bandwidth that we have to allocate for that integration.

So we feel like we can make it accretive by the end of the year. In terms of volume that we're doing, as you can imagine, the environment has been very challenging for home sales and refinancing.

And so the volume was quite low relative to historical levels. And you should really think about it as a technology integration and significantly increased capacity for us to step on the gas pedal to increase our market share gains. And we intend to do that on the back of the full integration.

So expect it to have a much more meaningful impact in 2024 once we feel great about the ability to scale not just the technology but our processes and our people. To ensure our members have a great experience, time to fund is critically important in purchase

mortgages, and we want to have the best time to fund possible for our members with high satisfaction. I'll let Chris talk about the accretion.

Christopher Lapointe^ Yes. So overall, what we assumed in the back half of the year is that this was not going to have a material impact on the overall business, either from a top line or a bottom line perspective. But from an accretion perspective, we would expect it to deliver positive contribution.

Operator^ Our next question comes from the line of John Hecht with Jefferies.

John Hecht^ Congratulations on a great quarter. I wonder if you guys can just talk about over the course of the year, we've got certain things happening like the potential moratorium ending for student loans and obviously the changes that are expected in the interest rate markets. Maybe just considering all that, can you give us your kind of expectations for the mix of originations over the course of the next few quarters?

Christopher Lapointe^ Yes, sure. John, I can take that one. So what I would say is we aren't providing specific guidance at the product level, but we are expecting to continue to see modest growth in our personal loans business. This past quarter, we reached 8.2% market share. That was up from 5.8% last quarter and 5.50% a year ago. So there is significant headroom to continue to grow that business.

But as we've said in the past, we are going to continue to be prudent and thoughtful about how we approach that business and won't overextend ourselves. So expect to see continued modest growth in that business, similar to what you've seen over the course of the last several quarters.

On student loan refinancing, our guide and outlook has not changed from our Q1 earnings call -- or Q4 earnings call. What was contemplated in our full year guide is that the moratorium would end on June 30 and then people would go back into repayment 60 days thereafter, which means that we would see elevated demand for student loan originations in Q4 albeit at a lower monetization level given where interest rates are.

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We do think that there is still a large TAM that we can go after given where we can price the loans today. So we do expect to see an uptick in demand, but probably not to the levels that we saw back in Q4 2019.

Then in home loan originations, Anthony just touched on it, we do expect to see an acceleration in originations given the acquisition of Wyndham Capital. Right now, we have a very, very low market share. So there's a ton of headroom to continue.

Operator^ Our next question comes from the line of Eugene Simuni with MoffettNathanson.

Eugene Simuni^ Congratulations on great results. I wanted to go back to the trends in your deposits. Great to see very strong growth in Q1. But can you elaborate a little bit on the trend in March since the beginning of the bank crisis? And maybe if you can share anything on what are the trends in April. And just maybe as a broader question here, how is the behavior of your bank customers changed at all since the bank crisis and how are you adjusting to that? I'd love to hear your thoughts on that.

Anthony Noto^ It's another quarter since opening the bank about a year ago in February of continued strong performance of our SoFi Money account, which is checking and savings.

As you know, the strategy has really played out in spades throughout the year, offering high interest rate on checking and very high interest rate on savings, up to 4.2% now if you do direct deposit with us, getting all the other member benefits that we provide for you beyond that free certified financial planner, discounts on loans, our broad-based rewards program, all of which are now bundled to SoFi Plus, has really helped us drive not just strong adoption of SoFi Money but a lot of engagement as it relates to both deposits and spending.

We couldn't be more happy with the trends we're seeing in both of those. We expect them to continue into the second quarter that we've seen so far in April and throughout the May and June time period.

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What I'd say about Q1 is that it's really hard to sort of separate out what may have happened because of all the uncertainty and maybe a flock to safety as people trust SoFi and came to our product and used it more frequently.

I would say the trends in April are off to a start that would indicate we should be at a similar level of $2 billion plus in deposits at the end of the quarter. In terms of spending, we continue to see really strong growth in spending as our direct deposit members increase given that they're using it as their primary account.

And so that's also a contributing factor to our financial results that sort of gets overlooked because of just the strong performance on NIM that we continue to see and how much more scale that is. But the spending trend on debit and so forth has really mirrored the trend in deposits as well as NIM to reinforce our overall strategy, giving us an opportunity to have more touch points in helping people get their mine rate based on their spending and what's happening in their accounts.

Operator^ Our next question comes from the line of Reggie Smith with JPMorgan.

Reginald Smith^ I only have one question so it's going to be kind of long, I guess. I was curious, what are your loss expectations -- [life of loan] loss expectations for your most recent cohort of personal loans? How does that compare to maybe your '22 cohort? And then a follow-up to that is how are the 22s tracking relative to your initial expectations?

Anthony Noto^ Thank you for the question. I'll let Chris get into particulars. But at a high level, since 2018 we've architected our personal loans in a way that will drive to at least a 40% to 50% variable profit margin, and that includes all the variable costs, including life of loan losses and funding costs.

The reason why we target that level of profitability is so that our loans are durable through the cycle. If we're seeing trends that lead us to believe that we can't get to that level, we will make changes, sometimes that's increasing our WACC, sometimes that's being more efficient in our marketing costs, sometimes that involves driving down lower cost of funding.

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As it relates to the macroeconomic conditions impacting life loan losses, we will tighten credit. We've tightened credit in the past. We have a very sophisticated real-time ability to test pricing and credit and a number of early warning economic indicators that have caused us to be more conservative on what we underwrite and tighten credit throughout the year, and we'll continue to do that.

But we've been below our target life for loan losses of 7% to 8%, which is part of that equation of 40% to 50% variable profit margin. I just don't want people to think it's just about that metric. It's about the overall unit economics of getting to 40% to 50% variable profit margin, and that assumes 7%-8% life of loan losses, which we've been below and. Our cohorts have really continued to trend relative to that metric in a positive way.

Christopher Lapointe^ Yes. And I would just add on, if you look at all of our cohorts on a month-to-month, quarter-to-quarter basis, they've all been relatively consistent with the framework that Anthony just laid out. At the overall portfolio level, right now our annualized charge-off rate on the personal loans business is 2.97%. If you take the weighted average life into consideration for that portfolio, it gets you to an estimated life of loan losses of about 4.5%, which again is meaningfully below the 7% to 8% risk tolerance level that we have today.

Operator^ Our next question comes from the line of Moshe Orenbuch with Credit Suisse.

Moshe Orenbuch^ Great. And most of my questions have been asked and answered. But I thought -- and you talked about this a little bit in the prepared remarks, but I think it's actually quite interesting in terms of the ability to increase, whether it's cross buy or reduced marketing spend, because of the increase in the number of members across financial services SoFi Money.

Could you talk a little bit in a little more detail, like how you would expect to see that playing out over the course of the next year or 2? And kind of more specifically, is it a function of less marketing for consumer loans? Is it Lantern products? Like what are the biggest benefits to SoFi?

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Anthony Noto^ Yes. So we talk about a concept called the FSPL, Financial Services Productivity Loop. And the concept is very simply we want to leverage the broadest reach, most appealing high-engagement products, like Relay, like SoFi Money, like SoFi Invest and SoFi Credit Card to really build a significant amount of products in those categories. As we build that scale, we have information about our members that allows us to give them personalized offers that best meet their needs.

So for example, if we bring in a SoFi Money customer member, and that member does direct deposit with us, and we see the mortgage that they're paying or we see the student loan that they're paying, we see them sitting on a ton of cash we see them overrunning and having a significant amount of credit card debt, we can make a very specific recommendation to them on how to get their money right in that particular area.

We play that strategy out every day. Sometimes it's driven by technology and data and sometimes it's driven by the mechanical processes of our teams as well as our certified financial planners. That cross-buying allows us to bring in that second product with no customer acquisition cost and has a huge impact on unit economics.

So let's take a personal loan, for example, and this is just illustrative. Let's just say, over the course of the time, our average variable profit on a personal loan, and so that would be the revenue of that personal loan less the life of loan losses, the funding costs and variable operating costs and the customer acquisition cost, results in $800 of variable profit. That could have a customer acquisition cost of anywhere between $600 to $1,000.

If someone comes in through Relay, and they do credit score monitoring or they connect accounts or they're in checking or savings, and we see that they have a bunch of credit card debt and can benefit from consolidation, we would make a term loan offer to them or personal loan offer. If that person adopts that personal loan, the variable profit goes from $800 up by the savings on customer acquisition costs, so anywhere to $1,400 to $1,800.

That significant variable profit dollar amount above and beyond what we need can then be reinvested in better technology, lower prices, better service, higher interest rate on

checking or savings and it drives the flywheel. We're seeing that happen across the board.

Having the bank license only makes it better for us because we can now actually have lower cost of deposits, which improves our unit economics both on SoFi Money as well as our loan products. So we're seeing the compounding benefits of that over and over.

In terms of the outlook going forward, we averaged roughly about 1.5 products per member. I would expect that ratio to stay very similar over the next 12 to 18 months because we're driving really strong member growth.

And if you think about the denominator, if it's growing really strong, it's really hard to drive the overall portion of the products divided by the members. That's not a bad thing. That's actually a good thing because the bigger we make our member base, the big we'll make our products adopted by that number base over time.

Over the long run, we hope to have every product for our members. There's not a specific perspective that I have on the exact number other than that you do everything with us. Why? We're trying to build the best-of-breed products by category and so that we can help them borrow better, save better, spend better, invest better. And ultimately, if we do that, the number of products they have with us will be very large.

Operator^ Our next question comes from the line of Dominick Gabriele with Oppenheimer.

Dominick Gabriele^ Great results. So we saw significantly better revenue and adjusted EBITDA in the quarter. And I'm beginning to even wonder how much we need the student loan business to return to you guys have a really strong franchise [prevail]. But the incremental adjusted EBITDA margin was higher than expected in the quarter.

And if you take this quarter and the next quarter's guidance, you get still you're roughly 30% expectation for incremental EBITDA margins. And so could you just talk about any shifts that may have happened between this quarter, next quarter or if there's any seasonality as far as kind of that 30% expectation that we should be thinking about?

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Anthony Noto^ Thank you for the question. As it relates to student loans, I want to break it into two categories. You have our private student loans, i.e., the loans that people are taking out to actually go to school. So we're in the in-school student loan business. We're also in the student loan refinancing business. That business is one that takes our members who have either private student loans or federal student loans and refinance them at a lower rate or a longer term to lower their monthly payment, much like the home loan refinancing industry.

As long as the college education in the United States is not free, there will be a student loan market. Simply said, as long as the college education in the United States is not free, there will be a need for student loans. Sometimes, those student loans could be provided by the government and sometimes they can be provided by private institutions. Because of that dynamic, we will always be in the student loan business.

The question is, are we just in the private student loan business or the private student loan business and the refinancing student loan business? I believe we'll always be in both businesses regardless of what's decided by the Supreme Court on forgiveness and regardless of what happens with the moratorium.

Why? The cost of education is significantly greater than the ability of people to pay. Therefore, they have to borrow money to do that. As long as they're borrowing money, we can find a way for them to not just get access to that loan but to do it at a lower cost as they continue to improve in their financial lives. So it's never a question in our mind whether we're going to be in the business. It's just a question of what are the actual products and how do we best meet the members' needs.

Because I'll just reiterate again, we want to be there for every one of the major financial decision in someone's life and all the days in between, which means we have to be in the student loan business to execute our strategy. In terms of the particulars as it relates to EBITDA margin, I'll let Chris answer that.

Christopher Lapointe^ Yes. So in terms of the outperformance that we saw in Q1, Dominic, we saw revenue outperformance across both our Lending and our Financial Services businesses, primarily attributable to net interest income as I alluded to in my prepared remarks. From an expense perspective, we did see really good cap efficiencies

given the strong member and product growth, particularly in lending, where our customer acquisition costs on a per loan basis was down 20% sequentially.

And then in addition to that, we were able to manage expenses effectively again throughout the quarter, creating leverage across our entire fixed cost area. Collectively, the revenue outperformance, along with the efficiency gains drove the excess earnings that we decided to drop to the bottom line and take more of a conservative approach given the uncertainty in the market.

Overall, as we've discussed in the past, we strive to spend about 70% of our incremental revenue, as we've said. Depending on a number of factors, we may choose to drop more to the bottom line period to period. And that's what happened certainly this quarter, and you'll see periods of overearning followed by deployment of those resources back into the drivers of the business.

Anthony Noto^ And the only other thing I'd add is there's a lot of operating leverage in the business, and you're seeing that come through in Q4 and again in Q1. We are trying to balance investing to drive growth with prudent responsibility of driving towards profitability to give investors clear transparency on where our long-term margins and ROE can be. We couldn't be more confident about the long-term margins of the company and return on equity, but we need to move judiciously through the process of balancing both.

One of the things I would tell you is that we've been driving the growth that we have and the improvement in profitability with our Financial Services segment being unprofitable. So the Lending segment has a positive contribution margin. The Tech Platform has a positive contribution margin, and then we have large losses in Financial Services.

The reason why that's the case is because there's a 12- to 24-month payback on customer acquisition costs so we absorb that cost upfront and then we recoup it over time. We're finally to the point that we're actually a positive variable profit margin for the Financial Services segment. That means we're actually covering all that customer acquisition cost. And the next step for us now that we're positive on a variable profit

basis is getting the total variable profit dollars to be greater than the fixed direct cost of Financial Services.

And once we do that, all three segments will have positive contribution margin. So we're just getting started with the type of leverage and we drive over time. We will dampen your expectations on where the margins will be in the intermediate term because we also want to keep investing, but we will hit the milestones that we've laid out as it relates to GAAP profitability and Financial Services positive contribution margin unless there's a huge dislocation that we can't anticipate today.

Operator^ Our next question comes from the line of Robert Wildhack with Autonomous.

Robert Wildhack^ I wanted to ask one more about deposits. Anthony, it sounds like you're talking about at least another quarter of really solid growth. So zooming out beyond that, what's the current strategy and line of thought with respect to keeping the pedal down on deposit growth versus maybe giving up some of that growth rate but possibly taking a lot of pressure off your deposit cost and deposit betas?

Anthony Noto^ Well, the great thing about our company and our vertical integration is that the cost that we're -- currently have on our checking and savings account are lower than the cost that we've ever had in the business historically from a spread standpoint. So it's actually cheaper for us to fund via deposits than the way we've historically funded via warehouse lines.

And so that's a huge competitive advantage. The reason we can offer the interest rate that we offer is because we actually make more money than we would with warehouse lines and without being a bank. And so the cost is completely acceptable [where it's not], and we continue to be aggressive with the interest rate.

I think the bigger question is what happens when rates start to get cut and go down, I think we'll be able to hold rate much longer and higher than our competitors and really gain even more market share.

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Our goal is to have as many direct deposit customers as we can. That's a leading indicator of primary account, and we -- that's our strategy. Direct deposit is one indicator of that. There are others that we're using now and that will give people benefits from if they take those other actions outside of direct deposit. But the rate that we're providing is very competitive but it's very attractive to us for a financial reward -- return standpoint.

Operator^ Our next question comes from the line of Aaron Cyganovich with Citigroup.

Aaron Cyganovich^ Just a quick question on the Technology segment. It looks like the revenue is down a little bit sequentially. If you remove the client you left, kind of flattish. Do you expect any pull forwards or contract renewals there? And what do you expect in terms of revenue growth for that segment going forward?

Anthony Noto^ Yes. One of the things we wanted to point out is that the Technology Platform is in a transition from a lot of small accounts and earlier stage start-ups to fewer larger durable customers. We made the decision throughout 2022 to stop chasing a lot of smaller deals. And so what you see in the quarter is less new customers coming on and contributing to revenue that would have been signed in '22 in the earlier part of the year. And that transition is ongoing.

We expect the revenue to continue to stay at about this level throughout the year, and we'll start to see more meaningful contribution from some of the larger, more durable customers that we've signed up, a couple of which are actually on the platform now and contributing. But that will become bigger and more significant by the end of the year.

We really like the strategy. It's longer lead times, it's longer sales cycles. But the economic opportunity for each one of these partners goes well, well beyond just using the processing platform or APIs at Galileo to a number of other products.

One of the things that may not be obvious to everyone is that we're starting to see really strong traction and some of the products that are on top of the platform. So for example, Konecta is a natural language AI chatbot that helps with customer service. SoFi actually just integrated it itself in our business, but it's gotten great uptick from adoption from our partners.

We also rolled out something called PRP, which is Payments Risk Platform. We're leveraging all the data on the Galileo platform. We process about 6 billion transactions a year. That gives us great intelligence to be able to detect transactional fraud. We're now offering that product and capability to our partners and have seen really strong uptake there.

And then we also launched on our platform for the first time fully integrated SoFi, Galileo and Technisys a [pay it forward] product. The -- it's an installment-based product that's like buy now, pay later but it's delivered in your app. You apply in your app, you get a virtual card instantly. You get a card number, and you can execute that at any retail location or any online capability through an access like a debit card or a credit card but has different economics in the back end.

The great thing about the product is that it's driven all by interchange. It's not driven by a retailer's discount and it's not driven by an interest rate or a fee. And so there's a lot that's in the pipeline for the technology platform. The demand is as strong as it's ever been.

We're going to move through this transition of fewer smaller accounts to larger -- sorry, fewer smaller accounts than what we used to do to get to these larger, more durable customers. And we should start to see the benefit in the back half of the year in terms of an acceleration of revenue and then into 2024.

Operator^ Our last question goes to the line of Matthew O'Neill with FT Partners.

Matthew O'Neill^ Just want to clarify and make sure the prior question, Technology segment and the commentary around fewer smaller accounts and more larger ones going forward. Is that directly connected to the small dip we saw this quarter in the Galileo accounts, just some smaller ones coming off before some bigger ones are being folded in?

And then just as a separate follow-up, just curious on the macro front with what's going on in the rate environment. Is there a unemployment rate that you guys think about where things would start to become more concerning? Or there'll be some nonlinear

impact on the credit quality side? And are we anywhere kind of close to that assumption, if not, but just kind of curious what you guys are thinking about on the potential horizon?

Anthony Noto^ Yes. On the Technology Platform side, I think you're asking a question about accounts and the growth of that being slower year-over-year and down sequentially. That just reflects a partner that moves off the platform and those accounts moving off. So it's both new account growth offset by that partner that moved off in 2022 off the platform.

In terms of the unemployment rate, I'll give -- I'll hand it over to Chris to talk about how we think about underwriting credit and the macroeconomic factors that we're looking at.

Christopher Lapointe^ Yes. So our overall outlook on the macro hasn't changed from our Q4 earnings call. What we had talked about during that is that the rate curve was going to be consistent with where the forward curve was at the time and peaking around 5% to 5.25% and exiting the year at 4.5%. So that's still contemplated in our current outlook.

We assumed that the unemployment rate would be 5%. So we're holding with that as well. And we -- finally, we assumed that there would be a 2.5% GDP contraction. And then finally, we did assume that credit spreads would remain elevated. We have seen that over the course of the last several quarters, and we expect that to persist heading into Q2, Q3 and Q4. But that's all contemplated in our guide.

Anthony Noto^ And let me finish here by saying that we've been in an all-out sprint over the last five years to build out our digital product suite to meet our members' needs for every major financial decision in their lives and all the days in between.

Thanks to the incredible grit and hard work of our team at SoFi, we've been able to do that consistently. That said, we've seen tectonic plate shift for the industry in each of the last five years, and in some years, multiple times.

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But through that volatility and uncertainty, we continue to prevail and thrive hitting eight record quarters of revenue in a row and hitting strategic and financial inflection points all along the way. 2023 has proven to be as formidable in just three short months as any year and it's just getting started. We're likely to see another multi-tectonic plate shifting year.

That said, SoFi will be ready. We'll be ready because the benefits of our strategy to build a uniquely diversified business, combined with the national banking license, not only positions SoFi to be the winner takes most in the [separate] transition of financial services to digital but also provide greater durability through a market cycle and the many other model events that may occur.

I'm excited about where we are today and even more excited about where we can go from here. With that, thank you for your interest in SoFi. And we'll talk to you in three short months.

Operator^ This concludes SoFi's Q1 2023 earnings call. I hope you have a wonderful rest of your day.