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GreenSky, Inc. (GSKY)

Q1 2019 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you and welcome to GreenSky First Quarter Fiscal 2019 Earnings Conference Call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions will be given at that time. We are webcasting this call live on GreenSky Investor Relations website. After the completion of the call, a recording of the call will be made available on the same site.

I would now like to turn the conference over to Rebecca Gardy, Senior Vice President of Investor Relations at GreenSky. Please go ahead.

Rebecca Gardy
Senior Vice President, Investor Relations, GreenSky, Inc.

Thank you, Chris and good morning everyone. Earlier this morning, GreenSky issued a press release announcing results for its first quarter ended March 31, 2019. You can access this press release on the Investor Relations section of the GreenSky website. Joining me on the call today are David Zalik, Chairman and Chief Executive Officer; Gerry Benjamin, Vice Chairman and Chief Administrative Officer; and Rob Partlow, Chief Financial Officer.

Before we get started, let me remind you that our presentation and discussions today will include forward-looking statements. These are statements that are based on current assumptions and are subject to risk and uncertainties that could cause actual results to differ materially from those projected. We disclaim any obligation to update any forward-looking statements except as required by law. Information about these risks and uncertainties is included in our press release issued this morning as well as in our filings with regulators.

We will also be discussing certain non-GAAP financial measures on today's call. These non-GAAP measures are not intended to be considered in isolation from, a substitute for or superior to our GAAP results, and we encourage you to consider all measures when analyzing GreenSky's performance. These non-GAAP measures are described and reconciled to their GAAP counterparts in the presentation materials, the press release dated May 7, 2019 and on the Investor Relations page of our website.

Following our prepared remarks, we will take your question. As a courtesy to other participants, please ask no more than two questions. And in the event you have additional questions that are not covered by others, please feel free to re-queue and we'll do our best to come back to you. Thank you for your cooperation on this. And finally, a replay of this call will be available later today on our website at greensky.com.

And with that, I will now turn it over to David.

David Zalik

Chairman & Chief Executive Officer, GreenSky, Inc.

Thank you, Rebecca. Good morning, everyone and thank you for joining us. I'm very pleased to report that GreenSky's first quarter played out materially consistent with our seasonally adjusted plan, with both operating results and new merchant additions in line with expectations, with momentum continuing very nicely into the second quarter.

I'd like to start off this morning by providing a brief overview of our Q1 2019 performance and then share a few key takeaways from our recently held GreenSky Merchant Council Meeting before turning it over to Gerry to discuss our key operating metrics and then to Rob to review our financial results in greater detail.

You will see on slide 4 that we reported a 20% year-over-year growth in transaction volume in the first quarter to $1.24 billion. Ex solar originations, transaction volume grew 27%. This growth was aided by strong and growing demand in our elective healthcare vertical, which now represents approximately 10% of total monthly transaction volume. Importantly, Q1 origination volume was materially consistent with management guidance previously provided of 19% of 2019 full-year origination guidance at the midpoint.

On slide 8, you will see that in 2018 GreenSky enjoyed its most productive annual cohort of new merchant additions, setting the company up nicely for strong growth in 2019 and the years to come. This is an important continuation of a four-year trend of record annual merchant cohort growth.

GreenSky reported Q1 adjusted EBITDA of $18.7 million, representing an adjusted EBITDA margin of 18%. Recall that Q1 each year reflects GreenSky's lowest revenue quarter while at the same time, Q1 is burdened by elevated public company costs as well as accrual of annual sponsor volume driven rebates. Rob will cover additional details surrounding our Q1 operating results.

Let me now transition to the key takeaways from our GreenSky Merchant Council Meeting. During the last weekend in March, we hosted our first GreenSky Merchant Council Meeting which provided our senior management team extended one-on-one time with a number of our largest merchants and sponsors. As I reflect on what our team heard during this inaugural event, there were six key takeaways shared by virtually every merchant in attendance.

One, the fundamental demand for home improvement projects continues to be very strong. No merchant we met with reported seeing any softening in demand associated with the variability of reported housing starts. Two, project backlogs and merchants' qualified leads going into 2019 reflect a continuation of the healthy pace of new project starts experienced in 2018 suggesting that 2019 will be another record year in terms of dollar volume of home improvement projects completed. Three, the lead times to mobilize crews and kick off jobs continued to extend throughout the back half of 2018 as the shortage of skilled labor impacted all our merchants nationwide. Four, GreenSky's instantaneous paperless digital financing tools are playing an ever increasing role and enabling merchants to close more projects at higher unit prices per job. Five, our merchants believe that the distance between GreenSky and our leading competitors in terms of our technology and tools continues to widen. Six, the more that GreenSky can do to enhance our proprietary merchant technology platform with additional tools such as digital quoting, CRM, sales and marketing, universal applications, the greater the level of merchant account penetration to be achieved.

As I shared in our prior quarter's earnings release, the current GreenSky technology roadmap is incredibly robust, and we're excited about the products we'll be releasing in the coming quarters, informed in no small measure by the direct input we receive from our merchants.

I'll now turn it over to Gerry to provide an update on key operational metrics.

Gerry R. Benjamin

Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

Thank you, David and good morning. As a financial technology company, GreenSky is dedicated to driving the future of payments, advancing the way commerce has conducted. This year we're highly focused on two key initiatives, advancing our technology offerings and deepening our market penetration. Our proprietary technology platform is a key differentiator for GreenSky, and we're continuing to innovate on exciting value-added feature functionalities for all members of the GreenSky ecosystem.

GreenSky operates within a very large addressable market with our mobile, online and in-store point-of-sale finance technology. We have tremendous runway to grow our market share within our existing industry verticals of home improvement and elective healthcare. Concurrent with growing our presence in these two verticals, we're leveraging our playbook to selectively enter new verticals, including specialty retail and e-commerce.

You'll see on slide 6 of the investor deck, that as of March 31, we had 15,745 active merchants on our platform, an increase of 29% compared to last year. Our merchant base includes small owner-operated home improvement contractors, elective healthcare providers as well as large national home improvement and healthcare service organizations. Our merchants are leveraging the GreenSky platform to provide their customers with financing solutions, which are as important as ever in fueling the growth of their businesses.

Since last reporting on representative of new merchant additions during the first quarter of 2019, GreenSky has successfully on boarded four regional HVAC distributors and installers expected to generate more than $120 million in annual finance volume; three residential roof and exterior remodeling contractors expecting to generate in excess of $100 million in annual finance volume. Multiple interior and external general residential remodeling contractors and multiple owner operator franchisees of one of the largest domestic replacement window franchisor in the U.S., such franchisor is expected to generate in excess of $650 million in annual system wide retail sales.

And in our elective healthcare segment during the same period, we have brought on a 700-door national dental service organization or DSO expected to generate in excess of $200 million of annual patient finance volume, 350 additional clinic locations offering Allergan-licensed, noninvasive, body sculpting procedures, a large national dental practice management software sponsor integrating the GreenSky patients solution platform as its primary first look patient finance utility, a significant dental implant provider with 51 clinical locations nationwide and a myriad of general restorative and aesthetic dental practices representing more than 200 clinical sites nationwide.

Since the company's inception through the end of the first quarter, GreenSky has now enabled over 17 billion of transactions with over 2.4 million consumers. With financing plans that meet customer needs, merchants close more deals and with larger contracts, making our platform increasingly integral to driving their business growth.

Through our bank partners highlighted on slide 8, GreenSky facilitates loan types ranging from no payments and no interest if the purchases balance is paid during the promotional period to attractive reduced rate installment loans.

Our total aggregate Bank Partner commitments was $11.8 billion as of the end of the first quarter with $4.5 billion of unused commitments. Demand for additional GreenSky originated assets by our existing Bank Partners is strong and we see continued interest by new perspective Bank Partners.

GreenSky's proprietary technology platform is intuitive, it's paperless and it's user friendly. As David mentioned, this is a key differentiator as is our seamless integration. Merchants are increasingly using the GreenSky technology platform to improve customer experience, complete projects while supplying our Bank Partners with an attractive pool of prime and super prime borrowers.

Slides 10 and 11 reflect the average FICO score at origination of these consumers which [indiscernible] (00:11:10) exceptionally strong at a mean FICO of 769. Consumers with average FICO scores of 780 or above now comprised 36% of the loan portfolio at March 31, up sequentially from the same time last year and over 85% have FICO scores of over 700. In no case, have we relaxed credit standards in any fashion. 30-day delinquencies in Q1 2019 were 1.13%, up a modest 13 basis points compared to 1.18% in Q1 2018 predictively attributable to the growth in our patient solutions servicing portfolio. Delinquencies in home improvement are stable and totally consistent with prior years.

And finally on slide 11, we disclosed the Origination Productivity Index or OPI, which was 21.9% for the first quarter substantially equivalent to the 22.2% at the end or flat to Q1, 2018.

And with that, I'll turn it over to Rob to review our financial performance and provide an update on our 2019 full-year guidance. Rob?

Robert G. Partlow

Chief Financial Officer & Executive Vice President, GreenSky, Inc.

Thank you, Gerry. As I review the results for the first quarter during my remarks that all my comparisons will be relative to the first quarter of 2018 unless otherwise stated. Transaction volume increased 20% to $1.2 billion for the first quarter of 2019. Excluding solar originations which were approximately $48 million lower than last year, we grew transaction volume by 27% during the first quarter. We expect year-over-year growth to accelerate for the remainder of the year as originations of elective healthcare vertical continue to accelerate and we expand our initiatives in the specialty retail and e-commerce.

As we have discussed previously, origination volume follows a predictable seasonal pattern, with the first and fourth quarter being weaker than the second and third quarter. Total revenue grew 22% to $103.7 million in the first quarter. Transaction fees grew 18% to $84.0 million. The average transaction fee for the first quarter was 6.8% compared to 6.9% last year.

As a reminder, the first quarter of every year, we apply a volume-based promotional allowance for certain sponsors, which in 2019 reduce the effective transaction fee by $3.5 million. Adjusting for that rebate, the average transaction fee was 7.05% versus 7.1% in the first quarter of 2018. For the full year, we expect the transaction fee rate to be between 7.0% and 7.1%. As always, seasonal fluctuations in the mix of different promotional products offered by our merchants and providers will cause transaction fee percentage to ebb and flow throughout the year.

Servicing and other revenue totaled $19.7 million reflecting 34% growth of the loan servicing portfolio which ended the quarter at $7.6 billion. Servicing fees represented an annualized 1.05% of the average servicing portfolio. While revenue grew 22%, our adjusted EBITDA decreased from $27.5 million in the first quarter of 2018 to $18.7 million this quarter attributed to a combination of both timing as well as investment spending.

Two thirds of the delta is associated largely with common items related to the expected increase in the fair value change in the FCR liability that we expect to dissipate in the following quarters, which is resulting from spread compression and margin contraction as an increase in contracted Bank Partner portfolio yields associated with our increase in the benchmark rates coupled with a slight increase in credit losses of shareholders to the company's growing mix of healthcare plans which was expected. And a third of the increase is related to the higher expenses in both servicing, origination, and operating expenses, a piece of which is associated with being a public company as well as to drive our growth.

Turning to the components of cost of revenue, we breakout on slide 14 the components of cost of revenue into three distinct components, origination expense, service and expenses, and the fair value chains in the FCR liability. Origination-related expenses were $8.5 million or approximately 0.7% of originations.

We expect origination expenses will trend closer towards 0.6% of transaction volume in the coming quarters as we benefit from higher transaction activity. Servicing-related expenses totaled $10.7 million or approximately 0.6% of the average loan servicing portfolio. We continue to expect service and expenses to trend towards 0.5% over the next couple of quarters as we benefit from building scale within our operations.

The fair value change in the FCR liability was $38.8 million for the first quarter, or annualized 2.1% of the average loan servicing portfolio. The increase is $17.3 million versus last year as a function of both the growth and the deferred interest loan products, as a percentage of origination, as well as an increase in the bank partner portfolio yield, which negatively impacted receipts.

On slide 14, we have provided the detail of the components of the fair value change in the FCR liability. And on slide 15, we also break out the fair value change in the FCR liability by the drivers of this expense line. As discussed last quarter, I believe slide 15 is a key to understanding the fair value change in the FCR liability, as it lays out the two components, the expense for future finance charge reversals and receipts which act as reduction to the aforementioned expense.

I'll begin with the expense for future finance charge reversals which is the expense related to the building up of the liability on our balance sheet for future finance charge reversals. This expense was $70.9 million during the quarter or an annualized 3.79% of the average servicing portfolio, up from $49.6 million during the first quarter of 2018 or 3.58% of the average servicing portfolio. The increase in expense is due to both the growth and deferred interest loans in the portfolio as well as the higher APR and deferred interest loans originated since mid-2018.

As previously noted, we expect the FCR rate to continue to increase over the remainder of the year. Given the impact of higher APRs on transactions as well as the higher mix of deferred interest loans in our elective healthcare vertical, we expect the impact of this increased FCR rate to be largely offset by increases in incentive payments, a component of receipts as the year progresses.

Receipts from our servicing portfolio reduce the expense for future finance charge reversals and totaled $32.1 million or 1.72% of the servicing portfolio. The receipt percentage is down from 2.04% during the first quarter of 2018 due primarily to Bank Partner yields on new originations increasing on transactions during the first quarter of 2018 at a faster pace than the loan yields on new originations.

Recall that during the third quarter, our price increases on merchant transaction fees drove the mix of loans to higher finance charge APRs and resulted in loan rates increase in a much faster rate than bank margins. As a trend of higher loans vis-à-vis bank margins continues over the next several quarters, we expect receipts to increase on a year-over-year basis. Yet let me pause here to emphasize an important point, as discussed last quarter, receipts are adversely impacted in the fourth quarter and first quarter by the seasonality of consumer charge-offs and conversely, receipts benefit from the seasonality in consumer credit cycle in the second and third quarters. We expect the seasonality to positively impact receipts over the next two quarters.

Operating expenses were $34.2 million in the first quarter, an increase of 33% over the last year. The increase is driven by the growth in our sales and marketing expenses, investment in our technology platform and the cost of being a public company. As you know, we had no public company costs in the first quarter of 2018. In addition, the first quarter traditionally has a higher level of public company and other G&A expenses, accordingly, we expect our operating expenses to decline by $2 million to $3 million next quarter.

Operating profit was $11.5 million for the first quarter. And from a GAAP perspective, we had a first quarter tax benefit attributable to the exercise during the quarter of options and warrants. Net income was $7 million during the quarter because GAAP net income excludes non-controlling interest, a function of our Up-C structure, we believe pro forma net income is a useful measure of our enterprise's financial results. Pro forma net income was $6.5 million using an effective 19.25% effective tax rate, which is our estimate for the full year's effective tax rate.

As we've indicated on prior earnings calls, we believe that adjusted EBITDA is one of our key financial indicators on our business performance over the long term and provides a useful information regarding whether cash provided by operating activities is sufficient to maintain and grow our business. And for the first quarter, adjusted EBITDA was $18.7 million.

Turning to our balance sheet, we finished the quarter with $268 million of unrestricted cash. Free cash flow for the first three months of 2019 was $20 million as detailed on slide 22 (sic) slide 21 (00:20:53). We review the repurchase of our Class A shares as an attractive use of cash given the current price and have continued to be opportunistic in such respect. During the first quarter, we repurchased $4.3 million of additional shares of Class A common stock at an incremental cost of $51 million under our $150 million board approved share repurchase program. Furthermore in April, we repurchased an additional 99,000 shares for a total cost of $1.3 million. In total since we began the program in the third quarter of 2018, GreenSky has repurchased 9.1 million shares at a cost of $96.1 million.

Quickly turning to our guidance for the full year of 2019, as we announced in our earnings press release based on our first quarter performance and current market conditions, we are reaffirming our full-year 2019 guidance. This guidance includes transaction volume to increase between 27% to 35% of the fiscal 2018 to between $6.4 billion and $6.8 billion, revenue to grow between 30% and 38% of the fiscal 2018 to between $538 million and $572 million, pro forma net income to grow between 17% and 28% over fiscal 2018 to between $128 million and a $140 million and adjusted EBITDA to grow between 22% and 31% over the fiscal 2018 to between $210 million and $225 million.

And with that, I'd like to turn over to Rebecca to set up the Q&A.

Rebecca Gardy
Senior Vice President, Investor Relations, GreenSky, Inc.

Thanks, Rob. And that concludes our prepared remarks. Before we move to questions, I want to remind listeners that GreenSky is participating in two upcoming investor conferences. David Zalik will be presenting at the JPMorgan Global Technology, Media and Communications Conference in Boston on Wednesday, May 15 at 4:20 PM Eastern Time. Gerry Benjamin will be presenting at the Needham Emerging Technology Conference in New York on Tuesday, May 21st, at 8.20 in the morning. Both presentations will be webcast and available on GreenSky's Investor Relations website.

In addition, the company filed its 2019 proxy statement on April 30th, and announced that we will be holding our first annual meeting of shareholders on Thursday, June 6th at 10.00 AM. The event will be virtual only, and all details on how to access the call are contained in the proxy materials. And finally, GreenSky's 2018 annual report is now available on the investor relations section of our website.

Please remember, we are happy to take details modeling questions offline. And with that, operator, let's please have our first question.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And our first question comes from the line of Jim Schneider with Goldman Sachs. Your line is now open.

James Schneider
Analyst, Goldman Sachs & Co. LLC

Q

Good morning. Thanks for taking my question. Good to see the progress in the elective healthcare vertical now at 10% of volume, I think you stated. Maybe, David, can you give us a little bit of an update on the momentum you see in that vertical? And then, maybe a bit of a sense as we get to the end of 2019, how big you think that could be as a percent of the overall total? Thank you.

David Zalik
Chairman & Chief Executive Officer, GreenSky, Inc.

A

Thank you, Jim. Good morning. We're very excited about elective healthcare in 2018 ending the year with 10% of our volume being in healthcare was a very important milestone and a goal that we were very proud to accomplish and we're set up to double that this year. I don't think I caught the second half of your question.

James Schneider
Analyst, Goldman Sachs & Co. LLC

Q

Just in terms of where you'd expect that to be as a percentage as we exit the year? I guess it helps if you say you're going to double this year?

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

A

Jim, this is Gerry. The run rate at the end of 2018 gave us great confidence that we'll double the dollar amount in 2019 over 2018 and that should grow from 10% of system wide kind of enterprise revenue to something in the mid-teens.

James Schneider
Analyst, Goldman Sachs & Co. LLC

Q

Got it. That's helpful. Thanks. And then...

David Zalik
Chairman & Chief Executive Officer, GreenSky, Inc.

A

So, healthcare is going to double but the rest of the business is growing very nicely too.

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

A

Exactly.

James Schneider
Analyst, Goldman Sachs & Co. LLC

Q

Understand. Understand. Very clear. And then maybe just a question on the delinquency rate, given what you saw in the quarter, I mean, the delinquency, I think you said stepped up to 1.31% in the quarter, just some rough math on my part would suggest that if it was kind of on a 10% run rate then the delinquency rate and elective healthcare must be kind of like around 4 points or so. Is there anything else that was kind of in that number in terms of a step-up in the home improvement piece of it or is that math roughly right?

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

A

Totally consistent with the home improvement piece.

David Zalik
Chairman & Chief Executive Officer, GreenSky, Inc.

A

That's right. Home improvement was incredibly stable which was very encouraging to have that part of the portfolio, age and the delinquency to be incredibly stable within 1 basis point. So healthcare, as we've discussed for years, is a higher fee, higher delinquency business and it was exactly consistent with our expectations.

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

A

You about nailed it on the percentage basis, Jim.

James Schneider
Analyst, Goldman Sachs & Co. LLC

Q

Great. Thank you.

Operator: Thank you. And our next question comes from the line of John Davis with Raymond James. Your line is now open.

John Davis
Analyst, Raymond James & Associates, Inc.

Q

Hey. Good morning, guys. Well, I just want to touch on rates for a minute. Obviously, rates went up a lot faster than you expected last year but now I think that you've given guidance rates to enter your swap curves or swap rates are down, call it 70 basis points, 75 basis points. So maybe just talk about the impact there, has that resulted in potential upside or the pricing changes you didn't make, just commentary on the reduction in rates and how that'll flow into the P&L for the rest of the year.

David Zalik
Chairman & Chief Executive Officer, GreenSky, Inc.

A

Hey, John. Thanks for the question. As we've said for a couple of years when rates go up, it does not reduce our margin; when rates go down, it does not improve our margin and change of rates creates friction and a distraction for both our merchants and our sales organization. So, when rates stop going up, we don't have to raise rates to our merchants. And so, it's neutral to us.

John Davis
Analyst, Raymond James & Associates, Inc.

Q

Right, but on the bank funding side, right, you should get a benefit because those re-price every quarter. So just thinking about – is there some benefit on the funding line that you won't get on the transaction take rate line this year or has nothing really changed, I'm just trying to understand the FCR impact of the change in rates.

David Zalik
Chairman & Chief Executive Officer, GreenSky, Inc.

A

Yeah. So, as rates go up, what we charge the merchants, the corresponding interest rate to the consumer goes up. When rates stop going up, then we stop raising rates, and so our business is fixed at the time of origination. So, if a loan is originated in December, any subsequent rate changes won't impact the economics on that loan either on the revenue side or the expense side.

John Davis
Analyst, Raymond James & Associates, Inc.

Q

Okay. And then, Gerry, just want to follow up a little bit on Jim's question, just to clarify a little bit. So, the $6.6 billion of originations this year at the midpoint would be an increase of about $1.6 billion. So, if you're doubling the elective healthcare that would mean the $400 million of the growth is coming from elective healthcare and the $1.2 billion would be home improvement. I just want to make sure that I'm thinking about this in the right way.

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

A

Yeah. We don't typically break out to that level of detail, but you're in the right zip code.

John Davis
Analyst, Raymond James & Associates, Inc.

Q

Okay. All right. Thanks guys.

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.
A

Yes.

Operator: Thank you. And our next question comes from the line of Jason Kupferberg with Bank of America Merrill Lynch. Your line is now open.

Jason Kupferberg
Analyst, Bank of America Merrill Lynch
Q

Hey, great. Good morning, guys. I just wanted to start with a question about the overall outlook for the rest of the year, completely understand the expected seasonal softness in Q1. But just talk about your visibility on the acceleration in the transaction volume during the balance of the year, I think the comps do get meaningfully more easy and certainly you have momentum in some of the newer verticals maybe, you need to do low to mid-30s or so. The remaining three quarters to kind of get solidly to the midpoint of the guide. And same question really just on the EBITDA margins. Obviously, you had a couple of known headwinds in Q1, but just your comfort level and your visibility on accelerating significantly during the balance of the year there to achieve the full year target? Thanks.

David Zalik
Chairman & Chief Executive Officer, GreenSky, Inc.
A

Jason, thank you. So Q1 played out in line with what we expected and hoped for and I think that fundamentally seeing a solid Q1 and also seeing an excellent April gives us a lot of confidence going into the next eight months. Having four months anchored year is a very telling insight certainly into volume which is the biggest driver of our business. Seeing stable dynamics and take rates certainly makes our forecasting a lot less complicated and volatile, so that's good. And so we reaffirmed our guidance because we felt good about first quarter, we felt very good about a terrific acceleration of growth in April, and so that gives us a lot of confidence going into the rest of the year.

We're also seeing on a more granular level excellent cohort growth, the 2018 cohort that we signed up in 2018 did more business in 2018 than any other year one cohort in business. It's certainly off to a great start this year. The 2019 Q1 cohort is the biggest Q1 cohort we've ever had. So everything is showing really good positive momentum that we're looking at on the volume side and the EBITDA margin was exactly as we expected and we've seen year after, year after year, Q1 does not look nearly as good as Q2 and Q3 and Q4. So we're seeing it play out as we had hoped.

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.
A

Yeah. The only thing I would add on the EBITDA margin side, we affirm our guidance for the full year at 40% on the EBITDA as a percentage of revenue. So the simple math suggest as we move to Q2, Q3, we'll be producing EBITDA margins in the mid to upper 40s contrasting what we reported in Q1 with greater volume. So the year plays out and our forecast continues to look solid.

Jason Kupferberg
Analyst, Bank of America Merrill Lynch
Q

Okay. That's all good color. Any sort of update on the AMEX alliance, have you put anything into the guide at this point for that? And then, just very quickly on – it looks like the tax rate, you're now expecting something a bit lower, but the net income guide didn't change or just any color there? Thank you guys.

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

A

Sure. Sure. On the AMEX side, we updated in the press release, of course, the prospective merchant referrals and the cross referral that includes elective healthcare which turned down and I believe it was late February so that continues to progress nicely. On the direct to consumer piece, we've actually expanded a piece of the digital capability and the technology build, which has extended the launch just a bit, but we are expecting that to launch mid-year. We continue not – again not to include that in our 2019 guidance, it would just be premature until we see some results.

Rob, on tax rate you want to comment as to what you see for the full year?

Robert G. Partlow
Chief Financial Officer & Executive Vice President, GreenSky, Inc.

A

Yeah. For the full-year tax rate, we – look it's right now assuming 19.25% which we think is kind of our full-year expected tax rate. We did assume that is a little bit lower than our initial guidance. We certainly will continue to examine and think about our guidance, but right now we're standing pat with our current guidance.

Jason Kupferberg
Analyst, Bank of America Merrill Lynch

Q

Okay. Thank you.

Operator: Thank you. And our next question comes from the line of Tien-Tsin Huang with JPMorgan. Your line is now open.

Tien-Tsin Huang
Analyst, JPMorgan Securities LLC

Q

Yeah. Thank you so much. Just to build on Jason's question just with the acceleration comment in April, just curious on the magnitude for 2Q. And I know that the solar company gets a little bit easier [indiscernible] (00:34:31) moving up, any other colors to be clear on 2Q versus second half?

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

A

David's comment regarding the first four months of the year, sort of, validating the full year. We've got going back seven years of history. So, when David used the term anchor, it really becomes quite a predictor for the full year because we build our model up by cohorts, certainly in home improvement our dominant vertical. We've got tremendous visibility in our historical forecasting on volume that has been really quite good. It gets better with the passage of time. So it's hard not to be enthused, Q2 and Q3 are our season, logically the weather gets better, people are doing external work in their homes, the revenue and volumes ebb as you would expect. Anything you would add to that David?

David Zalik
Chairman & Chief Executive Officer, GreenSky, Inc.

A

Yeah. Yeah. Good morning. As we indicated, Q1 volume growth grew 20% year-over-year. April alone grew 27% and that's just the beginning of the busy season where we see an acceleration of growth. So we're very pleased with that as a good start for early spring.

Tien-Tsin Huang
Analyst, JPMorgan Securities LLC

Q

Thank you for that. That's really helpful. Just on the digital tools side, I think there's six points. David, that you mentioned from the merchant council meeting, so is there a backlog of new tools that are going to come out this year to drive some of this penetration, is that comment more shaping where you'll be investing in this year going into next?

David Zalik
Chairman & Chief Executive Officer, GreenSky, Inc.

A

No. We're spending handover fast on those tools right now and we have releases every four to six weeks and so we've got some very exciting tools. We'll be announcing and releasing throughout the year.

Tien-Tsin Huang
Analyst, JPMorgan Securities LLC

Q

Very good. Thank you.

David Zalik
Chairman & Chief Executive Officer, GreenSky, Inc.

A

And it's completely in response to what we learn from our merchants and our partners and the conversation usually goes what could we deliver that would dramatically improve your business that obviously further differentiates GreenSky.

Operator: Thank you. And our next question comes from the line of Andrew Jeffrey with SunTrust. Your line is now open.

Andrew W. Jeffrey
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Hey, good morning. Thank you for taking the question. Good to hear about the progress you're making in elective healthcare. You mentioned several, Gerry, new referral relationships, dental groups in particular in that segment of your business. I wonder if you could just elaborate a little bit on the sort of the competitive dynamic. Is GreenSky being added in these cases as sort of a new lender or against an existing incumbent or in a lot of cases are you exclusive? I know I think you mentioned your preferred in one case, just wondering about how that kind of plays out and whether a lot of the growth comes from sort of share within these practices?

Andrew W. Jeffrey
Analyst, SunTrust Robinson Humphrey, Inc.

Q

That's a good question. The dynamic is really predictable. We have no interest in being a second-look provider first and foremost. So any relationship we initiate or we respond to should we get an inquiry, it's only with the intention of being a first look provider. There is an incumbent with significant plastic in people's wallets to suggest that if you adopt GreenSky as your first-look provider, you won't accept the competitor's currency would be a misstatement on our part, but as we all know, it's not the clinician that makes the financing decision, it's the practice administrator or the finance manager or in case one person offers literally a receptionist at the front desk that paraprofessional that non-healthcare provider typically is determining who gets the applications. We're not going to stay at a provider that uses GreenSky other than as first look. So that doesn't mean they won't occasionally let someone that comes in an office with someone else's plastic in their wallet use that currency, but we are only looking for first look.

Accordingly nobody is going to move their business franchise without going through a beta or a trial just for prudency, so people will give us 10 locations or region or zone run it for a month, look at approval rates, look at the accommodation rates look at the user experience, get feedback from the front desk and in each case that feedback has been validating. This is a superior user experience. Our customers like it. We're being accommodated. We're able to convert folks from a console to a procedure quicker. Those are the ingredients that translate into what we call full adoption, but that cycle from trial or beta to full adoption is pretty predictable, but we're not interest in being a second look provider and being used episodically. That's of no interest to us.

Andrew W. Jeffrey Q
Analyst, SunTrust Robinson Humphrey, Inc.

Okay. Thank you. That helps. And then, is it safe to assume that as with most of the investments you make and the growth you bring on intra year that these newer referrals and so forth will contribute to 2020, more so than 2019 from an overall standpoint?

Gerry R. Benjamin A
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

Absolutely, absolutely.

Andrew W. Jeffrey Q
Analyst, SunTrust Robinson Humphrey, Inc.

Okay.

Gerry R. Benjamin A
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

Just like the cohorts in home improvement, best case you'll have someone on a half year and it will take a number of months to mature a new relationship. So, there's little and we say this time and time again there's little we're doing in 2019 in the way of sales activity that's going to materially impact our 2019 results. Those seeds were sown in 2018 and prior years. One of the benefits of the great visibility we have in our business model.

Andrew W. Jeffrey Q
Analyst, SunTrust Robinson Humphrey, Inc.

Okay. Thanks a lot. Appreciate it.

Gerry R. Benjamin A
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

Surely.

Operator: Thank you. And our next question comes from the line of Chris Donat with Sandler O'Neill. Your line is now open.

Christopher Roy Donat
Analyst, Sandler O'Neill & Partners LP

Q

Hi. Good morning, everyone. Rob, wanted to ask, kind of, a reminder question as we think about the ramp between first quarter EBITDA and the full-year number, it looks optically like a pretty big move but if you could just remind us the moving pieces in that like the expenses that drop away that you have in the first quarter and then some of the other seasonal components, just again looking more for reminder than anything else?

Robert G. Partlow
Chief Financial Officer & Executive Vice President, GreenSky, Inc.

A

Yeah. No, no. Great. Appreciate the kind of the reminder. Certainly, with the seasonality of originations, we fully expect the revenues going to pop in the second quarter as originations pop, kind of, the same seasonal pattern. We'll see as also the same time you'll see your FCR expenses come down and some of the seasonality of consumer credit benefits us in the second quarter. And correspondingly, while those two things are working in our favor from a cost perspective, I talked about how OpEx actually is not flat, actually down a couple million in the second quarter. So what you have is kind of a combination of revenue popping and your expenses coming down which really helped drive that kind of overall increase in EBITDA for the next couple of quarters.

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

A

Yeah. I think on our website, we gave explicit guidance by quarter of origination. So you can sort of see the pop in the revenue piece assuming a flat take rate. And to Rob's point that in combination, the elevated volumes in Q2, Q3 with a reduction in expenses translates into pretty potent EBITDA production.

Robert G. Partlow
Chief Financial Officer & Executive Vice President, GreenSky, Inc.

A

It really all falls to the bottom line is what I think about it.

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

A

Yeah

Robert G. Partlow
Chief Financial Officer & Executive Vice President, GreenSky, Inc.

A

We, kind of, have this fixed cost, OpEx piece of our business and you have a contraction in your margin that first quarter's originations are lower and I think you have that kind of leverage, the organization really pops in the second, third quarters.

Christopher Roy Donat
Analyst, Sandler O'Neill & Partners LP

Q

Got it. But as we think about 2020 and 2021, the seasonality remains the same right? This isn't a new phenomenon. This is just something as does just having been with the company, I haven't seen for. Okay.

Robert G. Partlow
Chief Financial Officer & Executive Vice President, GreenSky, Inc.

A

Absolutely. Absolutely. First quarter is always kind of the seasonal headwind. It's always, you never feel good about your first quarter, but we actually do feel good about our first quarter because it is exactly as we expected. And as you look back over time, we have the same kind of contraction of our margin and it's really because of these seasonality originations and the consumer credit and it's always reaffirming as David highlighted. We really start seeing the benefits that things happen really in March. April as we've talked about, certainly is off to a great second quarter as you can see the originations popping.

Christopher Roy Donat
Analyst, Sandler O'Neill & Partners LP

Q

Okay. Okay. And then another one, I guess, this also fits in the reminder category as your healthcare mix goes from something like 10% to 15% by year end of revenue, what's the – just remind us the difference between say fee rate in healthcare versus home improvement, and then also implications for FCR?

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

A

Good questions. To move from 10% to 15%, we'd suggest that the healthcare business is larger as a percentage of the total pie than it is. It will move to something between 10% and 15%. It won't get to 15% by year end given the dynamic growth. In the home improvement business, we're going to grow that another billion dollars this year. So lot of big numbers catches up there.

With respect to the transaction fee, we do see a higher fee in the healthcare business. It's totally product dependent. I think folks are aware we launched our first revolving product about six months ago, that's been well-received in the marketplace. If I had a guess, I would think that we'll pencil out 25 basis points to 50 basis points higher in transactions, something in that vicinity, not a 100 basis points or 150 basis points higher, but it's product mix dependent.

Christopher Roy Donat
Analyst, Sandler O'Neill & Partners LP

Q

Anything on FCR?

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

A

Greater use of deferred product mix and healthcare. So you will see a little bit bump in the FCR related to those deferred interest products. That steps fine, those deferred interest products come with a nice transaction fee, and it's cash upfront, but we will book the FCR accrual, and the seasonality in net accrual will mimic what Rob mentioned earlier year-over-year, so predictably it will ebb and flow from first quarter, and things will get stronger both on the origination side in Q2 and Q3 and the consumer credit cycle where defaults go down around tax refund season. So you have a couple phenomena contributing into expanding margins in Q2, Q3. It will be the same next year though in that regard.

Christopher Roy Donat
Analyst, Sandler O'Neill & Partners LP

Q

Okay. Thanks very much.

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.

A

You're welcome.

Operator: Thank you. And our next question comes from the line of James Faucette with Morgan Stanley. Your line is now open.

James E. Faucette
Analyst, Morgan Stanley & Co. LLC

Q

Great. Thank you very much for the question. You mentioned that there had been some acceleration in the month of April. And I'm just wondering how much of that is maybe just normal seasonality versus a reflection of improved confidence et cetera from consumers end and your merchant partners?

David Zalik
Chairman & Chief Executive Officer, GreenSky, Inc.

A

Good morning. Thanks for the question. Well it's both. When you are in the middle of winter and people are on vacation and contractors take some vacation and people aren't doing home improvement, waiting for spring and then when you see it and you go from 20% growth to 27% year-over-year growth, it's certainly nice to be in spring time. So for us it is consistent with seasonality but it's certainly more growth year-over-year in April than we saw in Q1.

James E. Faucette
Analyst, Morgan Stanley & Co. LLC

Q

Yeah. Okay. That makes sense, particularly, the year-over-year growth commentary. And then you also mentioned that there was, continued to be skilled labor shortages et cetera. How do you think about that and how that may be keeping down your opportunity set right now and is that at all a headwind or is there, I guess, any other factors that we should be aware of that could be limiting what you could do and that you're kind of using in your formulation of outlook and targets for this year?

David Zalik
Chairman & Chief Executive Officer, GreenSky, Inc.

A

Yeah. Look, I think labor and a volatile political environment has been a headwind for us for years. I don't think that the labor shortage is new. It continues. I think it is amazing that there is so much to consumer demand and merchant demand in such a robust full economy where there is an obvious labor shortage for our platform. And I'm amazed at how much growth we're able to earn and how many merchants we're able to sign up and retain and how much additional penetration we get cohort after cohort after cohort despite having reported tightness in labor.

So we wanted to communicate it because we're hearing it from our merchants, we've been hearing it for years. We're watching some very innovative merchants literally take a 14-week training programs for kids out of high school and saying, give us 14 weeks and we're going to train you on how to be an HVAC technician, really amazing, where they're creating their own trade schools. So we have the pleasure of getting to see entrepreneurs being beautifully entrepreneurial. So yes, there's a labor shortage and that's certainly not helped by the immigration policies or the volatility of immigration policies, but nevertheless we've seen great growth over the last three years.

James E. Faucette
Analyst, Morgan Stanley & Co. LLC

Q

That's great.

Gerry R. Benjamin
Vice Chairman & Chief Administrative Officer, GreenSky, Inc.
A

I don't think we've got a call with an investor group or someone on the phone hasn't reported that they want something done at their home and it's four to six weeks before they can get anybody to come out and give them a quote, let alone start a piece of business. So it's a common phenomena that seems to be occurring all across the country, no geographic pocket but everywhere, gets the result of full employment.

James E. Faucette
Analyst, Morgan Stanley & Co. LLC
Q

Yeah. That's useful. Thank you.

Operator: Thank you. [Operator Instructions] And our next question comes from the line of Rob Wildhack with Autonomous Research. Your line is now open.

Robert Wildhack
Analyst, Autonomous Research
Q

Hey, guys. You talked about a couple of new verticals and mentioned e-commerce in particular. That seems more competitive with FinTech. So first, is there anything different in the required investment in the new verticals that could be showing up in OpEx today? And secondly, can you talk about maybe some broader strategic differences when entering into a new vertical like e-comm?

David Zalik
Chairman & Chief Executive Officer, GreenSky, Inc.
A

Hello, Rob with Autonomous. Good morning. Good question. So, we are FinTech and we have unique advantages over in a very different approach to some of the e-commerce only credit platforms. What we see is they tend to focus on small ticket and sub-prime and near-prime. And our solution is number one, omni-channel which means there are lots of retailers that have physical stores and showrooms and retail stores as well as website e-commerce. So, that gives us a wonderful competitive advantage to be able to engage a merchant and a consumer who might start shopping online concluded in the store or the other way around. And so our differentiation is in the omni-channel, in the ability to support superfast prime large transactions, which by the way is where most of the commerce happens. It is not our business model to provide credit to those that don't have an abundance of credit. That's not what our banks are looking for and it's not where commerce happens.

So when we enter a new vertical just as we did healthcare, we look for where there is friction and how we can use technology and tools to accelerate commerce and create value-added differentiation. We were doing that in healthcare. We're doing that in e-commerce and specialty retail. It's the same platform. So we are spending aggressively, investing in our technology, not only to continue to add features functionality tools in our home improvement platform, but also in our elective healthcare platform, now e-commerce and specialty retail. One thing that's very gratifying is the investments that we make in one of these verticals, many of them help the other ones. So we're investing in e-commerce. Well, it turns out there is lots of home improvement and home good companies that want to use those tools too. So it's one vertical that's helping the other. Rob, did I answer your question?

Robert Wildhack
Analyst, Autonomous Research
Q

You did. Yeah. Thank you. That was really helpful.

Operator: Thank you. And that does conclude today's question-and-answer session. At this time, I would now like to turn the conference back to Rebecca Gardy for any further remarks.

Rebecca Gardy

Senior Vice President, Investor Relations, GreenSky, Inc.

Thank you, Chris. We want to thank everyone for joining us today. Our next quarterly earnings call will be the first week of August. We look forward to speaking with you again then if not sooner.

Operator: With that, ladies and gentlemen, this does conclude today's conference. Thank you all for your participation. You may now disconnect.