

25 November 2022

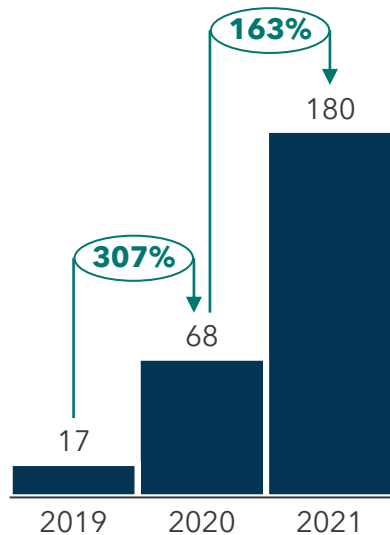
Flagship Advisory Partners Analysis of Consumer Financial Protection Bureau's "Buy Now, Pay Later: Market Trends and Consumer Impacts Report" 2022

Image credits: **Klarna**

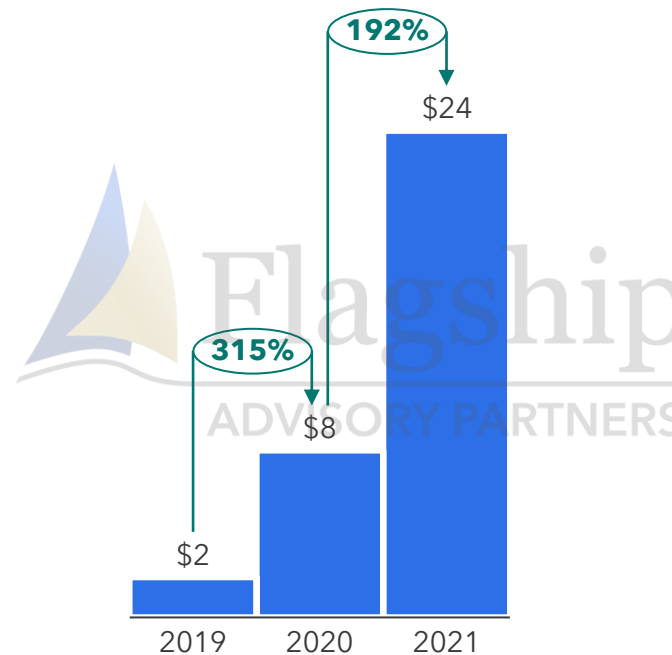


Based on data gathered by the CFPB from the top five U.S. BNPL lenders, the U.S. BNPL market as of 2021 was small but growing ~200% per year.

New U.S. BNPL Loans
(in mil.)

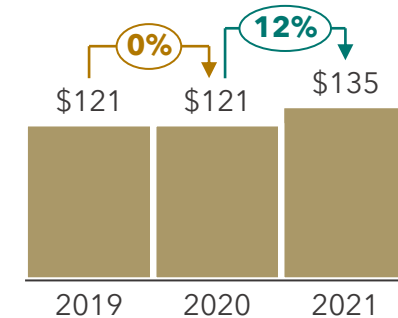


U.S. BNPL Gross Merchandise Volume
(in \$ bil.)



U.S. Avg. Individual BNPL Loan Size
(in \$)

In 2021, **89% of BNPL repayments were made using debit card**. Credit represented 10% of loan repayments.



51% of U.S. BNPL volume is from apparel merchants, but BNPL is rapidly gaining adoption in other retail categories.

U.S. BNPL Gross Merchandise Value per Merchant Vertical (in \$ bil.)

Merchant Vertical	2019		2020		2021		% Mix Change '19-'21	CAGR '19-'21
	GMV \$bil.	% of Total	GMV \$bil.	% of Total	GMV \$bil.	% of Total		
Apparel	\$1.34	66.1%	\$4.74	57.0%	\$12.43	50.5%	-15.6%	+205%
Personal Effects ¹	\$0.09	4.5%	\$0.72	8.7%	\$2.76	11.2%	+6.7%	+454%
Mass Market ²	\$0.13	6.5%	\$0.92	11.0%	\$2.65	10.8%	+4.3%	+351%
Beauty	\$0.29	14.0%	\$1.07	12.8%	\$2.01	8.2%	+5.8%	+163%
Other ³	\$0.12	5.7%	\$0.26	3.1%	\$1.49	6.1%	+0.4%	+252%
Home	\$0.03	1.7%	\$0.29	3.5%	\$1.11	4.5%	+2.8%	+508%
Travel/Entertainment	\$0.01	0.5%	\$0.06	0.7%	\$0.8	3.2%	+2.7%	+794%
Services ⁴	\$0.01	0.5%	\$0.1	1.2%	\$0.64	2.6%	+2.1%	+700%
Automotive	\$0.002	0.1%	\$0.03	0.4%	\$0.27	1.1%	+1.0%	+1.062%
Health	\$0.01	0.2%	\$0.09	1.1%	\$0.23	0.9%	+0.7%	+380%
Everyday ⁵	\$0.003	0.2%	\$0.04	0.5%	\$0.23	0.9%	+0.7%	+776%

¹Includes: Games & Hobbies, Electronics, Fitness/Sporting Equipment & Jewelry

²Includes: Wholesale, Department Stores, General Goods, Merchandise & Retail

³Includes: Deals & Miscellaneous

⁴Includes: Education, Legal Fees, Finance, Insurance, Non-profit & Websites

⁵Includes: Utilities, Transportation (Fuel, Non-hardware expenses) & Groceries

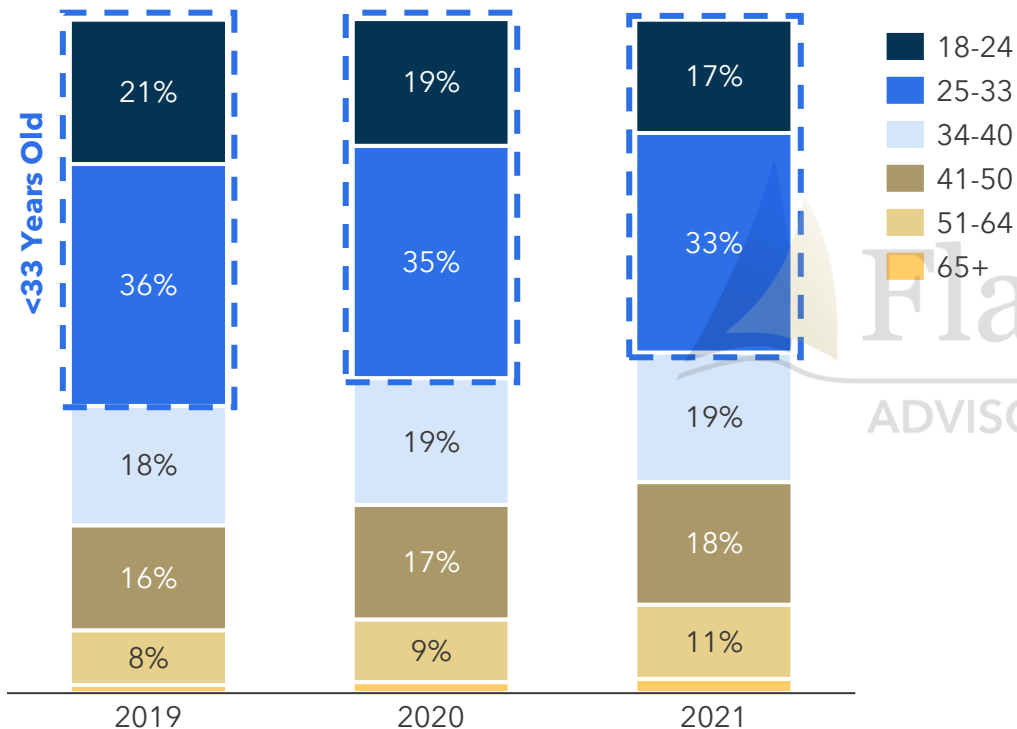
Notes: Data from CFPB's U.S. survey with Affirm, Afterpay, Klarna, PayPal, and Zip

Source: Flagship Advisory Partners' analysis of Consumer Financial Protection Bureau's "Buy Now, Pay Later: Market Trends and Consumer Impacts Report", released September 2022, analyzed November 2022

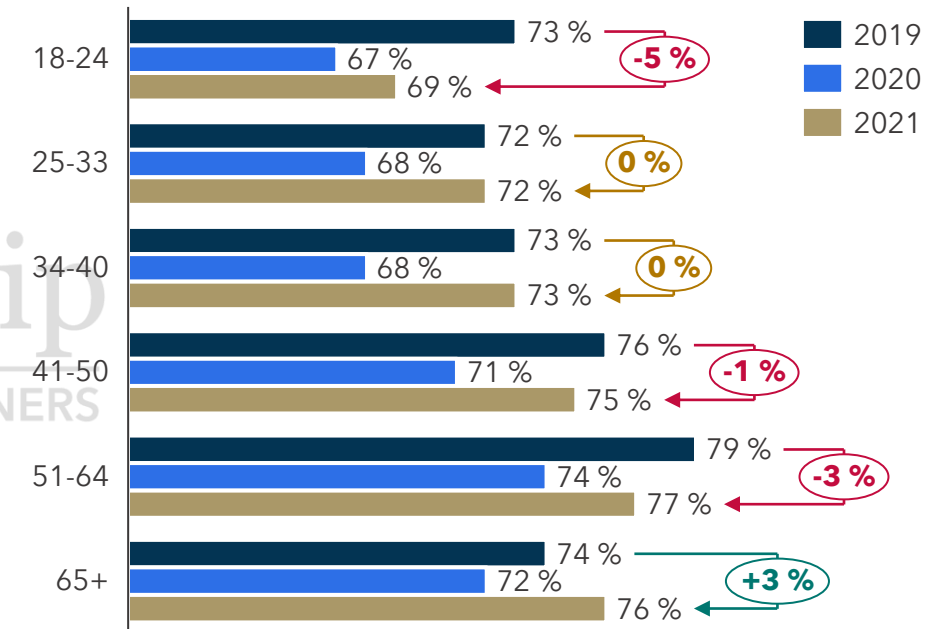
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50% of U.S. BNPL users are 33 are younger, but the share of older users has increased. Approval rates are high overall.

U.S. BNPL Borrower Base by Age Cohort
(% of total borrowers)

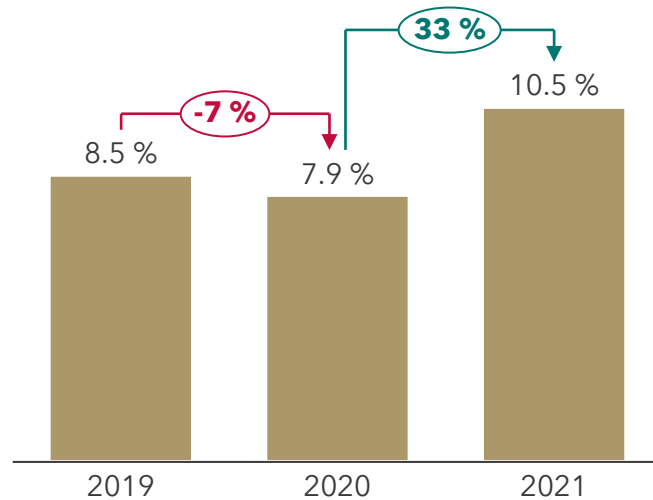


U.S. BNPL Credit Approval Rates by Age Cohort

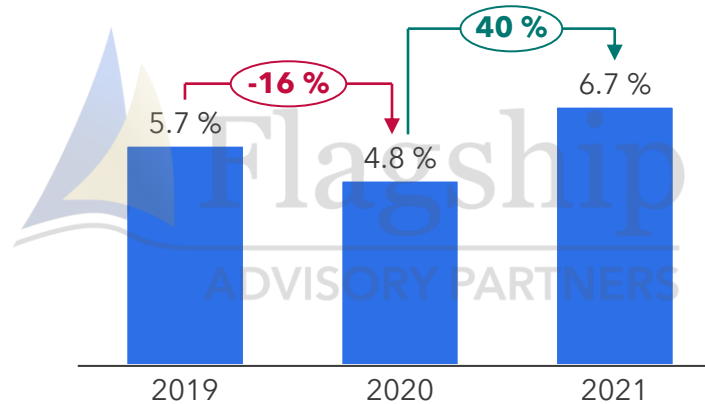


US BNPL late fee revenue increased significantly in 2021.

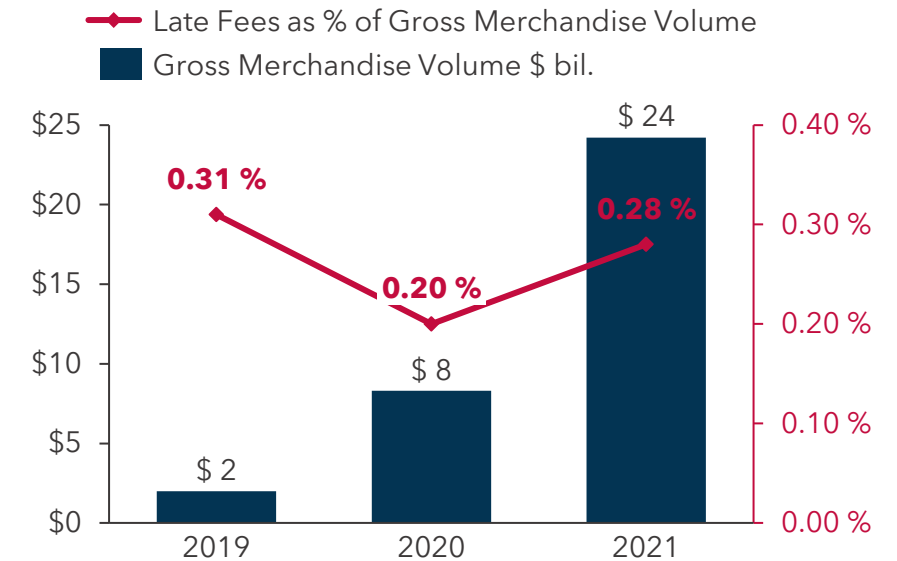
% of US BNPL Borrowers Charged 1+ Late Fees



% of US BNPL Loans Charged 1+ Late Fees



Late Fees as % of US BNPL Gross Merchandise Volume (\$ billions)



COMMENTARY FROM CSFB

- The recent growth in late fee rates indicates the usage patterns that could lead to borrower overextension caused by:
 - **Loan stacking:** borrowers taking out multiple loans from multiple providers
 - **Sustained usage:** continued BNPL consumption impacting non-BNPL payments

Notes: Data from CFPB's U.S. survey with Affirm, Afterpay, Klarna, PayPal, and Zip

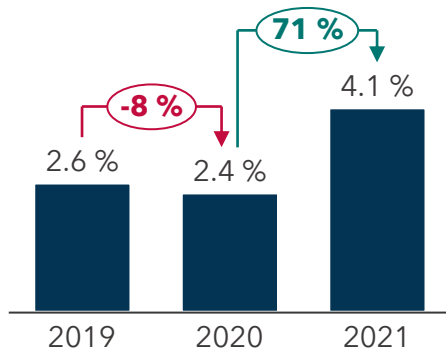
of borrowers and loans charged 1+ late fees divided by the total number of borrowers and loans

Source: Flagship Advisory Partners' analysis of Consumer Financial Protection Bureau's "Buy Now, Pay Later: Market Trends and Consumer Impacts Report" released September 2022, analyzed November 2022

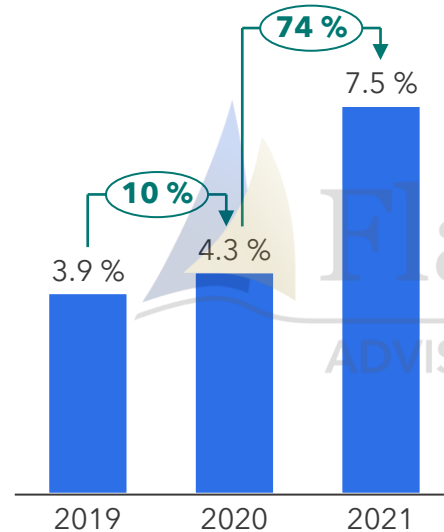
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BNPL delinquency rates have increased significantly; nearly doubling on a per borrower basis.

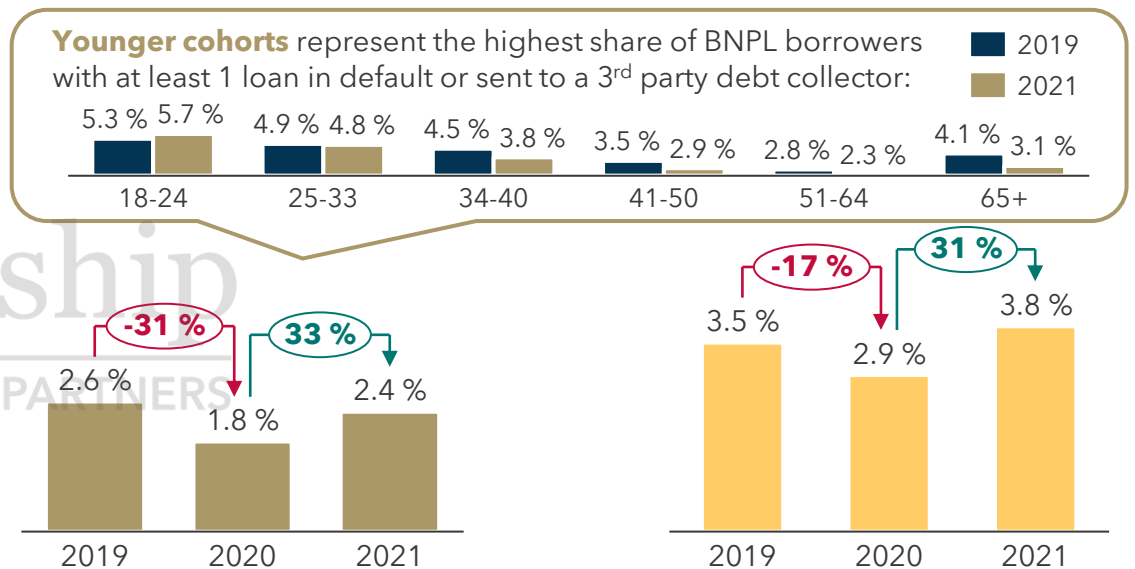
**U.S. BNPL Delinquency Rate¹
by # Loans**
(delinquent loans/total loans)



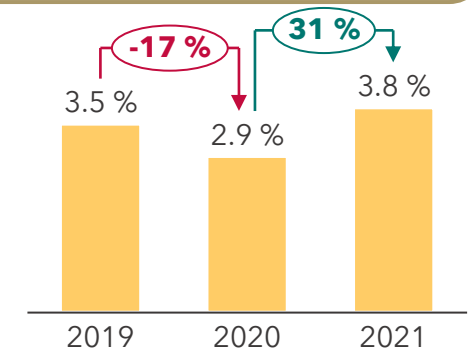
U.S. BNPL Delinquency Rate¹ by # Borrowers
(delinquent borrowers/
total borrowers)



% U.S. BNPL Loans Charged Off²
(loans charged off/total loans)



% U.S. BNPL Borrowers with Loans Charged Off²
(borrowers with at least 1 loan
charged off/total borrowers)



(1) Failed/declined loan repayment to BNPL lenders by end-user due to insufficient funds or credit

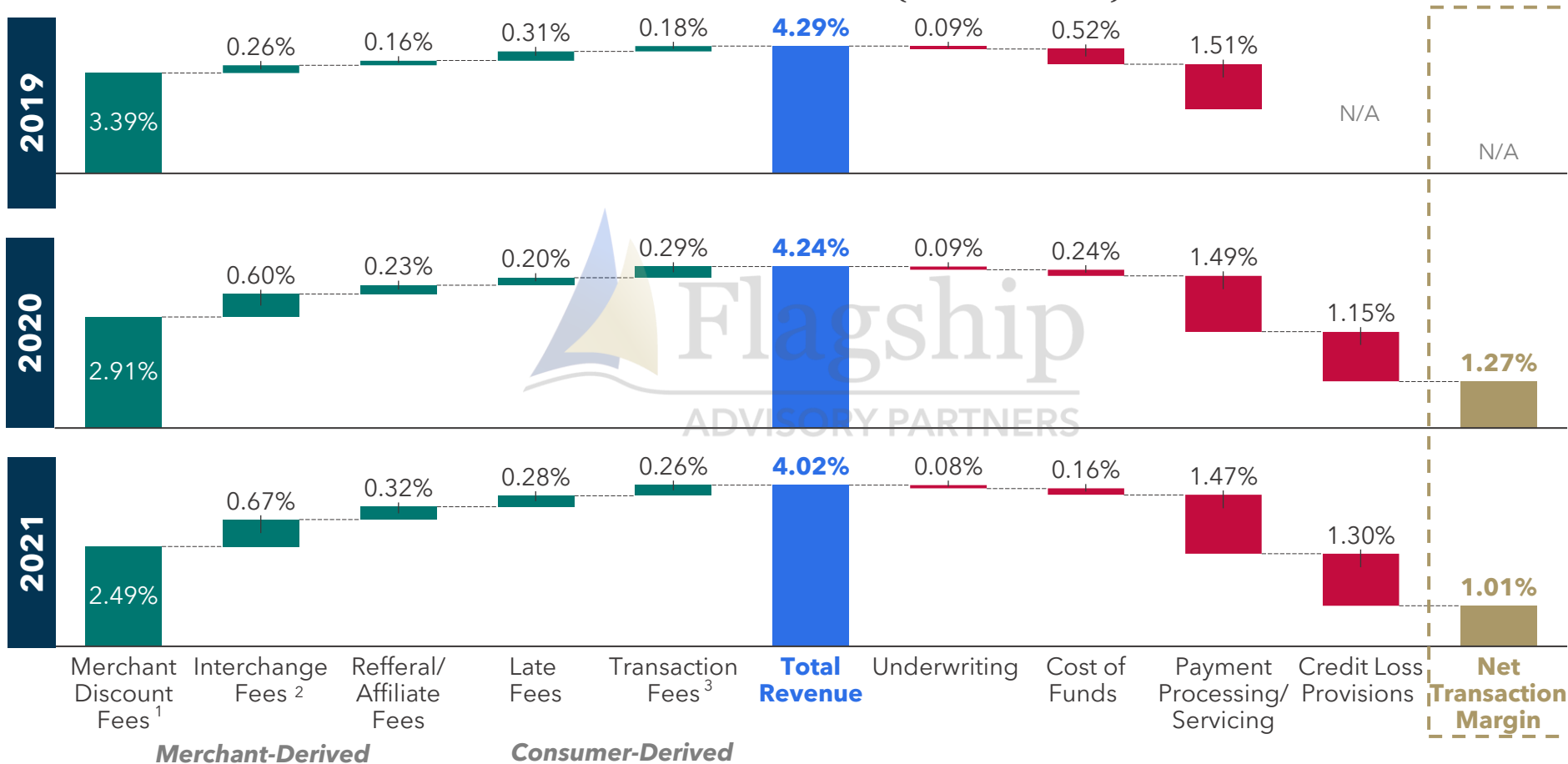
(2) Final stage of a loan's delinquency that a lender assigns with a low expectation of collection

Notes: Data from CFPB's U.S. survey with Affirm, Afterpay, Klarna, PayPal, and Zip

Source: Flagship Advisory Partners' analysis of Consumer Financial Protection Bureau's "Buy Now, Pay Later: Market Trends and Consumer Impacts Report" released September 2022, analyzed November 2022

BNPL issuer margins have decreased due to lower merchant discount fees, higher referral fees, and increased credit losses.

U.S. BNPL Aggregated Unit Margins: Total Revenue & Expenses (% of total GMV)



Net Transaction Margins decreased from 2020- 2021 based on 2 main drivers:

- Decline in Merchant Discount Fees (3.39% to 2.49%, '19-'21)
- Increase in Credit Provisions Losses (1.15% to 1.30%, '20-'21)

- (1) Per-transaction fees charged to merchants with whom the BNPL lender has a direct contractual relationship
- (2) The lender's share of standard card interchange fees charged to the merchant to process a loan that occurs on a BNPL lender-issued virtual debit or credit card
- (3) Fees collected from consumers for taking out a BNPL loan, specifically collected from customers who take out a loan from a non-partnered merchant via a lender-issued virtual card

BNPL lenders are attempting to push customers to use their centralized shopping apps (vs. acquiring customers from accepting merchants), although this “super app” strategy has not yet proven out among Western consumers.

PULL: Merchant Partner Acquisition Model

BNPL Lenders **pull** in customers through merchant checkouts



***Underwriting:** BNPL lenders use different data metrics (i.e., 1st time and/or low credit-score applicants) to underwrite higher-risk segments during the credit application stage. CFPB noted as a topic for discussion the absence of traditional “ability to pay” calculations during this underwriting process.

PUSH: App-Driven Acquisition Model

BNPL Lenders **push** customers to merchants through referral clicks



Facilitated by **single-use**, bank-issued **virtual cards** where BNPL lenders earn a portion of the **interchange fees** collected during the transaction

Benefits of an app-driven acquisition model:

- Facilitates direct consumer engagement along all customer journey touchpoints
- Any online merchant can accept BNPL without a contract
- Creates an additional source of revenue from virtual card transactions

But requires BNPL providers to drive customers to their apps (which can be challenging)

While the long-term outlook for BNPL is good due to strong underlying UX and customer value proposition, BNPL providers face clear near-term challenges on unit economics, credit risk, and increasing regulation.

U.S. BNPL Opportunities & Challenges (Based on CFPB's Report)



BNPL PLAYERS

- ✓ Increased uptake among older consumers
- ✓ Increased traction in less traditional merchant categories
- ✓ B2B
- ✓ Direct relationships with customers via centralized shopping app (albeit challenging to make successful)
- ✗ Increasing regulation
- ✗ Increasing credit risk
- ✗ Challenging unit economics (e.g., increasing cost of funds)
- ✗ Downward pressure on merchant discount rates



MERCHANTS

- ✓ Strong UX and customer convenience
- ✓ Customer access to credit proven to drive retail sales
- ✓ Declining cost of acceptance
- ✗ Competition from BNPL provider shopping apps
- ✗ BNPL providers likely to lower approval rates to manage credit risk
- ✗ Longer term provider supply risks due to challenging unit economics



CUSTOMERS

- ✓ Strong UX and convenience
- ✓ Additional regulation may increase customer transparency and reduce over-extension
- ✓ Convenience and price comparisons via BNPL provider shopping apps (potentially)
- ✗ BNPL providers likely to lower approval rates to manage credit risk
- ✗ Risk of debt overextension (lack of affordability checks)
- ✗ Late fee burden



TECHNOLOGY PROVIDERS

- ✓ Need for BNPL providers to reduce credit risk creates opportunities for risk management vendors
- ✓ Opportunities to integrate BNPL into other software (e.g., B2B BNPL)
- ✗ Margin-constrained customers (BNPL providers)

✓ Opportunities ✗ Challenges

Thank You!



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