

The Rise of Buy Now, Pay Later (BNPL)

1. Introduction

Buy Now, Pay Later (BNPL) is a modern payment solution that allows consumers to make purchases and pay for them in instalments over time, playing a significant role in the evolving fintech landscape by offering flexibility and convenience in financial transactions.

The objective of this case study is to explore the rapid growth of Buy Now, Pay Later (BNPL) services and assess their impact on consumer spending habits and credit risk within the fintech sector.

2. The BNPL Business Model



You'll often see BNPL payment plans available when you check out online. For in-store shopping, providers usually offer virtual cards that can be downloaded from the provider's mobile app, saved to a mobile wallet and used at the register.

- So how does it work? Let's overline the typical process from the customer's perspective:
- At checkout, online or in-store, consumers are given the option to pay with BNPL.
- Then, they'll typically have to fill out a short application, providing information like name, address, email address, date of birth, phone number, and Social Security number.
- The purchase amount is divided into equal instalments, usually four or fewer, with the first instalment paid at the time of purchase.
- The remaining instalments are automatically charged to the consumer's debit or credit card

on a schedule, typically every two weeks or monthly.

- Many BNPL providers do not charge interest or fees for on-time payments. However, late fees or deferred interest may apply if payments are missed or delayed.

Most Widely Used BNPL Platforms



Source: Mordor Intelligence



BNPL companies generate revenue primarily through merchant fees for offering the service, interest charges on consumer instalments, and late fees for delayed payments.

3. Growth Trajectory and Market Penetration

The rising popularity of Buy Now, Pay Later services is underscored by the staggering growth of the market, which was estimated at \$753.53 billion in 2022 and is expected to reach around \$9.2 Trillion by 2032. This impressive expansion, with a compound annual growth rate (CAGR) of 29% from 2023 to 2032, highlights the increasing consumer demand for flexible payment solutions.

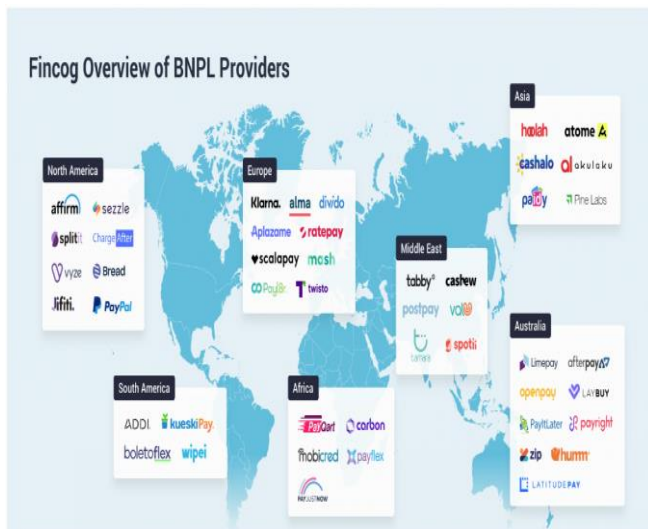
Global Buy Now Pay Later Market

Size, by Channel, 2022-2032 (USD Billion)



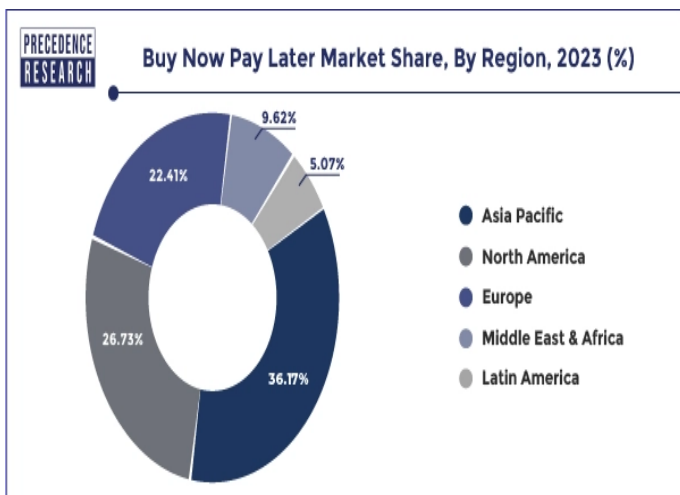
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Popular BNPL apps like Tabby, Klarna, AfterPay, and Tamara cater to this demand by offering the ability to purchase goods and services immediately and pay for them over time, making purchases more accessible and financially manageable.



4. Key Factors Driving BNPL Growth

- **Consumer Demand for Flexibility:** Shoppers appreciate the ability to manage their finances better by spreading out payments.
- **E-commerce Boom:** The rise of online shopping has fueled the demand for BNPL options at checkout.
- **Low-Interest Alternatives:** Compared to credit cards, BNPL services often provide a more cost-effective way to finance purchases.



5. Statistical Insights

Worldpay's Global Payments Report (2023):

BNPL transactions have seen significant growth globally, with an annual increase of over 30% in some regions. BNPL is increasingly popular in e-commerce, making up a substantial share of online transactions.

McKinsey & Company's Global Banking Annual Review (2023):

BNPL is expected to continue its rapid expansion, with projections indicating it could account for 5-10% of global consumer credit by 2025. Regulatory pressures and competition are anticipated to impact the growth trajectory.

TransUnion's 2023 Consumer Credit Trends Report:

BNPL usage is growing among younger demographics, with a notable increase in adoption among those aged 18-34. A rise in missed payments and delinquencies has been observed, highlighting potential risks for consumers and lenders.

Experian's Consumer Credit Review (2024):

BNPL usage has increased by 25% over the past year, with a focus on its impact on credit scores and financial health. There is growing concern about the cumulative impact of multiple BNPL plans on consumers' overall creditworthiness.

J.D. Power's 2023 Credit Card Satisfaction Study:

BNPL services are influencing traditional credit card usage patterns, with many consumers opting for BNPL to avoid high-interest rates on credit cards. Satisfaction levels with BNPL services vary, with a trend toward increasing consumer preference for flexible payment options.

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6. The great habit change:

- **Impact on Consumer Behavior :**

Less Debt and More Savings: The pandemic led to increased savings for consumers, with US government relief payments helping many Americans pay off debt, resulting in a \$116 million reduction in revolving consumer credit by January 2021. In the UK, the furlough scheme protected incomes, leading to a record savings rate of 19.9% in early 2021.

More Online Shopping: COVID-19 restrictions accelerated the shift to online shopping, with the UK's online sales share rising from 20% in 2019 to over 30% in 2020. BNPL transactions grew, accounting for 5% of the UK e-commerce market, with expectations to reach 10% by 2024. In the US, BNPL spending surged, with forecasts predicting 76 million BNPL users by 2024.

Gen Z and Millennial Dislike of Credit Cards:

In the UK, 25% of BNPL users are aged 18-24, while in the US, 36% of users are under 25. BNPL allows them to avoid credit card interest, with Afterpay saving US customers up to \$459 million in fees in 2021.

- **The Impact of BNPL on Retailers**

The pandemic drove retailers to adopt BNPL options, leading to increased sales and customer loyalty. Afterpay alone is projected to bring \$4.5 billion in net benefits to retailers in 2021, including \$8.2 billion in incremental sales and \$590 million in cost savings.

The Question of No Surcharge Rule: BNPL services charge merchants fees (e.g., Afterpay at 4%, Zip Co at 3%), but retailers cannot pass these costs to consumers via surcharges. If surcharges were allowed, 50% of BNPL users would switch payment methods, while 10% might abandon the purchase altogether.

7. Advantages and Disadvantages:

Pros

- Convenient way to pay for purchases over time

- Frequently no interest or lower interest rates than credit cards
- Good credit/high credit score not necessary to qualify
- Fast approval

Cons

- Payments can be hard to track
- Missing or late payments result in late fees and may damage credit score
- No rewards or cash back earned on purchases
- Payments may continue even if item is returned

8. Tips to avoid overspending with buy now, pay later

- **Set up a budget:** Check your monthly cash flow and consider upcoming expenses before committing to BNPL.
- **Don't buy on impulse:** Avoid buying items you don't need to prevent regret from ongoing payments.
- **Read the terms carefully:** Understand BNPL terms, including fees and repayment schedules, to avoid extra charges.
- **Limit the number of concurrent plans:** Coordinate with others to keep track of multiple BNPL plans and avoid overspending.

9. The Importance of Ethical Debt Collection

As BNPL continues to evolve, ethical debt collection must be at the heart of the business model to ensure long-term sustainability and consumer trust.

1. Protecting Consumers

Ethical debt collection practices safeguard consumers from aggressive and harmful collection tactics, which can lead to stress, mental health issues, and financial hardship. Key aspects include:

- **Transparency:** Clear communication about repayment terms and conditions.
- **Fair Treatment:** Respectful and humane handling of consumers who fall behind on payments.

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- **Supportive Measures:** Offering financial counseling and flexible repayment options for those struggling to meet their obligations.

2. Enhancing Brand Reputation

Companies that prioritise ethical debt collection are more likely to build and maintain a positive brand reputation. This approach can lead to:

- **Increased Customer Loyalty:** Satisfied customers are more likely to continue using BNPL services and recommend them to others.
- **Positive Public Perception:** A commitment to ethical practices can attract positive media coverage and consumer advocacy support.

3. Regulatory Compliance

Ethical debt collection helps BNPL companies stay compliant with regulatory standards, avoiding legal repercussions and potential fines. This compliance is critical as regulators increasingly focus on consumer protection in the BNPL sector.

4. Reducing Default Rates

By treating customers fairly and providing them with the support they need, BNPL companies can reduce default rates. Ethical debt collection practices encourage:

- **Timely Payments:** Consumers who feel respected and understood are more likely to make timely payments.
- **Improved Financial Health:** Providing financial education and support can help consumers manage their finances better, leading to fewer defaults.

10. Regulations on BNPL in the UK:

- The UK is introducing tighter BNPL regulations, with a consultation document suggesting less stringent rules than previously proposed.
- Proposed rules include treating customers in financial difficulty fairly and allowing complaints to the Financial Ombudsman Service.
- Regulations may start in late 2022 or 2023.

11. Conclusion

The future of BNPL is bright, with significant potential for growth and innovation. However, the path forward is fraught with challenges. Companies that can navigate intense competition, regulatory scrutiny, and economic fluctuations will thrive, while those that cannot may face financial difficulties. For consumers, the continued evolution of BNPL promises greater flexibility and convenience in managing their purchases.

By staying attuned to market trends, investing in robust risk management and technological advancements, and prioritising ethical debt collection, BNPL companies can secure a prosperous future. As the industry evolves, both consumers and providers stand to benefit from the dynamic and adaptable nature of BNPL services. Ethical debt collection is not just a moral imperative; it is a strategic advantage that can drive long-term success in the competitive BNPL landscape.

12. References:

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