Buy Now, Pay Later
Understanding the demand and opportunity behind the hype
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State of the market

Rethinking Financial Health through BNPL Services

Uncertain conditions over the last decade have pushed consumers to focus more on their financial health. Consumers are looking to have control over their finances including improving their credit. The economic fallout of the COVID-19 pandemic and the continued rise of digital solutions has only heightened this attention.

These needs have positioned Buy Now Pay Later (BNPL) services, financing large purchases through lending at the point-of-sale, as a very appealing option for a number of consumers.

BNPL solutions have gained popularity as streamlined, flexible payment options that allow consumers to pay for large purchases or that would otherwise stretch their typical cash flow. With more consumers interested in conserving their savings but also shopping more online, it’s not surprising, to see that 64% of BNPL consumers have used these services more since the pandemic began.

72% of Americans say “I am more focused on my financial health and how to protect myself these days”\(^1\)

45% of US adult BNPL consumers said they used these services to split up purchases that otherwise wouldn’t fit into their budget\(^2\)

56% of Americans have used a buy-now-pay-later service, and 36 percent of those who use it do so frequently—at least once a month

Source: The Ascent Survey of 2,000 American Adults, conducted March 10, 2021 (a Motley Fool Service)

1. Mastercard Health And Wellness Thought Leadership, December 2020
2. C&R Research
Understanding the BNPL consumer

Although most popular among younger generations, BNPL is growing across age segments to help manage cash flow.

- Younger consumers lacking long credit histories are looking for new ways to borrow for purchases and are averse to taking on more debt as they work to reduce existing debts, such as college loans.

- However, point-of-sale financing appeals not only to consumers with thin credit files, but to well-established consumers as well. Nearly two-thirds (65 percent) of receivables originated by POS lenders are from consumers with credit scores higher than 700.

### Usage of BNPL by Age Group

<table>
<thead>
<tr>
<th>Age</th>
<th>Used BNPL¹</th>
<th>Growth²</th>
</tr>
</thead>
<tbody>
<tr>
<td>18-24</td>
<td>61%</td>
<td>62%</td>
</tr>
<tr>
<td>25-34</td>
<td>60%</td>
<td>28%</td>
</tr>
<tr>
<td>35-44</td>
<td>61%</td>
<td>21%</td>
</tr>
<tr>
<td>45-54</td>
<td>53%</td>
<td>26%</td>
</tr>
<tr>
<td>55+</td>
<td>41%</td>
<td>98%</td>
</tr>
</tbody>
</table>

¹. As of March 2021
². Between July 2020 and March 2021

While many purchases made with BNPL options are discretionary, such as electronics and clothing and fashion, it also plays a role in covering basic household purchases:

### Most popular uses of BNPL

<table>
<thead>
<tr>
<th>Purchase</th>
<th>Used BNPL¹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Electronics</td>
<td>48%</td>
</tr>
<tr>
<td>Clothing and fashion items</td>
<td>41%</td>
</tr>
<tr>
<td>Furniture or appliances</td>
<td>39%</td>
</tr>
<tr>
<td>Household essentials</td>
<td>33%</td>
</tr>
<tr>
<td>Groceries</td>
<td>24%</td>
</tr>
<tr>
<td>Books, movies, music, or games</td>
<td>23%</td>
</tr>
<tr>
<td>Others</td>
<td>9%</td>
</tr>
</tbody>
</table>

Consumers are widely adopting POS financing, and 71 percent of adopters have used it more since the beginning of the pandemic. Most are using this method to break up larger payments so they can better manage their budget, while some are just looking for access to a different type of credit:

### Why consumers are using BNPL

<table>
<thead>
<tr>
<th>Reasons for using BNPL service</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>To make purchases that otherwise wouldn't fit in my budget</td>
<td>48%</td>
</tr>
<tr>
<td>To avoid paying credit card interest</td>
<td>37%</td>
</tr>
<tr>
<td>To borrow money without a credit check</td>
<td>25%</td>
</tr>
<tr>
<td>To safeguard personal data</td>
<td>21%</td>
</tr>
<tr>
<td>I don't like to use credit cards</td>
<td>19%</td>
</tr>
<tr>
<td>My credit cards are maxed out</td>
<td>17%</td>
</tr>
<tr>
<td>I can't get approved for a credit card</td>
<td>14%</td>
</tr>
<tr>
<td>I don't have bank accounts</td>
<td>8%</td>
</tr>
<tr>
<td>Some other reason</td>
<td>6%</td>
</tr>
</tbody>
</table>

1. McKinsey & Company, Buy now, pay later: Five business models to compete
2. The Ascent Survey of 2,000 American Adults, conducted March 10, 2021 (a Motley Fool Service).
3. MASTERCARD HEALTH AND WELLNESS THOUGHT LEADERSHIP, DECEMBER 2020
POS financing is the fastest-growing payment alternative in North America. Now is the time for Banks, Fintechs and Merchants to act.

Growth in today’s BNPL landscape is being driven by fintechs that are building end-to-end consumer experiences akin to online marketplaces. This approach is quickly building stickiness with consumers, driving repeat behavior. Traditional financial institutions may be at risk of disintermediation from the point of purchase and miss out on opportunities to acquire and retain new, younger consumers for future growth.

For merchants, providing choice of payment options is critical as consumer spending habits change. Merchants are already seeing value in these solutions, as most POS financing options enhance cart conversion, increase average order value, and attract new younger consumers. Merchants that have long sought to win consumers’ loyalty by offering private label credit cards (PLCC) are also seeing value in integrating BNPL into the checkout experience to attract new consumers not currently shopping with them, or to offer financing for a specific purchase without requiring consumers to acquire a new card.

**BNPL solutions are proving to be a sales enabler for merchants**

- **+45%** of BNPL users said they used these services to split up purchases that otherwise wouldn’t fit into their budget.¹

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1. Mastercard New Payments Index 2021
2. Strawhecker Group, 2021

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### Point-of-sale financing is growing faster than other unsecured lending, expected to be $182B by 2023

**Outstanding balances for unsecured lending products, $ billion**

<table>
<thead>
<tr>
<th>Year</th>
<th>Point-of-sale financing</th>
<th>Personal loans</th>
<th>Private-label credit cards</th>
<th>General-purpose credit cards</th>
</tr>
</thead>
<tbody>
<tr>
<td>2016</td>
<td>1,029</td>
<td>371</td>
<td>1,171</td>
<td>268</td>
</tr>
<tr>
<td>2019</td>
<td>1,231</td>
<td>404</td>
<td>1,211</td>
<td>260</td>
</tr>
<tr>
<td>2020</td>
<td>1,114</td>
<td>387</td>
<td>1,088</td>
<td>271</td>
</tr>
<tr>
<td>2023</td>
<td></td>
<td></td>
<td>1,369</td>
<td>178</td>
</tr>
</tbody>
</table>

**CAGR, 2020-23 %**

- Point-of-sale financing: 18 to 20%
- Personal loans: 8 to 10%
- Private-label credit cards: -2 to 0%
- General-purpose credit cards: 5 to 6%

Source: McKinsey & Company, Buy now, pay later: Five business models to compete

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However there are some hurdles to even more consumer adoption

- **83%** of BNPL users wish it was accepted by more businesses².
- **20%** of BNPL users believe their service would take advantage of them².
BNPL Models

There are several ways in which buy now pay later solutions are being delivered and used today, and not only as another “loan” vehicle. Indeed, as consumers are demonstrating, BNPL has features that appeal to consumers at all ages, incomes, and credit scores. McKinsey has classified a variety of models and here we focus on three.

Card-linked financing: This model enables consumers to use their existing payment card to initiate an installment loan, with no need to sign up for a new service. Available for both online and in-store purchases, it has been mainly offered as post-purchase installments, but can also be offered pre-purchase, allowing consumers to convert an upcoming purchase with a merchant into an installment. Typically, the card issuer will offer a discounted APR rate for this service.

Short-term off-card financing: Younger consumers are adopting shopping apps that utilize Short-Term Off-Card Financing, often referred to as the “Pay in 4” model. In this construct, shoppers make smaller-ticket purchases (under $250) and pay it down in six weeks, primarily from their debit cards. Most originations stem from higher-margin discretionary spend categories, such as apparel and footwear, fitness, accessories and beauty.

Long-term off-card financing: Older or more affluent consumers are also drawn to BNPL services. Merchants in higher-ticket categories, such as electronics, furniture, fitness equipment, and travel, have witnessed strong growth --80 to 100 percent CAGR-- from consumers using Long-Term Off-Card Financing solutions (often with an APR) for purchases averaging about $800. For merchants that enjoy higher gross margins, but also incur higher acquisition costs, integrating these solutions can be advantageous.

Implications for Financial Institutions and Fintech Players

Rising interest in BNPL solutions is a call to action for the financial services industry to leverage their trusted position and enable new tools. But failure for banks to act could be costly, as an estimated $8B to $10B in annual revenues have already diverted away to Fintechs.¹

Financial institutions and Fintechs can offer a holistic engagement and acquisition strategy with financing tools for before, during, and after the point of purchase, especially has financial apps are used frequently by most consumers. BNPL can also be integrated into a purposeful graduation strategy to enhance their relationship with current customers and appeal to new segments.

Risks of Inaction

- Missed revenue opportunity from new payment volume
- Missed acquisition of new, younger consumer segments to other non-traditional lending platforms
- Lack of brand presence at the point of payment

Opportunities

- Leverage existing relationships with consumers and trusted brand positioning to personalize installment offers and create a seamless acquisition experience, especially from banking apps
- Utilize BNPL as a tool to engage younger demographics, promote financial wellness and graduate relationship over time into higher yield products like credit
- Create touchpoints with consumers throughout the purchasing journey to introduce other value added services like rewards and benefits
- Partner with other Fintechs that can increase speed to market

¹. Mastercard Internal Study
Implications for Merchants

BNPL offers many advantages for merchants including higher conversion rates, average order value, and increased access to new consumer segments. But they can also have some risk such as challenging integrations, additional fees, operational pressures and lack of consumer trust that can impact the overall ROI for a merchant. Hence, carefully choosing a strategy can ensure that benefits are maximized and risks are minimized.

Risks

- Costly system integration and impact to UX flow
- Difficulty retaining control over the customer and their shopping experience
- Increased operational costs related to customer service, chargebacks and processing fees
- Liability exposure on fraud, late payments and delinquency
- Reputational concerns around transparency of loan terms and repayment through BNPL providers

Opportunities

- Generate incremental customer acquisition and revenue from various customer segments
- Drive ROI by displaying relevant short-term and long-term installment offers at checkout on high-ticket items or to first-time buyers
- Minimize operational costs by integrating BNPL solutions into existing payment infrastructure
- Promote trust and financial wellbeing through transparent installment offers with responsible lending terms
Introducing Mastercard Installments.

Reinventing Installments to give consumers more payment choices wherever they shop

Mastercard Installments is a new program that enables banks, lenders, BNPL players and wallets the ability to offer BNPL experiences at scale, reaching merchants across the entire Mastercard acceptance network

- **No additional integration for merchants:** Existing integration into Mastercard’s trusted network enables merchants to instantly support secure BNPL payments backed by the security and peace of mind that comes with Mastercard.

- **Flexible and trusted for consumers:** Provides a ubiquitous way to pay online and in-store through equal installments, without the need for a debit, credit or prepaid card, across Mastercard’s vast acceptance network.

- **Scale and simplicity for BNPL providers:** The Mastercard Installments program provides the framework, trust, and optional services to streamline a BNPL strategy, all without the cost of building acceptance relationships merchant by merchant.

For more information, talk to your Mastercard representative or visit www.mastercard.com/installments

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