Buy Now, Pay Later, Consumer Preference and Collections Outlook

Consumer adoption of Buy Now, Pay Later (BNPL) products skyrocketed in the past year, fueled in part by an increase in online shopping due to Covid-19, indicating changing credit and payment preferences that are poised to outlive the pandemic. In this report we use TrueAccord data about debt trends, repayment performance and consumer preferences to gain insight into the BNPL phenomenon and its long-term outlook.

Highlights:

- Since the onset of the pandemic, younger consumers (18-34) are going into collection for lower amounts, reflecting an uptick in BNPL usage
- BNPL debts see higher and faster repayment rates than similar-sized credit card debts
- Installment payment plans are popular with consumers for both new loans and repayment of existing loans

The Demand

According to the CFPB's 2021 Consumer Credit Card Market Report, the pandemic accelerated the downward trend in credit card approval rates for those looking to open a new line of credit. In the midst of economic uncertainty, credit card issuers tightened their underwriting process, leading to an approval rate of 36% in 2020, down from 41% in 2019. Simultaneously, customer satisfaction with credit card issuers declined over the past year due to increasing financial uncertainty, combined with factors such as high interest rates, shrinking credit limits and changing customer demands.

In California alone, according to a report from the Department of Financial Protection and Innovation (DFPI), traditional consumer loans were down 41% from 2019-2020 while online loans over the same period increased almost 1,600% primarily driven by BNPL products. In fact, the report shows that 91% of all consumer loans originated in California in 2020 came from the top six BNPL lenders and an estimated 44% of all Americans have tried a BNPL product.

BNPL lenders like Affirm, Klarna, and Afterpay allow consumers to split a purchase from any of their merchant partners into a number of installments at the point-of-sale, then repay the loans through debit or credit cards, usually set up as automatic payments. BNPL products are marketed directly on the merchant's website where at the time of check out a customer can select to use the BNPL product to purchase or even rent whatever goods or services they wish to purchase.

BNPL companies implement innovative technology and features to drive customer experience and retention throughout the process, not only for the BNPL lenders but for the merchants who offer their customers the option to use BNPL products. Merchants like BNPL products not only because more consumers purchase their goods and services, but also because they lead to larger purchase amounts, with an average order value increase of 20% to 35% and cart conversion increase of 20% to 85%.

The Product

BNPL hits a sweet spot with consumers looking for an alternative to credit cards. BNPL products are convenient and easy-to-use. They are seamlessly integrated into the eCommerce sites of the merchant so that customers can evaluate the BNPL product and terms during the check out process. Perhaps more critical for consumers, BNPL gives consumers an accessible credit option that doesn't rely on credit scores. With zero interest or upfront fees, BNPL products give consumers a new way to manage cash flow with smaller balance sizes and flexible repayment plans. For consumers who do not have enough money in the bank now for a purchase, the ability to make a small upfront payment with a set number of future payments in order to access the goods or services they need can help them to manage their budgets. This behavior, coupled with neobank-driven use of debit cards for day-to-day spending, may be signaling a shift in consumer approaches to cash flow and credit management that will continue to favor BNPL in the future.

Default & Recovery

Some consumers will at some point default on these loans, just as they would with credit cards. According to TrueAccord data, the average BNPL balance in collection is less than 8 times the average credit card debt, making the consumer's financial responsibility smaller and more manageable than the larger credit card balances.

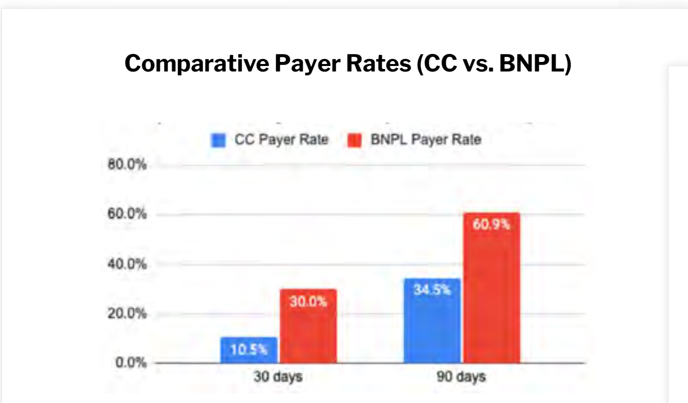
Defaulting on a BNPL product can still have adverse effects that default and charge off management will help consumers avoid or at least minimize. While BNPL products do not use the same credit underwriting factors as credit cards, some BNPL lenders do report missed payments to the credit bureaus which could affect credit score just the same. While others may not report to the credit bureaus, late payments can still impact consumers by overdrafting from accounts set up for automatic payments, the inability to use BNPL accounts for future transactions and, in some cases, late fees. Flexibility is crucial in order to minimize those adverse effects when servicing these accounts as they fall behind: highly customized, longer-term payment arrangements are used by 49% of all consumers repaying balances via TrueAccord. A repayment schedule that aligns to periods when consumers are most likely to have cash available leads to a marked 45% drop in payment plan drop-off, and low-friction tools to delay or reschedule individual payments reduce drop off by an additional 13%.

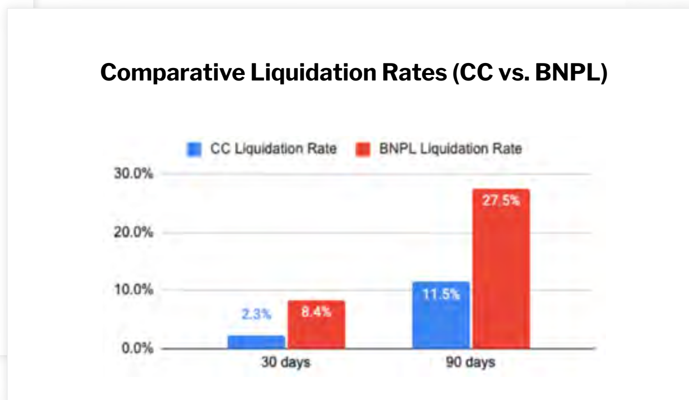
BNPL providers obsess over creating a positive customer experience, even in collections. They are faced with an ultra-competitive customer acquisition environment: according to a TrueAccord survey of BNPL users, the typical BNPL customer used up to six different BNPL providers in the last 12 months. Retaining consumers, therefore, becomes a priority in the whole customer lifecycle, even post-delinquency. TrueAccord achieves this in three major ways: first, by offering a variety of contact channels. Offering texting in collections, for example, is trickier than in other product areas due to compliance limitations, but adding it on top of email-only communications shows significant repayment improvements of more than 230%. Second, retention is boosted by offering a highly flexible repayment strategy, as mentioned above, allowing consumers to customize their plans according to their needs and budgets and by implementing settlement offers or discounts. Targeting repayment strategy outreach, based on TrueAccord data, leads to 12% higher repayment rates in the first 60 days. Finally, identifying and encouraging consumers who are motivated by regaining access to their BNPL service, using the correct combination of content and communication channel, increases repayment rates by 11%.

BNPL defaults are different from credit card defaults in various ways, and it's no surprise that their engagement pattern with our system differs as well. BNPL customers are digitally savvy, their average balance in default is lower, and due to BNPL's intense focus on experience and reacquisition, they reach TrueAccord sooner to allow our process to kick in and get them back on track faster and with less friction (60 days for BNPL vs. slightly over a year for the average credit card account). Consumers also tend to prioritize lower balance accounts first when repaying their debt.

As consumers demonstrate their [preference for digital-first financial services], engagement rates post-default continue to be on the rise. Based on TrueAccord engagement and repayment data, beginning with initial correspondence, the email open rate for BNPL customers in debt is 32% higher than for like-size credit card accounts, with a nearly 40% higher click rate for BNPL vs. credit card accounts. This is the result of digital-only acquisition and servicing in pre-default, and it plays well with our digital- and mobile-first debt repayment product.

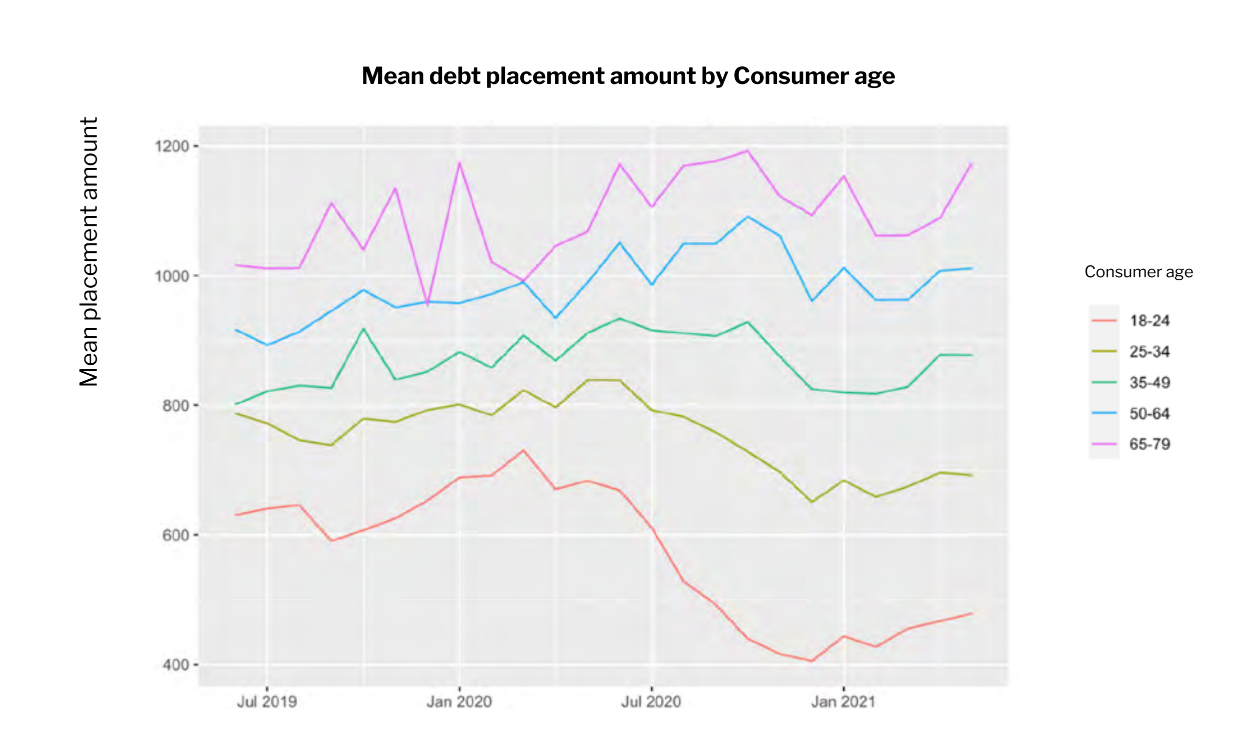
Higher engagement leads to better repayment rates. According to TrueAccord data, the percent of BNPL customers who make a payment is more than double the like-size credit card accounts at 30 days post placement and 50% higher at 90 days. The liquidation rate or repayment rate for BNPL accounts is 2.5 times that of credit cards at 30 days post placement and almost double at 90 days.





These are encouraging numbers for retention-focused BNPL providers. Having gone through several millions of defaulted BNPL accounts, TrueAccord's system can now customize a contact and repayment strategy for individual consumers in a way that gets them back on track sooner, leading 60.9% to make some sort of payment in the first 90 days. Coupled with our ability to identify consumers who are eager to reactivate their account and to offer flexible repayment plans that consumers stick with, defaulted BNPL accounts become a strong avenue for reduced churn and retention. TrueAccord also doesn't add any fees or interest on top of defaulted balances, so consumers' financials aren't harmed further by going into default.

The Outlook



Debt types and payment preferences are changing – traditional credit card debt is being supplanted by BNPL, especially with younger consumers. According to TrueAccord data, since the onset of the pandemic, younger consumers (18-34) are going into collections for lower amounts, reflecting an uptick in lower-value BNPL account defaults, though not necessarily higher default rates than credit cards. The prevalence of BNPL accounts in default reflects its growth as a share of eCommerce payments in general. Since BNPL debts see higher and faster recovery rates, this trend is actually beneficial for consumers in debt and BNPL providers alike. Consumers can rely on BNPL products for short-term cash flow management as well as an easy, flexible and affordable way to get back on track when they have over-committed. Because companies originating the vast majority of BNPL balances are our clients, TrueAccord can offer a broad view of the consumer's overall debt load that may not appear on their credit report, allowing them to manage their repayment in a way that works for them. This further strengthens BNPL options. Consumer demand for this credit product has caused even traditional banks and credit card issuers to start adding BNPL-like financing options to stay competitive and retain customers looking for alternative payment options.

When compared to high-interest, high-balance credit card alternatives, the BNPL installment pay plan provides a popular alternative. But BNPL can get even better. BNPL is an opportunity for financial service providers to design a new, more inclusive credit and payments network that works for consumers, rather than against them. If more BNPL providers report on-time payments to credit bureaus, low balance first-time purchases could help build credit files, especially for those without access to credit, while helping consumers with cash flow management issues to spread out payments over a time. With their focus on a seamless user experience and customer retention throughout the full life cycle of a BNPL account (including those in default), BNPL companies are an attractive financial services option for consumers and it's no wonder use of these products continues to rise.

About the Data:

TrueAccord is an intelligent, digital-first collections and recovery platform that collections leaders across industries trust to drive breakthrough results while delivering a superior consumer experience. We developed this report to understand trends in consumer payment preferences, specifically around BNPL usage and repayment. All data featured in this report is proprietary, aggregated, and anonymized data from TrueAccord, based on our work helping more than 16 million consumers of major banks, issuers, eCommerce companies, and direct lenders since 2014.

TrueAccord