BUY NOW PAY LATER

Buy Now Pay Later (BNPL) is acclaimed as one the great financial innovations of the last decade, 'successful' due to unfulfilled demand for unsecured consumer lending.

BNPL apps exploit legal loopholes or passive legal positions in many countries – yet these products lend consumers money, and consumers will default.

BNPL is not new, it has 300-year history in Europe and 250 years in USA, building apps is a new twist on a very old idea.

The last successful BNPL 'phase' was in 1980s, destroyed by rapidly rising interest rates.

TREASURY REGULATION OPTIONS

Australian government released options to regulate BNPL app 'industry' and is seeking opinions from any Australian interested in BNPL.

Regulation has three potential options –

Option 1 – Strengthening the BNPL Industry Code and introducing an affordability test
Option 2 – Requiring BNPL apps to hold an Australian credit licence and complying with reduced regulation under the Credit Act
Option 3 - Regulating BNPL apps under the full Credit Act

Treasury suggests several supplementary reforms, notably:

- an enhanced role for ASIC as regulator of BNPL, with extended ASIC funding arrangements
- the Reserve Bank of Australia (RBA), payment regulator, has suggested changes to no-surcharge rules could improve competition and efficiency

This submission only supports Option 3, with additional added enforcement items to ensure full compliance by all BNPL apps and 'Copycat' providers especially across consumer issues, key service areas and KYC/AML.

BNPL Fintech apps have been totally unregulated for eight years preferring to exploit the regulatory arbitrage.

BNPL - SIMPLE TO USE

At its core BNPL is a simple appealing concept offering 'free' instalments.

Consumers make $100 purchase, in most cases $25 is required upfront then 3 'interest free' instalments of $25 over 6 weeks (14–42 day loan)

A $100 purchase earns $4-$6 in merchant revenue, late fees the other key revenue source.

Many BNPL apps are blended providers, also offering loans, lines of credit and fixed instalment loans. Yet all Fintech players are unregulated and unprofitable at a time of record low interest rates.

Since when is offering up to $20,000 loan or credit line not lending?

HOW IT WORKS

Consumers use a mobile app usually online to access split payments of small transactions.

BNPL apps provide full payment of merchants, less 3-6% with credit risk taken by BNPL provider.

Fintech start-ups like Afterpay Holland, Affirm and Klarna created this niche by developing the Application Programming Interfaces (API) & Software Development Kits (SDK) to make this happen.

BNPL MODELS

BNPL models vary, even major consulting groups do not agree on the definitions.

What is clear is BNPL has seven distinct variations.

1. Traditional BNPL instalments
2. Fintech online shopping apps
3. Virtual cards within mobile wallets
4. 'Off card' instalments
5. Rent to own instalments
6. High value transactions offering different terms
7. SME sales finance linked to instalments

All these models need to be fully regulated to ensure consumers are treated in a similar consistent manor.

AUSTRALIAN BNPL MARKET

There are over thirty BNPL apps trying to achieve scale.

Twelve BNPL platforms were floated on the ASX since 2013 all unregulated and unprofitable lending products.

Another 20 start-ups with ten prominent providers: Affirm, *Brighte, CreditLine, Deferit, FuPay, Klarna, Plenti, Roar, Inkpay, PayitLater*.

Established fully regulated players include ANZ Visa BNPL, CBA with StepPay, unsecured lender Humm, consumer lender Latitude with 'LatitudePay', NAB/Citibank, PayPal with 'Pay in 4' and Suncorp's Visa BNPL.

There is now a clear regulatory gap between fully regulated banks/financial players and totally unregulated Fintech apps. This gap needs to be closed and requires full regulation.

The nine ASX unregulated listed stocks and 20 start-ups make no profits.

Douugh
Fatfish*
Ioupay*
OpenPay
Laybuy (NZ)
Payright
Sezzle (US)*
Splitit (US, UK)*
ZIP,ZIP Money
*Operate offshore only

Affirm
Brighte
Block/Square/Afterpay/Clearpay
Butn (SME business)
BizPay
Cloudfloat (SME business)
Deferit bills
FuPay
Gimmie
HandyPay
Inkpay (tattoos)
Klarna
Limepay
MoulaPay (SME business)
PayitLater
Payo (restaurants)
Plenti
Quickfee (SME services)
Spenda (SME business)
Unlocked (SME business)

COPYCAT START-UPS

Of real concern are the BNPL ‘copycats’ in other sectors using the same unregulated loophole. This needs to be closed with some urgency as behaviour is predatory and totally uncontrolled.

SME LENDING

Butn - provides loan services to small business recently raised $20 million valuing the business at $80 million and hinted at IPO.

Other SME lenders include – *Cloudfloat*, *MoulaPay, Spenda* and *Unlocked*

agPay and *DelayPay* – Agriculture instalments.

Deferit - allows utility, telco, car registration or childcare bills into four instalment repayments.

Grapple – allows SMEs better cash flow management.

MrYum – Eat Now Pay Later – partnership with Afterpay for pub menus using QR codes.

Payo – provides BNPL loans to restaurants and consumers.

Quickfee - operates in SME and professional markets offering instalments to SMEs, accountants, and other professional groups.

PROPERTY & REAL ESTATE

Bricklet – real estate start-up breathlessly described itself as “dynamic micro-investing” platform *Bricklet* is providing buyers the opportunity to become an independent part owner of their chosen residential or commercial dwelling via BNPL.

Flexibond - allows rental bonds to be paid in instalments charging 32% interest - they say they are unregulated.

Frontya – allows home deposits to be enlarged with instalments.

Wefund – property development ‘disruptive technology’ to assist developers move projects forward rapidly and pay using instalments.

Tenanting, Safetynet – provide loan advances for renters at 5% a week.

Ownhome – claims to allow renters to buy their own home – all on 50 years plans!

Mybond/Splitpayments – BNPL for bond payments by renters.

SALARY ADVANCES

Beforepay a payday lender advancing wages who ‘only charges’ 54% - 65% yet claims to be unregulated. Others include: *FuCash, Instapay, MyPayFast, MyPayNow, PayActiv*, *PayTime, Wagepay* - with regulated Commbank AdvancePay.

BNPL REGULATORY ARBITRAGE - EXPLOITING LOOPHOLES

BNPLs exploit a thirteen-year-old loophole - the Australian National Consumer Credit Protection Act 2009 (NCC). The NCC does not apply to certain loans, including low-cost short-term credit (less than 62 days), insurance premiums paid by instalments, bill facilities and staff loans.

As a result, BNPL apps have no legal requirement to comply with credit laws or offer hardship programs nor register with a dispute resolution scheme, like the Australian Financial Complaints Authority.

The RBA has not required BNPL apps to comply with its 2004 no surcharge rule, which all other payment providers must comply with. BNPL merchant contracts force no surcharging of consumers thus avoiding a 3-6% surcharge on all sales.

There is evidence BNPL apps are only paying merchants after goods are dispatched, which can be days or even weeks post-purchase.

BNPL – YET TO REACH SCALE

After 8 years BNPL has still to achieve scale and ubiquity with only 1.7% share of card sales and very small share of all retail payments.

Australian consumers use 74.7 million cards spending $815.4 billion annually.

BNPL with 4.9 million consumers with 7 million accounts and estimated $16 billion sales.

Australian Consumer Payments – Full Year 2022

Payment type	Volume in $ billions
Debit Cards	513.9
Credit/Charge Cards	293.4
NPP/ Osko Digital – consumer only use	178.8
ATM Cash	104.6
Corp/Commercial Cards	77.4
Buy Now Pay Later – RBA report	16.0
Cash – notes*	8.6
Pre-Paid Cards	7.7
Cheques*	4.7
TOTAL	**$1205.1**

Data – ex RBA Oct 2022 * private research Nov 2021

BNPL ‘bill’ customers and receive payment two weeks later, these ‘cycles’ are like debit cards, ATM cards, P2P cash transfers. All these business models have short term usage and industry measures are in days and months not years.

Credit and charge cards are measured yearly with monthly spend/payment as are loans and mortgages.

Yet BNPL customer numbers use the credit card measure of one transaction in 12 months, this massively inflates customer numbers hence the very low spend.

<u>MONTHLY CONSUMER SPEND</u>

Charge Cards - $4,420

Credit cards - $1145

Debit cards - $980

BNPL apps - $96 to $285

PrePaid Debit - $41

(2022 RBA figures)

There are clear signs BNPL has peaked in Australia, after only eight years of full operation, before regulation and all external competition fully ramps up.

The RBA reported in March 2021 BNPL sales in Australia $11 billion or 1.7% of card sales, with 80% online. RBA also reported Afterpay sales $8.3 billion or 75% BNPL market share in Australia.

After 17 years BNPL apps have estimated 225 million global accounts and 2021 sales of US$78 billion across Europe, North America and Australasia.

Compare these figures with ‘China mobile’ and BNPL’s size is laughable. China mobile (Alipay and WeChat) after 12 years reached 2.4 billion accounts with annual 2021 sales of US$61 trillion in 28 countries.

As real time digital payments (RTP) based on the 2004 ISO messaging grow with benefits of fast, cheap payments which also supply more data. This is the biggest technology threat to BNPL who currently depend on Visa/MC interchange – this is will change revenues and future digital rates will be massively cheaper reducing the key revenue source.

HISTORY IS IMPORTANT

BNPL apps are a new twist on a very old idea, so much for ‘innovation’.

Who was first, who’s biggest?

BNPL has been around if finance/lending has been used, there is evidence the Romans and Greeks used BNPL.

Modern BNPL can be traced back to -

US Singer sewing machines used BNPL in 1850’s.

GM forced Henry Ford to follow its BNPL initiative in the 1920’s.

Global airlines and IATA used ‘Fly Now Pay Later’ along with European department stores and mail order companies in the 1970s.

Certegy established BNPL EziPay in Adelaide in 1989.

Rapidly rising interest rates ‘killed off’ BNPL in the 1980s, as providers could no longer fund the gap between paying merchants and being paid by consumers.

MOBILE & BNPL APPS

Telco start-up Smart in Philippines used mobile wallets in 2000.

Alipay was founded in China in 2004 and along with other Asian players in Hong Kong, Korea, Singapore and Taiwan explored wallets and instalments.

The current BNPL app ‘craze’ started with Klarna in 2005, followed by Afterpay in Holland also a 2005 start-up.

BNPL requires both integration into a retailer’s ecommerce platform and sometimes their physical point of sale.

Fintech start-ups like Afterpay Holland, Affirm and Klarna created this niche by developing the Application Programming Interfaces (API) & Software Development Kits (SDK).

Most banks and card issuers core processors don’t offer a downloadable API or SDK for retailers, initially making it difficult for banks and card issuers to enter this small niche.

The big payment/lending players have already bridged this gap quickly and bringing massive scale to this niche e.g. Visa, Mastercard issue virtual debt cards, PayPal, Amex and Apple all have product either in the market or in development.

FINTECH START UPS

Europe is the ‘home’ of current BNPL apps with Klarna and Afterpay Holland both commencing in 2005 and now over 45 BNPL companies.

BNPL Fintech apps:

KLARNA EUROPE

Swedish start- up founded in 2005 with the objective of making online shopping more convenient. Expansion into Norway, Finland and Denmark followed in 2006-8 as well as a banking licence.

Klarna is the largest BNPL app with 150 million consumer accounts, US$80 billion in sales and 450,000 merchants.

AFTERPAY EUROPE

Founded in Holland in 2005 as part of collection agency.

Afterpay Europe – a Dutch start-up is now part of Bertelsmann Group with market share across central Europe.

Afterpay Europe is not to be confused with Afterpay Australia, which started in 2014 and uses the Clearpay brand in Europe.

Read the 2016 interview with Afterpay founding CEO Stefan van den Berg in the appendix

AFFIRM

US start up founded in 2012 by four partners including Max Levchin of PayPal fame. Levchin became CEO in 2014 and remains in the role. Affirm was IPO in 2021 and has 11 million customer accounts with US$20 billion in sales.

AFTERPAY AUSTRALIA AND CLEARPAY

Afterpay Australia launched its app in 2014, a full nine years after the Dutch start-up. Seems the Afterpay name was only registered in Europe, often the case with start-ups as its expensive maintaining a global name registry.

Afterpay Australia uses very careful language.

“Afterpay is an Australian innovation. Not only is it new to the Australian market, the presence of BNPL products internationally is still in its early stages”

Also, important to note the original Afterpay from Holland has over 4 million customers in its home market and 2.8 million in other European markets.

Afterpay Europe outperforms Afterpay Australia in their receptive 'home' markets - Holland population 17 million with 4.2 million customers - Australia and New Zealand population 31 million with 3.7 million customers - not even close!

ZIP

ZIP Money was founded in 2013 as a ‘digital’ lender offering loans.

BNPL was launched in 2015 following Afterpay’s launch in 2014.

ZIP was IPO in 2015 and embarked on an aggressive M&A expansion.

ZIP claimed operations in Australia, Canada, Czech Republic, India, Mexico, New Zealand, Philippines, Poland, Saudi Arabia, Singapore, South Africa, UAE, United Kingdom and USA.

INTERNATIONAL ONLINE COMPARISON

Global 2021 online market estimates US$5.67 trillion (China is over $2.2 Trillion or 38%)

The global rankings 2021 are – with economic ranking in brackets.

1. China (2)
2. USA (1)
3. UK (7)
4. Japan (3)
5. Germany (4)

Other top ten markets in order: France, South Korea, Canada, Russia and Brazil.

Australia is ranked 12th in online markets like its economic ranking.

BNPL is only a factor in 3 of 10 top online markets USA, UK and Germany. BNPL apps have no realistic chance of successfully entering China, Japan, South Korea, Russia, Brazil or India.

This also ignores other markets with existing entrenched BNPL offerings – most of Latin America e.g., Argentina, Chile and many parts of Asia and Europe.

Paypal $1.25 billion with growth rate 34%
Stripe $640 billion 60%
Amazon estimate only $626 billion 36%
Adyen $610 billion 70%
Shopify $175 billion 47%
Square $168 billion 49%

BNPL apps estimated global sales $78 billion of pure BNPL ‘Pay-in-4’ in 2021 with growth 34% representing 14 basis points market share of online sales.

BNPL apps only feature in seven ‘major’ markets – Australia, Germany, Netherlands, New Zealand, Sweden, United Kingdom and USA.

Online ecommerce platforms are much bigger, growing faster and don't have any bad debts (some fraud), yet BNPL spin claims they are a major online force?

REGULATION

BNPL faces regulation in: Ireland, New Zealand, Sweden, Singapore, UK, USA and Europe which already has some caps on fees and disclosure of competitive interest rates/fees.

ASIC has avoided regulating BNPL sector despite its own research in 2018 and 2020 clearly showed these apps lead to financial stress among young consumers.

The regulators need to consider the business risks and operational model used by BNPL apps.

- Consumers used as "off balance sheet" securitized borrowings.
- Fintech model depends on extremely low interest rates
- Very high bad debts - averaging 30% of revenue.
- Very high ‘late fees’ which, when converted to APRs, are up to 68%.
- Small 'loan' amounts over a short period.
- BNPL typically do not assess a consumer’s ability to repay.
- Majority do not use credit bureaus for new applications or update performance.
- Majority do not report payment obligations or default to credit bureaus.

The RBA’s ludicrous stance on surcharging and has not moved in eight years, stating BNPL is currently too small to ‘designate’ i.e. regulate.

Yet the RBA fought a legal battle with Visa in 2003/4 arguing the opposite, that consistency was paramount for payment system integrity and security

“Dr Lowe said the stance was in recognition of the innovation the instalment products brings to customers and the relatively small overall volume transacted compared to existing payment methods”
AFR Dec 7th 2020 Afterpay Benefits Outweigh Harm :RBA.

RBA/PSB should find that BNPL contracts cannot stop retailers surcharging consumers if consistency in payment policy is to be maintained. Retailers will then surcharge to recover margins 3-6% for online 3-4% in high street stores, which is consistent with all other payment types.

This will totally undercut BNPL's claim that consumers pay no fees or charges and consumers habits will adjust as with other changes in the payment market. RBA Research indicates results with potentially 60% of consumers rejecting BNPL usage if surcharges are imposed (50% say they will switch to debit or credit 10% would cancel).

CONSUMER ISSUES

ASIC research highlights key issues around young consumers over spending, buying items they don't need and cannot afford.

Reports in 2018 and 2020 highlight key issues: 44% of users earn less than $40,000, one in five users are missing payments, 20% of users are cutting back on essentials because of over commitment and 15% sort additional loans to pay off BNPL debits.

A key issue with unregulated lending is the number of young consumers (mostly young women) who are now having their credit ratings impacted, UBS estimates 9% or 450,000 consumers have defaulted on Afterpay loans in just 3 years in Australia.

ASIC 2020 report also showed the overspending/increased debt relationship between BNPL and credit cards. Heavy BNPL users with credit cards are more likely to default, yet ASIC took no action sitting on its hands unlike other regulators e.g. Sweden and UK.

In the U.K the regulator announced in 2020 it plans to regulate on BNPL payments. The FCA argues that BNPL payment options urge consumers to spend more than they can afford.

The UK BNPL volume is half Australia's which highlights the different approach to consumer welfare, regulation and start-ups.

"Changes are urgently needed to bring BNPL into regulation to protect consumers," Christopher Woolard, chair of the review at the FCA .

In the UK 70 MP's from both sides of politics signed a joint letter calling for BNPL regulation sighting Wonga, a payday lender scandal impacting young consumers.

Not for profit legal centres and budget advisory groups say BNPL represents their largest client base, this challenge has yet to be faced.

Late fees are another example of regulatory avoidance, by labelling these fees as 'late fees' BNPL apps avoid any comparison with APRs – yet they are the same functionally. Market leader Afterpay claims to look after young consumers yet charges outrageous late fees which can only be seen as gouging.

Afterpay has three tiers of late fees – up to $40; $40 to $272 and over $272. The bulk of transactions fall within the second band – Afterpay claims an average transaction of $170 however in Senate evidence stated $130.

An unpaid debt of $40 has $10 fee before cancellation at the end of 8 weeks – so a consumer who has already paid $10 upfront is charged $10 in late fees which is 25% interest (33% on balance owing), so much for looking after Millennials and Gen Z!

A $125 default attracts - $10 late fee plus $7 per bill cycle or 23% interest in one month, which is equivalent to the top tier of credit cards. Applying APR calculations across a range of late fees and cancellation shows 48-68%, this is pure gouging.

<u>CURTIN UNIVERSITY STUDY</u>

BNPL is touted as 'free' instalments for all, freedom to buy what you want at no cost - that's not the real however - another bogus claim by Fintech apps.

BNPL costs have been modelled by Curtin University in a study for Financial Counselling Australia.

Curtin University July 2022 study concluded -

"We found that the **fee structure** of **BNPL companies** is, in general, **highly regressive**, i.e. the less customers owe, the greater the effective interest rate they are charged"

"For a **purchase amount of $40** for example, where a customer incurs maximum late fees, the effective annual interest rate is"

CBA StepPay – N/A

Humm – Little things (5 fortnightly repayments) APR **16.13%**

Afterpay 28.25%

LatitudePay 28.33%

Zip Pay 29.32%

Humm – Little things (10 fortnightly repayments) **177.44%**

"In contrast, the interest rates on credit cards are equivalent to annual effective interest rates of approximately 22%".

Numerous research studies have shown 25-35% of BNPL consumers pay late fees, just as only 34% of credit card users pay interest in Australia.

GOOD SHEPHERD REPORT

In a report “Safety net for Sale” financial council group Good Shepherd highlight significant BNPL debt and entrapment issues in Australia and New Zealand.

Key summary of report

BNPL indebtedness up 8 times since 2017 – much higher rate than BNPL sales.

84% councillors report ‘debt management’ involve opening new BNPL accounts – this only worsens consumers situation, highlighting the absence of credit reporting and lending rules.

“BNPL marketing plays on the ‘no interest’ alternative to credit cards, encouraging overspending without regard to repayment and the costs.

75% report BNPL used for basic – food, child cloths, baby products.

73% report clients missing essential payments.

“Low and inadequate incomes appear to be driving BNPL use.”

25% of Good Shepherd clients rely on welfare payments or cutting back.

Good Shepherd highlights the lack of consumer protections, coercive use (what the US regulator calls ‘debt stacking’) and debt collections.

It’s hard to believe but BNPL makes PayDay Lenders look good!

A US example –

Consumer Financial Protection Bureau (CFPB) Report

The US consumer regulator reported on BNPL with a view to regulation September 2022.

It highlighted serious concerns about BNPL, its business model and consumer use. The CFPB raised concerns across four areas – scale and usage, lack of profitably, consumer harm/credit losses and overspending with increased debt.

Usage and Scale

“We cannot measure the impact of BNPL payments on borrowers’ checking accounts, including non-sufficient funds or overdraft fees, or on borrowers’ capacity to repay other expenses or obligations.”

Consumer Harm

“BNPL product is often structured in ways that may present borrowers with undesirable operational hurdles, including the lack of clear disclosures of loan terms, challenges in filing and resolving disputes, and a requirement to use autopay for all loan payments”

“As a result, the credit performance of individual borrowers across lenders or over time cannot be assessed from the data collected.”

“There is also no way to evaluate the structural soundness of the lenders’ credit models.”

Data Harvesting

“BNPL lenders often collect consumer data… to increase the likelihood of incremental sales and maximize the lifetime value it can extract from each current, past, or potential borrower.”

“These practices may compromise consumers’ privacy and autonomy and contribute to the overextension risks”

Overspending/Debt

“BNPL business model may encourage overextension… (with) risks: loan stacking, which can cause borrowers to take out several loans within a short time frame at simultaneous lenders…”

The CFPB raised concerns at ‘loan stacking’ by BNPL apps with serious issues of increased debt.

The US FTC has also stated it will act on BNPL advertising and online claims.

LACK OF REVENUE

BNPL apps have very low revenue per customer, excessively high bad debts and with longer term funding risks sustained profitably is most unlikely.

The Australian sector has average revenue per customer of $54, bad debts of 30% of revenue which is four times higher than European BNPL’s and face real funding costs of 5-15%.

BNPL apps do not use retail bank measures for revenue per customer, activity rates, bad debts which use receivables as the key measure when applied to consumer loans. BNPL instead use bad debts as a percent of sales, as this measure appears to lower bad debts, yet bad debts are the largest single operating expense.

Afterpay’s bad debts/collection costs for F21 of $220.1 million representing 26.7% of core revenue. This is high for any BNPL product and is four times higher than European players.

Afterpay’s accumulated bad debts since 2014 total $433.9 million or 25.6% of revenues.

Commonwealth Bank in 2021 by comparison has revenues of $21.8 billion while actual bad debt write-offs total $525 million, with 48% of these corporate losses.

Bendigo Bank’s 2021 annual revenues were $1.44 billion and bad debts of $18 million and impaired provisioning of $208.8 million – to total 14.5% revenue.

CHARGE CARDS vs BNPL

Charge cards are probably the closest product to BNPL as they require full payment of each monthly bill, do not charge interest but charge late fees.

American Express (Amex) Australia has 70% of its sales from charge cards, the remaining 30% from revolving credit cards and loans.

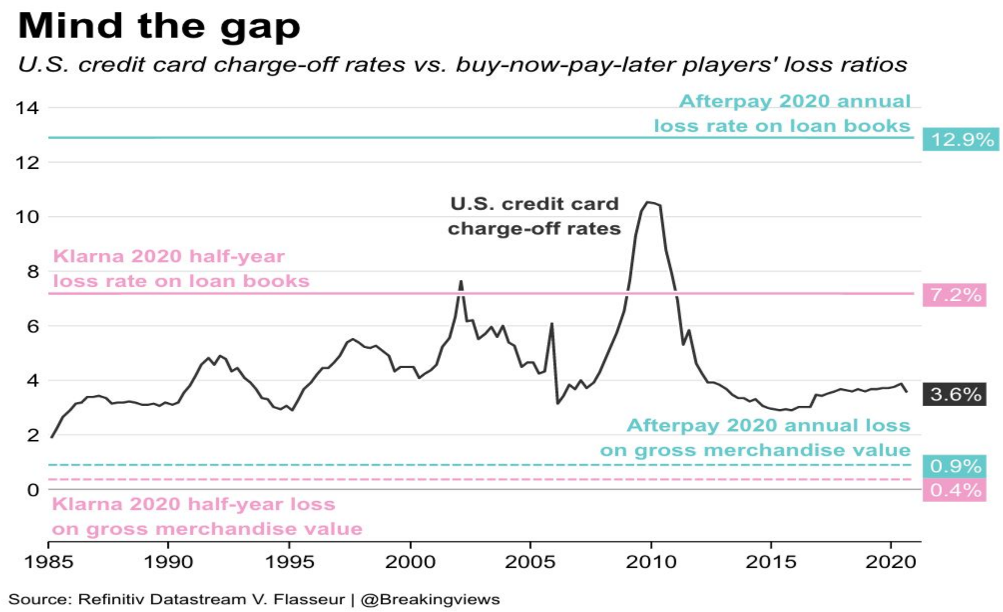
Amex's Australia accounts ex ASIC show 2021 sales of $48.9 billion and bad debts/provisions of $10.4 million, only $1.4 million was added to provisions in 2021.

Afterpay 2021 global sales $21.1 billion bad debts/collections $220 million.

Amex has over twice the sales - BUT 21 times less bad debts than Afterpay!

BNPL v CREDIT CARDS

Afterpay and Klarna 2020 bad debts verses the US credit card charge-off rates (bad debts) clearly demonstrates the excessive risks taken. The US credit card excesses of the 2010 GFC charge-offs peaked at 10.6%, well below Afterpay's 12.9%. Klarna at 7.2% is also extremely high verses US card losses of 3.6%.



This chart also shows the folly of allowing GMV (sales) to be used as a measure of credit losses – with Afterpay at 0.099% and Klarna 0.045% appear very low, this is deeply flawed.

BNPL define active customers as any customer who has one transaction in 12 months, another retail bank measure which inflates customer numbers. Actual BNPL usage numbers per cycle range from 5-20% active customers – this is very low, yet credit losses are high.

BNPL BAD DEBT TRICK

BNPL apps play an accounting trick with bad debts – they compare bad debts against total sales or GMV (gross mechanise value) which reduces bad debt calculations significantly.

The example, a BNPL $100 sale requires $25 dollars to be paid upfront – so the loan is $75 and not $100.

BNPL by comparing credit write offs to total sales and reducing bad debts by 25% - this is a massive red flag in what are already huge bad debts.

BNPL sales also include returns by consumers, which run at 30% for online sales, but can be as high as 55% in shoes, cosmetics and high fashion. This artificially boosts BNPL sales as many returns are full credits. Any bad debt calculation is further diluted by including returned sales, another red flag.

The BNPL dirty secret of bad debts was given a public airing earlier this year.

ZIP Chair said "The industry as a whole, which has seen bad debts spike, really missed that moment. And we are now going to have to dig our way out of that." SMH May 23rd 2022

This is total nonsense, high bad debts are a constant in this 'business model' and did not suddenly spike, especially when compared to other consumer lending, which has been at record lows.

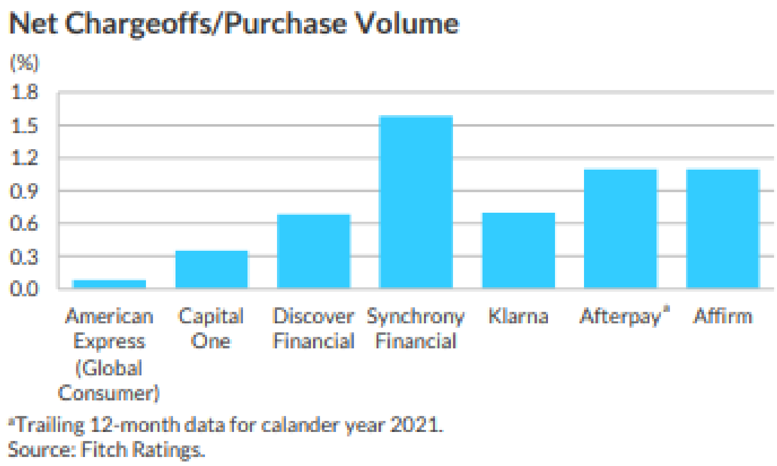
The real comparison is bad debts to receivables as all other lenders do – using this correct measure the major BNPL apps numbers are staggering.

USA Credit Cards Industry 2021 2.62% of receivables.

Afterpay 13.9% of receivables
ZIP 9.7%
Klarna 8.1%
Affirm 6.5%

BAD DEBTS vs SALES

Even when sales (GMV) are used BNPL's bad debts are much higher than other mainstream consumer lenders. The Fitch chart show US players using sales – note had much higher the BNPL apps are, they should be lower than American Express.

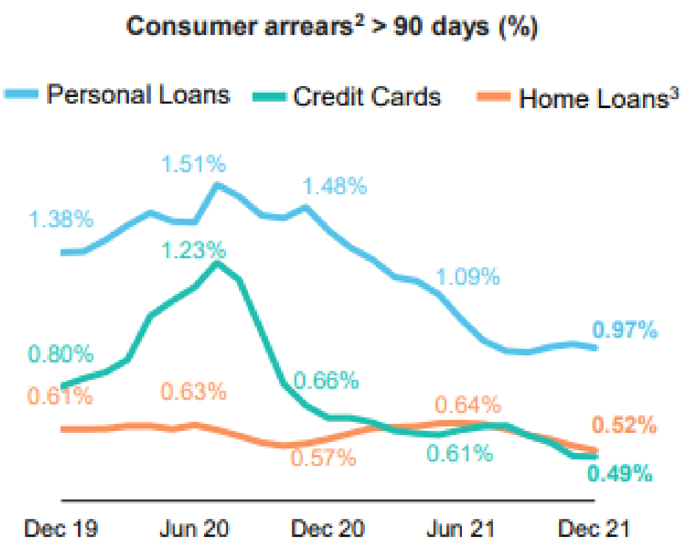


COMMONWEALTH BANK vs BNPL

Australia largest retail bank is the Commonwealth Bank of Australia (CBA).

CBA's 2022 results show the massive difference in credit risk taken by BNPL apps.

CBA credit cards at 90 days overdue are 49 basis points to receivables (this is a low number for any unsecured lending product).



CBA writes off credit card bad debts at 180 days and would expect to recover up to half the 90-day figure, this gives credit card write offs 0.25 vs Afterpay at 13.9%!

Put another way Afterpay bad debts are 55 times higher than CBA.

Australian BNPL apps in 2021 had bad debts of 32% of revenue – Afterpay $220 million, ZIP $123.8 million, Humm BNPL $33.2 million

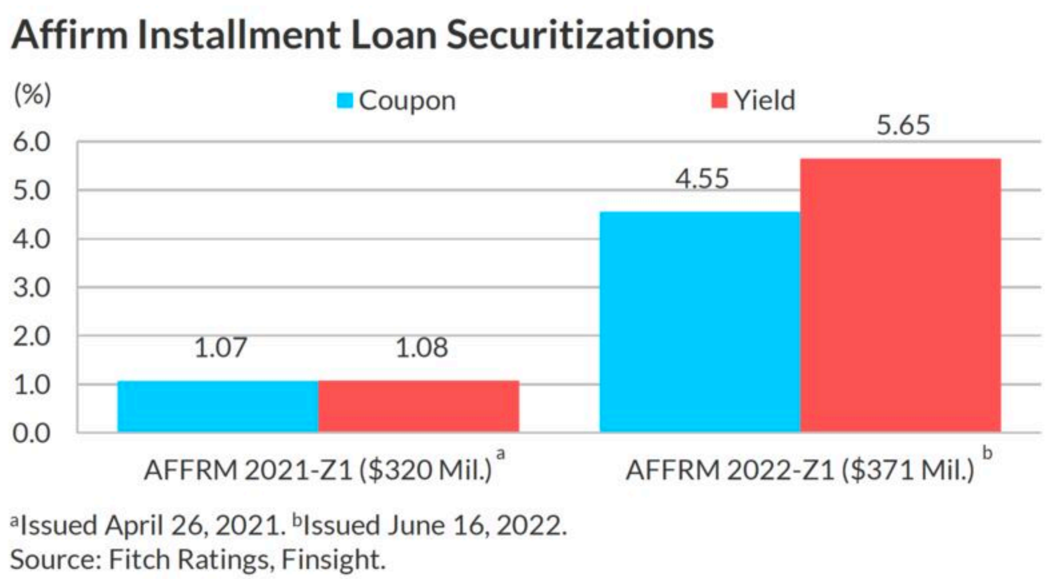
FUNDING COST – 'Free' MONEY HAS GONE

Record low interest rates over the past seven years has provide record low funding costs.

Even with this environment most Fintech's and all BNPL apps still cannot make profits, and making profits is now the name of the game.

Gone are excessive growth plans, burning heaps of investors cash and ripping money out of unprofitable businesses via ESOP share schemes based on excessive valuations.

Most BNPL apps raise funding using securitization of their receivables or the more expensive secondary market. A majority of BNPL securitization is based on the 90-day bill rate plus a margin as this Affirm chart shows.



ZIP A CLASSIC EXAMPLE

ZIP obtain its funding using ANZ securitization of its customers receivables, great when intertest rates are low, but not much fun when rates explode as 2022 shows.

Prudential the funding agent provides monthly reports to bond holders detailing funding rates, receivable performance, funding costs and administration costs.

Prudential reports show:

ZIP funding costs have exploded, up 46.6% in 3 months with more to come – June funding was $5.09 million, $61 million annualized, which is $21 million extra in costs at June rates.

With more rate rises in 2023 ZIP is facing $70-80 million in increased funding costs for its Australian business alone, if the 90-day bill futures are correct. Australia is 48% of ZIP sales so a similar risk applies to US and other regions.

Bad debts are still getting worse (despite management claims of action), Q4 reported bad debts were 3.40% of sales or $75 million, up from 2.83% in Q3.

Prudential reports show 90 day plus receivable aging getting worse by 30.5%, this will flow through to future write offs adding another $25-28 million to bad debts.

Also identified are 10.2% cost increases in securitization fees, or $1.2 million.

These three items add over $100 million to ZIPs cost base and negate all the recent claimed cost reductions of $30 million, yet management still claim they can make a profit?

Klarna has similar issues – even though in Sweden it owns a bank and can access broader funding options (in theory), its funding costs have sky rocketing.

Bloomberg reported a 2024 floating rate bond saw Klarna's discount margin -- a measure of the credit spread over benchmark borrowing rates -- climb to 272 basis points.

Funding costs increased 120 basis points this year. In addition to borrowing costs rising, the extra price (yield) Klarna must pay to sell more debt is increasing rapidly.

BNPL CODE OF CONDUCT

The voluntary BNPL Code of Conduct is a classic, 95% of all transactions are exempt – so what is the point?

Firstly, its voluntary, so what happens if any BNPL apps don't comply?

Short answer is nothing of substance.

The vast majority of transactions are exempt with a $2000 lower limit, Afterpay is 75% of the market its average transaction reported to the Senate Inquiry $130.

No requirement to report transactions to credit bureaus each week/month.

Nothing in the BNPL Code of Conduct on KYC and only a nod to AML regulations.

The hardship program is a box ticking exercise, BNPL apps only need to respond to a request within 21 days. The hardship program runs outside the financial ombudsman program and has no true external oversight, nor are they required to publish outcomes.

BNPL BUSINESS MODEL

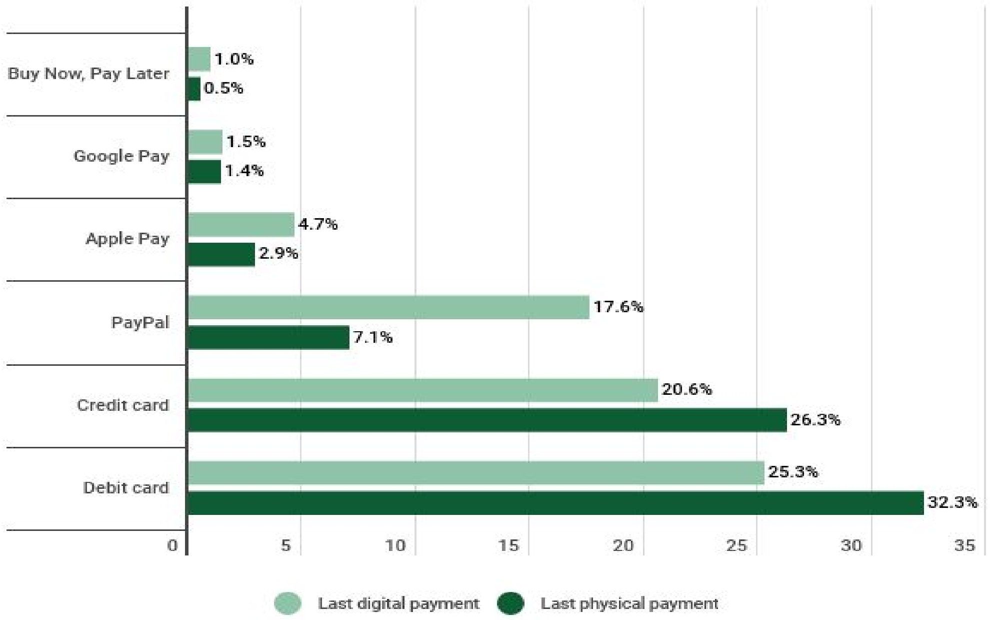
BNPL is a very high-volume low margin business.

Yet success in payments requires scale, ubiquity and profits.

The BNPL app profit model is highly questionable – a $100 sales earn $4 in merchant revenue with 56 cents in late fees = $4.56.

Expenses are $4.95 – of which $1.10 are credit losses, 26 cents funding (this will double in 2023), 34 cents share purchase and $3.25 in marketing, operations and salaries. Losses of $0.39 per transaction

This US chart demonstrates the total lack of scale in the most BNPL apps most important market



The CFPB required BNPL apps to provide key data on their financial performance. This data highlights the BNPL challenges – falling margins, down 26% in the key merchant revenue.

Credit losses are 32% of revenue and increasing while expenses are increasing (this excludes ESOP share schemes).

BNPL ESOP incentives are based on the mythical 2% ‘Net Transaction Margin’, the CFPB numbers blow this out of the water with the real number 1.01% and its declining.

The mathematics of offering BNPL service,
Aggregated unit margins, 2019-2021

	2019	2020	2021
REVENUES			
Merchant Discount Fees	3.39%	2.91%	2.49%
Interchange	0.26%	0.60%	0.67%
Referral/Affiliate	0.16%	0.23%	0.32%
Late Fees	0.31%	0.20%	0.28%
Transaction Fees	0.18%	0.29%	0.26%
Revenue Total	**4.29%**	**4.24%**	**4.02%**
EXPENSES			
Underwriting	-0.09%	-0.09%	-0.08%
Cost of Funds	-0.52%	-0.24%	-0.16%
Payment Processing and/or Servicing	-1.51%	-1.49%	-1.47%
Credit Loss Provisions	N/A	-1.15%	-1.30%
Expense Total	**N/A**	**-2.97%**	**-3.01%**
NET TRANSACTION MARGIN (NTM)	**N/A**	**1.27%**	**1.01%**

Based on a Consumer Financial Protection Bureau study based on figures reported by Affirm, Afterpay, Klarna, PayPal and Zip. **Source:** Consumer Financial Protection Bureau

BNPL CASH FLOW

Given none of the BNPL companies make a profit in the lowest funding environment in 30 years the future path to profitability is highly questionable.

A review of cash flow demonstrates this key issue.

Afterpay is an example of 'pure' BNPL Pay-in -4, having not extended its product beyond instalments into other lending (new owner Block has now done this). Examining its early years are important as this identifies key structural issues in the business model.

The holes in Afterpay business model can be clearly seen and its dependence on low interest rates and high write offs is staggering. Afterpay has never made a profit, indeed the bigger it gets the worse its losses, an unsustainable business.

Afterpay's cash flow model saps money out of its capital structure, only being counterbalanced by its ability to continually raise cash – its cash burn rate gets bigger each year.

Afterpay Simplified Income Statement millions

Fiscal Period	Jun-20	Jun-19	Jun-18	Jun-17
Revenue	**$310.77**	**$151.36**	**$85.38**	**$17.33**
Cost of Goods Sold	$92.68	$41.36	$21.15	$3.98
Gross Contribution	$218.09	$110.00	$64.24	$13.35
Selling, General, & Admin. Expense	$145.30	$85.59	$37.82	$7.53
Research & Development	$0.00	$0.00	$0.00	$0.00
Other Operating Expense	$133.26	$80.66	$47.60	$15.39
Total Operating Expense	**$278.57**	**$166.25**	**$85.42**	**$22.91**
Operating Income	-$60.48	-$56.25	-$21.18	-$9.57
Interest Income	$0.97	$0.39	$0.40	$0.26
Interest Expense	**-$15.55**	**-$8.09**	**-$4.96**	**-$0.59**
Net Income	-$13.65	-$29.77	-$6.73	-$7.28
Shares Outstanding (Diluted Average)	259.147	231.919	214.551	175.463

Afterpay Simplified Cash Flow Statement

Fiscal Period	Jun-20	Jun-19	Jun-18	Jun-17
Cash Flow from Operations	-$161.46	-$98.74	-$78.96	-$59.66
Cash Flow from Investing	-$33.57	-$11.31	-$10.66	$12.84
Cash Flow from Financing	$448.20	$248.01	$85.29	$54.29

Rising interest rates negate any chance of profits, as can be seen from net interest expense – this will triple in coming months and stay elevated if interest rates do not return to record lows.

Afterpay Simplified Balance Sheet

Fiscal Period	Jun-20	Jun-19	Jun-18	Jun-17
Cash, Cash Equivalents, Marketable Securities	$418.25	$160.73	$19.08	$22.39

The company is sitting on some cash, but not enough to fund Afterpay's growth.

	Jun-20	Jun-19	Jun-18	Jun-17
Fiscal Period				
Total Receivables	$539.61	$314.37	$179.21	$74.42

54% of assets are receivables, a majority of which are securitized with assigned security given to bond holders - this is a significant risk. It highlights an important characteristic of Afterpay's structure - the absence of fixed assets.

Fiscal Period	Jun-20	Jun-19	Jun-18	Jun-17
Accounts Payable	$124.73	$76.38	$32.17	$14.79

Payables are growing at a faster pace than receivables, the difference does indicate the a near term strain on cash flows to finance near-term credit facilities.

Fiscal Period	Jun-20	Jun-19	Jun-18	Jun-17
Intangible Assets	$73.56	$61.86	$54.34	$52.01
Goodwill	$27.47	$27.65	$17.68	$30.85

Goodwill reflects sums paid above fair value for any asset and is most likely linked to the company's acquisitions e.g. Clearpay, Pagantis and Afterpay USA

Fiscal Period	Jun-20	Jun-19	Jun-18	Jun-17
Long-Term Debt & Capital Lease Obligation	$320.75	$34.46	$121.11	$35.36

Understanding in detail the characteristic of debt is paramount.

APPENDIX

BBC Panorama investigation –

https://www.youtube.com/watch?v=ow0brTHaEZs

ABC TV News   BNPL faces perfect storm – regulation, bad debts, funding costs, interest rates, competition

https://www.youtube.com/watch?v=hj8_XKfxlio

Verdict UK – Banking and Payments mag

https://www.verdict.co.uk/uk-government-buy-now-pay-later-regulation/

Curtin University research commissioned by Financial Counselling Australia, shows BNPL fees are effectively a quasi-interest rate and more costly than cards

https://www.financialcounsellingaustralia.org.au/docs/comparative-analysis-of-credit-card-interest-rates-vs-bnpl-fees/

Good Shepherd report on consumer damage down 2022

https://goodshep.org.au/publications/the-role-of-buy-now-pay-later-in-exploiting-financial-vulnerability/

Harvard Business Review US BNPL study

https://www.hbs.edu/faculty/Pages/item.aspx?num=62913

CFPB BNPL report

https://www.consumerfinance.gov/about-us/newsroom/cfpb-study-details-the-rapid-growth-of-buy-now-pay-later-lending/

Klarna CNBC interview –

https://www.cnbc.com/2022/06/10/klarna-ceo-defends-business-despite-massive-losses-and-layoffs.html

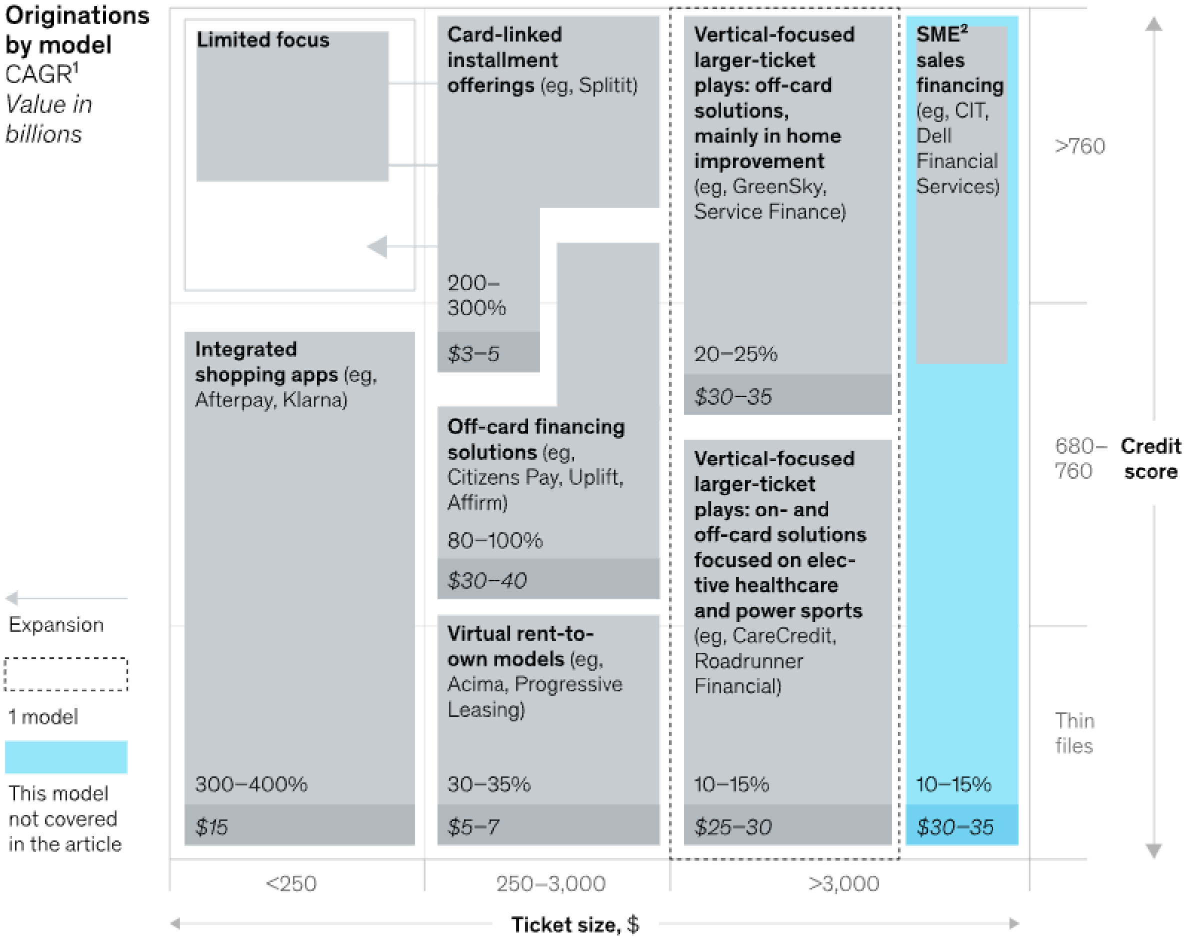
Klarna WSJ magazine article –

https://www.wsj.com/articles/klarna-ceo-sebastian-siemiatkowski-home-11632400195?mod=Searchresults_pos8&page=1

Affirm CEO interview

https://www-wired-com.cdn.ampproject.org/c/s/www.wired.com/story/max-levchins-war-on-credit-cards-bnpl/amp

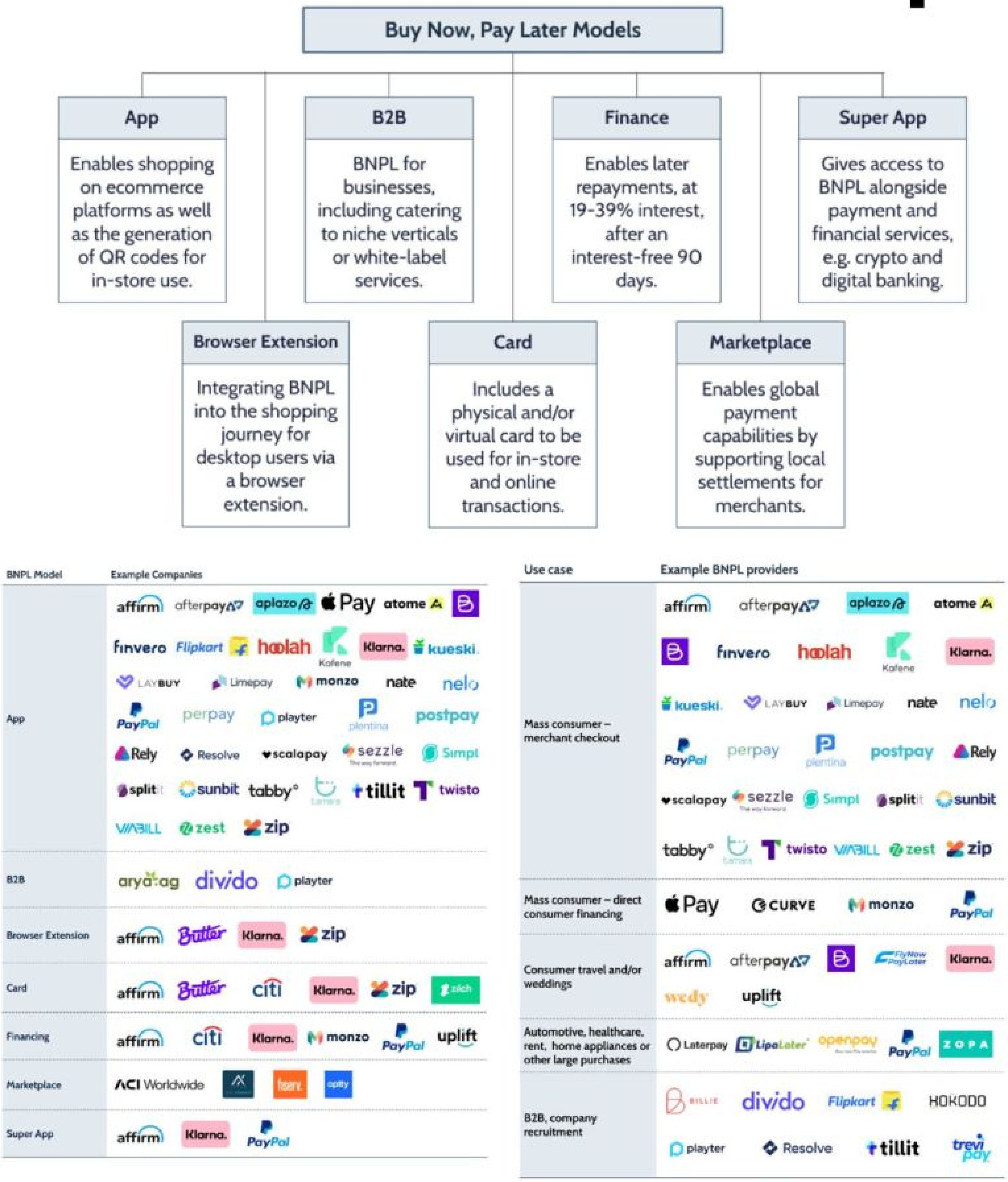
Most point-of-sale financing involves one of five distinct sets of models.



[1]Compound annual growth rate.
[2]Small and medium-size enterprises.

McKinsey & Company

BNPL Models & Landscape



Source: FXC Intelligence

Edits by: @linas.beliunas

Table 1: Comparison of BNPL variations (Non-exhaustive)

	Pay in X	Pay in full later	POS lending	Installment loan	Credit card issuer plans
Typical ticket size	Low value ~ $50-300	Low to high value ~ $50-5,000	High value ~ $300–5,000	High value ~ $300–15,000	Above $100
Typical Duration	Short duration ~ 1-3 months	Short duration ~ 2-4 weeks	Longer duration ~ 12-24 months	Longer duration ~ 12-36 months	Longer duration ~ 3-18 months
Usual sales channel	Smartphone app / Online	Smartphone app / Online	Offline in-store, phone	Offline in-store	Smartphone app / Online
Usual Credit Check process	Instant affordability decision (soft check)	Instant affordability decision (soft check)	Extensive application incl. credit bureau pull (hard check)	Extensive application incl. credit bureau pull (hard check)	Linked to existing cardholder credit limit
Interest Rate	Interest-free	Interest-free	Interest-free or interest bearing	Interest bearing (in exceptional cases, interest-free with upfront payment)	Interest-free, with fixed monthly fee
Typical consumer and transaction profile	Skews towards younger, digitally savvy, more credit constrained customer; repeat buyer	Skews towards digitally savvy and more credit constrained customer; repeat buyer	Less credit constrained customer, mostly used for one-off purchases	Less credit constrained customer, used for one-off purchases	Less credit constrained customer, used as an alternative plan to usual credit card T&Cs
Popular industry verticals	Apparel, health, beauty	Apparel, health, beauty	Car service, electronics, travel	Home furnishing, furniture, electronics, jewelry	All purchases from select credit cards
Example players	Fintechs: Klarna, Affirm, Afterpay	Open invoicing players: RatePAY, Mash, Divido	Specialised providers: Synchrony and Hitachi Personal Finance	Banks: BNP Paribas, or Santander	Credit card issuers: Chase (My Chase Plan), and Citi (Flex Pay)

Exhibit 1: Key BNPL firms including valuation

Note: Only main geographical areas are presented here, with a selection of BNPL firms (illustrative and not exhaustive), several other players compete in these markets. Valuation is in $ billion per July 2021. Source: BCG FinTech Control Tower and Pitchbook, Enterprise valuations from Yahoo Finance, Stockopedia

CASE STUDY – FINTECH START UPS AFTERPAY and ZIP MONEY

McLean Roche Submission to Productivity Commission – March 2018

Written by Grant Halverson

One Fintech start-up group that's very interesting are phone apps which target 15-35 year olds offering instalment payments. Examples are AfterPay and ZIP Money are the two largest start-ups -- with OpenPay in its infancy.

They compete in Australia with existing 'legacy' players including banks, credit unions and unsecured lenders such as Certegy Ezipay (owned by Flexigroup) and GEs old business now Latitude (owned by PE- KKR, Deutsche Bank Varde Partners) offering instalments, debit cards, credit cards and personal loans.

Three years after launching AfterPay has 1.5 million customers and 11,500 retailers - ZipMoney has 550,000 customers and 4500 retailers.

AfterPay, ZipMoney, OpenPay and others, position themselves as new technology with a new revolutionary idea that has the capacity to change the way retail and online shopping is conducted globally - a rather big claim.

Consumers can use the app in-store or online and a sales can be split up to 4 instalments to be paid over 8 weeks, with zero fees if all payments are made on time. The retailer pays 4% on all transactions - consumers who fall behind or don't pay are charged late fees and penalties.

Consumer research is very strong as it appeals to budget conscious millennials and looks to cut across credit cards personal loans and even debit cards - this group are very averse to credit cards.

Sales to date - AfterPay second full year June 2017 $574 million - last 6 months $959 million which is 320% growth - ZIPMoney is similar sales for 12 months $425 million - last 6 months up 180% - while sales are off a very low base its certainly showing growth.

The current business model is very vulnerable to higher interest rates and there are issues around credit and funding running at 60% of costs, but it's certainly has traction in both Australia and New Zealand.

The Australian debit card market totalled $288.5B in 2017 so market share is small at 1.5%. The unsecured credit market totals $152 billion with instalments totalling $15 billion, these start-ups now have 1/3 share of that segment - this should be a red light for regulators given the high growth and young consumer group involved.

The industry see these new start-ups as updating an old idea, retail instalments by adapting mobile apps and taking limited advantage of online credit reporting. Many industry players are dismissive of AfterPay and ZIPMoney due to the small market share - currently less than 1% of debit/credit card spend. Very few executives I speak to have even done a competitive overview of these start-ups and those that know them point to issues around AfterPay and its merger last year as a way of dismissing them due to lack of credibility.

The industry players recognize the technology step that After Pay has made. Concerns with the current revenue model is only sustainable in a low interest environment and if consumer are charged interest or other fees the model will implode - numbers suggest a 1% increase in funding costs would be add as much as 28% to costs

The key issues for AfterPay revolve around their credit losses which are very high for an instalment product. The accounts for June 2017 showed bad and doubtful debts at $8.1 million on sales of $570 million (no split for bad debts vs doubtful debits) - which equals 1.42% sales. This is very high for an instalment loan which offers very limited risk through 4 repayments over 8 weeks. The average transaction size for AfterPay and Zip Money is $142 which means each repayment is $35.50. If a consumer misses one payment this should raise a warning flag within the collections area. The typical risk/credit loss rate for instalment lenders internationally is between 15 - 25 basis points of sales – therefore credit losses should be around $1 -1.4 million. Some allowance should be made as these start-ups ramp up and the figures disclosed in the annual accounts do not disclose bad debt write-offs.

Similar products competing with AfterPay and Zip Money are Laybuy and charge cards like American Express, Diners Club and JCB. Laybuy risks are mitigated by the retailer retaining to goods until the full price is paid. Charge cards bad debts range between 20-35 basis points of sales – this is a higher risk category than instalments as consumers have an 'unlimited spending' capability over one month and are required to pay the full balance each month

Instalments are not credit cards and have no relationship to them - yet AfterPay compares themselves to revolving credit cards which appears to be a way of justifying high credit losses. This also should be a major red light for regulators given the number of consumers involved and the financial performance verses similar overseas products.

ZIPMoney appears to pay significantly more for its funding costs which is hard to understand - their accounts have funding at $11.5 million vs AfterPay at $5.2 million - yet ZIPMoney has less sales at $410 million. ZIPMoney also has high credit losses but not at the level of AfterPay.

One issue contributing to high credit losses is the lack of data made available for credit checks – this is being addressed by the Federal Government and could be partially resolved by July1st 2018 but only if the banks are required to provided 2/3 years of data. To make good credit/risk decisions unsecured lenders need 3- 5 years of comprehensive data, including all payments, increases in loans or limits and a total view of all borrowings.

Similar Fintech start-ups in the USA, UK and Canada include: Klarna, Affirm, FinanceIt and Splitit, verses traditional competitors such as PayPal Credit, GE Money and Cetelem

These start-ups fall under ASICs regime and it has to be questioned whether they have the skills, market knowledge and experience to manage a group of unsecured consumer lenders who also operate in retail payments. These start-ups also fall under the RBA/Payment Systems Board as they undertake payments. APRA has the skills most closely required but only regulates deposit taking institutions.

Industry Interview: AfterPay by verdictfinancial.com

The online payments market in the Netherlands is heavily dominated by iDEAL, with a 51% share of all online commerce by value in 2014. Despite the presence of such a large player, some new companies have managed to successfully break into the market: one such player is AfterPay. Senior Consumer Payments Analyst Sam Murrant spoke with AfterPay founder and CEO Stefan van den Berg concerning its pay-after-delivery service.

- **Could you give me a bit of background on AfterPay?**

AfterPay has been around since 2005 – we started out as part of a collection agency, but we really launched as an online payments service in 2010 when we became an independent start-up instead of a credit management service. We specialize in pay-after-delivery services, allowing customers to make payments via invoice after the goods are delivered. From the start AfterPay has focused on customer engagement by offering a consumer-friendly, seamless "pay-after-delivery" payment brand, AfterPay. AfterPay offers consumers the ability to pay these invoices via the payment method of their choice, and is currently integrated with two thirds of the e-commerce industry players and payment service providers in the Netherlands.

Our consumer payments service became a leading Dutch brand in 2012, and we launched our services in Belgium in 2013. After being acquired by **arvato Financial Solutions** in 2014, we've expanded to the Nordics and Germany. Currently, AfterPay has 1.5 million active users and is roughly comparable in size to PayPal in the Dutch market, with about a 6% share of all online transactions by volume in the Netherlands (excluding the travel and hotel sectors).

- **Is there a lot of demand for pay-after-delivery services?**

Our research suggests that 30% of Dutch consumers prefer to pay after delivery, for a number of reasons including ease of use, being able to check the product before having to pay, and budget planning. Security is the most important reason consumers use AfterPay – if a consumer selects the AfterPay option at checkout they don't have to enter their private payment details online, and they can be sure of receiving the goods they pay for.

On the merchant side AfterPay provides a full end-to-end service. AfterPay bears the risk of non-payment (based on our credit scoring application) as we guarantee payout and no charge-backs for our merchants after we've approved a customer for AfterPay use. Customers are approved in realtime based on our credit scoring application. We also take care of all AfterPay-related communication with customers from a consumer-central viewpoint. Customer-friendliness is one of our key success factors. AfterPay settles with its merchants in 14-30 days.

- **iDEAL is a pretty big player in the Dutch market – how do you compete with that?**

iDEAL isn't really a competitor of ours actually – AfterPay users can pay their invoices using iDEAL, in fact! We don't have our sights set on the wider e-commerce market as we're pay-after-delivery specialists, so we serve a different need to providers that cater to consumers who pay when ordering goods.

Our biggest direct competitor would probably be **Klarna**, which is another pay-after-delivery provider. Our strategy for competing with other pay-after-delivery providers is based on brand recognition and customer-centric services. Every merchant that accepts AfterPay has to display an AfterPay button on their website and as a result 58% of Dutch consumers are aware of our brand. We're also creating positive brand associations through our convenient user experience for consumers and through our dedicated merchant support and quick, easy merchant on-boarding.

- **Interesting – what are your ambitions for AfterPay in the next few years?**

We've got ambitious plans for our future. Thanks to our parent company arvato Bertelsmann we've been able to expand from the Benelux region to other parts of Northern and Central Europe and we're aiming to continue that growth by expanding into Poland, Austria, Switzerland, and Asia in 2016 and 2017. We're also planning to launch a mobile payments app later in 2016, which will allow consumers to make purchases at the point of sale using NFC technology.

By Samuel Murrant, Analyst, Consumer Payments

14 maart 2016

ThinkSmart offloads shares in POS financing startup ClearPay

23 August 2018

ThinkSmart Limited (AIM: TSL), a leading digital payment solutions provider, announces that it has sold 90% of the share capital of ClearPay to AfterPay Touch Group Limited ("AfterPay''), a company listed on the ASX.

ClearPay, a company which commenced trading in July 2017 and formally launched in March 2018, allows retailers to offer their customers the ability at the point of sale to make purchases of up to £450 and spread the cost over three interest-free monthly payments.

The Company's subsidiary, ThinkSmart Europe Limited ("TSE"), has sold 90% of the issued shares in ClearPay to AfterPay for 1,000,000 shares in the capital of AfterPay (currently valued at AUD $18.55m) ("Consideration Shares") to be issued to TSE.

An initial tranche of 750,000 shares will be issued to TSE at completion on 23 August 2018 (am AEST) and a second tranche of 250,000 shares will be issued to TSE on 23 February 2019, being 6 months from completion.

AfterPay are acquiring the ClearPay corporate entity, including ClearPay's contracts with relevant service providers and key employees with local knowledge of the UK market and regulatory landscape. ClearPay's existing retailers and customers currently transacting on ClearPay's system will be afforded the opportunity to transition onto AfterPay's global platform upon launch, expected to be within the next 6 months.

Utilising the local capabilities of the ClearPay entity and team, Afterpay will prepare to launch its globally scalable system into the UK within the next 6 months and will immediately engage with relevant retailers with a local UK presence.

The Company's subsidiary, RentSmart Limited has entered into a business separation and transitional services agreement with ClearPay to support the transaction and facilitate the transition to AfterPay.

A proportion of the 10% shareholding in ClearPay retained by TSE will be made available to employees of ClearPay under an employee share ownership plan ("ESOP"). After completion, TSE will make available some of the shares in ClearPay held by it for the grant of options under the ESOP (up to 3.5% of the total share capital of ClearPay). Any such options will only be exercisable on an ultimate exit event or at such time as TSE no longer holds shares in ClearPay.

TSE also has rights of pre-emption to subscribe for shares in ClearPay in any follow on fundraise. Afterpay has an option to acquire the remaining shares held by TSE (and any shares forming part of the ESOP), exercisable any time after 5 years from Completion based on agreed valuation principles. If the option to purchase is not exercised by AfterPay within 5 years and 6 months from Completion then TSE may exercise a put option to sell the remaining shares in ClearPay held by it (and any shares forming part of the ESOP) to AfterPay at a price calculated on agreed valuation principles.

The Company is also a party to the sale and purchase agreement and is guaranteeing the obligations of TSE under that agreement. For the 12 month period to 30 June 2018 ClearPay incurred unaudited losses of £0.6m and at 30 June 2018 had unaudited balance sheet net assets of £1.4m (excluding inter-company debt).

As part of the transaction AfterPay will ensure that the Consideration Shares are listed on the ASX. It is TSE's current intention to dispose of the initial tranche of Consideration Shares over the medium term in an orderly manner whilst retaining an ongoing investment in AfterPay. It is expected that shareholders will be rewarded in the form of a special dividend and capital return whilst the business will ensure that it retains sufficient cash reserves for further expansion and product development opportunities.

The business intends to advise shareholders at their full year results in mid-September of the detail of the return.

The Group will continue to operate its existing core credit and leasing business, and to invest in its proprietary leading digital payments solution SmartCheck.

Commenting, Ned Montarello, ThinkSmart's Executive Chairman, said: "The Board is pleased to crystallize a significant return on investment for shareholders with the sale of 90% of ClearPay, while still retaining an ongoing investment in what, in our view is the leading player in this sector globally, having recently successfully entered the US market.

AfterPay's product, ongoing success and go to market strategy is compelling and we are delighted to now be a part of this story.

In a market three times the size of Australia the acquisition of ClearPay will assist AfterPay in becoming the dominant player in the UK market with the potential for significant growth over the next five years.

Afterpay to adopt ClearPay name for UK launch

SYDNEY MORING HERALD By Colin Kruger May 1, 2019

Afterpay has turned its focus to the imminent launch of its buy now, pay later business in the UK where it will use the name of the business it acquired last year: Clearpay.

"We will be using the same logo, we will be using the same tech, one of the reasons why we've done that is that there's a number of issues that we need to deal with, and the quickest way for us to get into market was to actually use the ClearPay name," said Afterpay executive director David Hancock at the Macquarie Australia investment conference in Sydney on Tuesday.

According to figures cited by Afterpay, the UK market is worth $720 billion, with $130 billion of this online. By comparison, the Australian market is $320 billion with online worth just $30 billion.

“The UK is a really good opportunity for us to work with very large global brands,” Mr Hancock said.

In Australia, Afterpay accounts for 10 per cent of online sales, and about one in every four Millennials in Australia use the platform. This now gives the company a very influential role in the retail market in engaging its customers on behalf of retailers.

Loading

"We are the largest referrer outside of Google for leads," Mr Hancock said. "So many of our retailers really want to be on the platform because they are generating new leads for new customers."

This includes David Jones which has worked with Afterpay to increase its engagement with users which are expanding from its Millennial user base to include a growing number of 37 to 55-year-olds."Whilst we are a Millennial-focused company, we are seeing a halo effect of that pushing into other cohorts," said Mr Hancock.

Speaking of US competition, Mr Hancock said its product offering remains unique and "we don't see anyone as a direct competitor" to its service.

Afterpay forced to change name for UK launch by Dutch rival

SYDNEY MORINH HERALD By Colin Kruger May 9, 2019

Buy now, pay later platform Afterpay was forced to adopt a different brand in the UK after a rival European company secured rights to use the Afterpay name in the critical market.

The European incumbent is an Amsterdam-based company owned by Arvato – the financial services arm of German conglomerate Bertelsmann.

Arvato successfully opposed Afterpay Australia's attempt to trademark its name in the UK in June last year.

Arvato's Afterpay offers a post-pay service where online shoppers can delay payment until after they receive the goods they have purchased. Arvato's Afterpay funds the transaction until the customer pays. "With Afterpay you only pay for what you keep. Therefore: you pay afterwards!" says the company website.
Afterpay Touch, in comparison, offers a payment by instalment process over three weeks, and it also funds the transaction until its customers complete the payment.

Arvato's Afterpay said it was the most popular post-payment service in its home base of the Netherlands, with 4 million users on its platform. More than 70 million online purchases were made in the Netherlands last year with spending totalling €7.2 billion ($11.5 billion). Afterpay accounted for 15 per cent of these transactions.

"Afterpay is available today in Sweden, Norway, Finland, Denmark, Germany, Austria, Switzerland, the Netherlands and Belgium, with more markets coming soon," the company website says.

Arvato Afterpay was approached for comment about its expansion plans. The company has held rights to the Afterpay name in the UK since February 2011.

The UK market offers a significant growth opportunity for the Australian company after its launch into the US about eight months ago. The UK market is worth $720 billion, with $130 billion of this online, the company said.

By comparison, the Australian market is $320 billion with online worth just $30 billion, and it has rivals including Zip, Splitit and Flexigroup.

Afterpay executive director David Hancock hinted there were problems with the name last weekafter confirming that the company will use the name it acquired with a UK business, Clearpay, for its "imminent" launch.
"One of the reasons why we’ve done that is that there's a number of issues that we need to deal with and the quickest way for us to get into market was to actually use the Clearpay name so that will be slightly different.”

Afterpay later told the *Sydney Morning Herald* and *The Age* that its logo will provide the brand consistency across its growing operations.

“The arrow logo is the brand identification we focus on digitally and it translates across markets," said a company spokesman.

“We’re entering the UK market as Clearpay but retaining the global Afterpay model. It’s the model that resonates most with customers and with retailers, and it’s that model we intend to replicate in the UK.”

Harry Dudley, an investment analyst with Afterpay investor Watermark Funds Management, said: "I don't think the name will really present an issue."

"It's the platform itself; it's the simplicity of the product," he said.

Afterpay's share price is predicated on the company replicating its success here in these larger overseas markets.

Retails sales on the Afterpay platform totalled $2.3 billion last year, with more than $2 billion coming from its home markets in Australia and New Zealand from its 2.3 million active customers.

More than 10 per cent of online sales in Australia are now funded through Afterpay and it claims to have attracted one in every four Millennials to its platform.

“The UK is a really good opportunity for us to work with very large global brands,” Mr Hancock said.

News of the UK launch drove Afterpay's share price to record highs last week, valuing the company at more than $6.6 billion.

Its share price has risen more than 400 per cent since May last year, partly driven by the success of its launch into the US market less than a year ago. It closed down 0.5 per cent to $26.43 on Thursday.

Buy Now, Pay Later Is an Innovation That’s 200 Years Old

Stephen Mihm, Bloomberg - August 20 2021

Everything old is new again.

Witness fintech giant Square's recent acquisition of Afterpay, a company that enables consumers to buy now and pay later via regular payments administered by the Australia-based company.

Afterpay appeals to young millennials eager to move beyond conventional forms of financing such as credit cards. This may seem cutting edge to the youngsters, but it's nothing but a reboot of a credit system their great-great grandparents knew and loved: the installment plan.

Imagine, for a moment, a world without credit cards and other familiar forms of consumer financing. If someone two centuries ago wanted to purchase a big-ticket item such as a plow or cart, they had to front the full purchase price or borrow from family and friends.

That started to change in the early 19th century. According to historian Lendol Calder, the first forms of installment credit app

The first installment plans, like most that followed, rested on a legal foundation that structured them as a formal contract. When a buyer failed to make a payment, the seller could repossess the goods. Eventually, courts also permitted sellers to retain whatever payments had been made.

But installment plans remained unusual until the middle of the 19th century, when a growing number of essential — and expensive — consumer goods came into the market. These included mechanical reapers like the ones invented and marketed by Cyrus McCormick. Even the cheapest such machine was well beyond the price range of the average farmer. But their appeal was obvious: they cut harvesting time by 95%.

It was the sewing machine that turned the installment plan into a popular form of credit. In the 1850s, a number of companies began marketing sewing machines to consumers, especially housewives.

These time-saving inventions cost well over $5,000 in today's dollars, far beyond the means of the middle-class families that wanted them. Unlike a reaper, which might pay for itself in one season, sew

The genius behind the new credit system was the Singer Company's Edward Clark, who first asked in 1856, "Why not rent a sewing machine to the housewife and apply the rental fee to the cost of the machine?" He apparently took inspiration from piano manufactures in New York City, who had introduced a similar concept at the time.

Singer’s credit system transformed the company’s fortunes. Within a year, sales tripled, and within a decade, Singer had blown past all competitors, largely because it had devised a new method of financing that eventually demanded a mere dollar a week from prospective buyers.

By the end of the century, specialized retailers -- so-called “installment houses” -- had become ubiquitous in the nation’s cities. They offered a wide range of household goods on credit: furniture, bedding, dishes, even clothing. Many conventional retailers responded by offering their own installment plans.

By the early 20th century, installment plans had become so ubiquitous that a researcher at Columbia University marveled, “One may buy a house and furnish it from top to bottom with every article of necessity, convenience, and luxury he desires; he may clothe himself and his family; he may deck himself with jewelry and all sort of articles of adornment; he may go abroad, and having seen Paris, he may die and be buried — all on the instalment plan.”

At first, installment plans were associated with working-class consumers, many of them immigrants, who needed the flexibility that installment plans provided. This, combined with the fact that some crooked retailers abused the installment system to pawn off shoddy goods on unsuspecting consumers, gave the practice a bad name.

And then things changed. The key development was the rise of the ultimate durable consumer good: the automobile. Few people could purchase this big-ticket item in one payment. Banks didn’t want to lend money for them. In response, a handful of entrepreneurs formed the first “sales finance” companies in the early 1910s. These enabled auto dealers to extend installment credit to would-be buyers.

Henry Ford’s son, Edsel, tried to persuade his father to form their own subsidiary to provide this kind of financing to buyers. Ford refused, thinking that buyers should be forced to pay cash.

Executives at Ford’s chief competitor, General Motors, proved wiser. In 1919 they formed the General Motors Acceptance Corporation, which brought installment credit into the mainstream. It revolutionized auto sales, sparking a massive increase in consumption and enabling General Motors to outsell Ford by decade’s end.

In the process, installment credit became respectable. By 1930, it financed most cars, radios, furniture, washing machines, vacuum cleaners and phonographs purchased in the U. S.

This growth continued into the 1930s, despite the Great Depression. Though some commentators blamed installment credit for leading the nation to economic ruin, the reality was otherwise, and this system of middle-class finance remained firmly entrenched.

The advent of postwar systems of credit — namely, the credit card — led to a decline in installment purchases, particularly for smaller items.

Stephen Mihm, a professor of history at the University of Georgia

How Old-Style Buy Now, Pay Later Became Trendy 'BNPL'

BLOOMBERG By James Boxell 15 September 2021

Millennials and Gen Zers have an addictive new way to buy stuff that would look familiar to their great-grandparents.

"Buy now, pay later" is a type of consumer credit that really got going in the 19th century when Singer sewing machines were sold for a "dollar down, dollar a week."

The modern fintech twist in "BNPL" is that it's aimed at people making impulse purchases of fashion or jewelry or electronics rather than sofas or refrigerators. It's delivered through apps that have become popular, leading to high valuations of startups such as Klarna, Affirm and Afterpay.

Regulators from the U.K. to Singapore worry that young borrowers are getting in over their heads, and there's new competition from Apple Inc.

1. How did it originate?

The "installment plan" is the precursor to today's BNPL craze. Paying off purchases weekly or monthly evolved from 1840 onward, as makers of furniture, pianos and farm equipment looked to make products more attainable. Cars later brought installment credit further into the mainstream, though credit cards eventually became the preferred way to spread payments on smaller purchases.

2. Why not use credit cards?

They tend to be disliked by the young people attracted to BNPL; Britain's Financial Conduct Authority cites data showing 25% of users are between 18 and 24 years old, and half are 25 to 36. As a group, young shoppers are wary of providers that profit when customers don't pay their balances. They prefer the feeling of control they get from fast BNPL payment schedules, often spread over four to six weeks. Because of these, and because purchases are generally cheap, they're usually interest-free.

3. What's new here?

Most BNPL isn't about buying big-ticket items; it's about using an app to snap up that must-have jacket in the expectation that you'll pay it off quickly. The average spend on a transaction in the U.K. using Klarna Bank AB's app is 75 pounds ($94).

4. What drives its popularity?

The apps are simple and typically involve only minimal credit checks. Retailers — which pay the BNPL provider a small percentage of the transaction value, as they do with credit cards — frequently tell shoppers there's "no need to wait until payday."

5. What about late payments?

San Francisco-based Affirm Holdings Inc. doesn't charge late fees, nor does Klarna Bank AB on its "Pay in 30 days" product, though many of their peers do. BNPL customers who don't pay bills are blocked from further purchases and may be passed on to debt collectors.

6. Who dominates?

While Stockholm-based Klarna is still the BNPL beast, with 147 million active consumers, it's also been losing money and is coming under increasing scrutiny from regulators.

It was valued at $46 billion in June 2021, but is likely to see its value drop to about $30 billion under plans to tap investors for more cash, according to people familiar with the matter. There have been expectations about an initial public offering, possibly within the next couple of years.

Klarna's biggest rivals, Affirm and Afterpay, have millions of customers, too, and the competition is intensifying as banks, credit card companies, fintechs and shopping sites team up to go after the business. US tech entrepreneur Jack Dorsey's Block Inc., a mobile payment company, completed the acquisition of Afterpay for $29 billion in January 2022. PayPal Holdings Inc. agreed to buy Japanese BNPL provider Paidy Inc. for $2.7 billion in 2021.

7. Where does Apple come in?

At a June 2022 presentation, Apple previewed its long-in-development "buy now, pay later" feature, which splits up the cost of Apple Pay purchases over four payments across six weeks. The feature, called Apple Pay Later, includes no interest or fees. Apple will handle the lending itself, sidestepping partners as it pushes deeper into the financial services industry. Affirm Chief Executive Officer Max Levchin responded that he wasn't worried about the new competition, saying his company offered more extensive and longer-term plans and there was plenty of room for growth for everyone.

8. How big is BNPL?

The payment method accounted for 2.9% of worldwide e-commerce transaction value in 2021, or about $157 billion, according to WorldPay's 2022 Global Payments Report. That's projected to rise to 5.3% in 2025, regardless of whether Klarna or others lose market share. Europe's leading the way, with BNPL making up 8.1% of 2021 e-commerce spend. But it's rising fast in the US too: It was 3.8% of online shopping by value in North America in 2021; that's expected to hit 8.5% by 2025. Its share of North American "point of sale" transactions should reach 2% by 2025, WorldPay estimates, or more than $250 billion. In the Asia-Pacific region BNPL is projected to account for 1.8% of e-commerce by mid-decade, or $78 billion.

9. What's the worry?

That it could be a form of irresponsible lending. Some regulators are concerned that painless borrowing is a "gamification" of shopping similar to Robinhood Markets Inc.'s stock trading app, creating a sense that spending isn't real. Consumers grappling with accelerating inflation and rising interest rates could load up on debt using different apps and then overdraw their bank accounts or take on credit card debt to service their BNPL accounts. The possibility that BNPL leads people into a chain of borrowing elsewhere could create hidden risk for the banking system. The Australian Securities and Investments Commission found that, over a year, 15% of BNPL users had to take out another loan to make their payments, and 1 in 5 cut back on buying essentials. Britain's FCA says the sector must be regulated, Australia has a code of practice designed to prevent customers from borrowing more if they're having difficulty with repayments, and California has fined unlicensed lenders.

THE MONEY GAME MAY 23, 2022

Buy Now. Pay (and Pay, and Pay, and Pay) Later.

By Scott Galloway @profgalloway

Let's role-play. It's March 2021. You're 23, a year out of college. Your last semester was ruined by the pandemic, but now you've got a job with a firm that's "reinventing commerce" in a loft with reclaimed wood and catered lunches. Bars are open, your friends are coming back to the city, and your bank balance looks good, healthy even: COVID means living cheap, with free cash from the government and no student-loan payments. You lease an apartment and begin dabbling in the markets — they're all surging. You pick up tips on Reddit, trade on Robinhood, buy crypto. One of your tokens turns a modest stake into real money almost overnight. By summer, your college crew is planning a reunion, and it's time to invest in an adult wardrobe to signal your budding success. It feels weird to spend hundreds of dollars on outfits — but now there's an app for that. On TikTok, try-on hauls from Shein teach you a killer finance hack: "Buy now, pay later."

It seems smart, almost responsible. You know credit-card debt is how boomer-economy consumers wrecked their finances. And BNPL isn't credit — it's debit with fixed payments taken right from your bank account, and you're told there's no interest or late fees. It helps you plan your spending, letting you spend more now — so you do. You use Afterpay to buy sneakers from Reformation, and Klarna to defer payments on tickets from Live Nation, and Affirm to get a Peloton. Your approach to spending feels New Economy — the traditional laws of finance don't apply.

But now it's May 2022. Inflation is at a 40-year high, there's war in Europe, and the NASDAQ just registered its worst month since 2008. Crypto is awash in scams; unicorns are talking layoffs. And soon, when the student-debt vacation ends, you're going to start getting a three- or four-figure bill every month. Good luck finding the cash to make payments you still owe on fast fashion and that Peloton.

Okay, hypothetical over. Schadenfreude may feel especially good when it's directed at people who still have their hair and can shut down a bar and roll into work with a grin the next morning. But we should all have a little more sympathy for the cash-strapped youth — especially because their BNPL-fueled mistakes could contribute to an extended recession (or worse) in the broader economy. The borrowing construct is introducing real risk into the system: Consumer debt jumped $52 billion in March, the largest increase on record. In California, 91 percent of consumer loans made in 2020 were BNPL loans. More than 40 percent of Gen-Z consumers will have used BNPL by the end of the year, the highest penetration of any age group. And now those debts are going bad.

BNPL isn't the only fintech fad that's fubaring the finances of a generation. Apps like Robinhood that gamify day trading and call it investing may be worse. Options trades make up nearly half of the company's revenue. But making these kinds of bets may be more dangerous than casino gambling — you can easily and unwittingly wager much more than you have, and structural inefficiencies put amateur investors at a disadvantage to the pros. (Disclosure: I'm an investor in Public, a trading app whose business model I believe mitigates these concerns.) At least the newly popular sports-betting apps are honest about being gambling, and maybe it doesn't matter what you call it if the dopamine rush is good enough. U.S. sports betting was up 165 percent in 2021 to a record $57 billion. Crypto in its many guises, from bitcoin to monkey pictures, still has plenty of young people convinced that the blockchain is the future of money. Making it all go round are billions in venture capital spent on cutting-edge behavioral science and top-drawer design to make apps deft at harvesting for private gain one of humanity's most potent resources: the optimism of young people.

BNPL seduced a generation with a great pitch. The firms position themselves as a financially responsible alternative to credit because, per Afterpay's former executive director, young people "don't want to be on credit." If the first rule of marketing is "Give people what they want," a corollary is "Give them what they *don't* want — just call it something else." Calling debt "a better way to pay" is masterful, tapping into young people's desire for innovation right at the point of greatest vulnerability: checkout. Merchants love BNPL because it increases basket size (by as much as three and a half times) and purchase frequency. (Maybe they learned it from my industry, higher ed, which has been selling young people on "college now, pay later" for decades.)

My NYU colleague Aswath Damodaran says that the best regulation is life lessons, and getting out over your skis financially may be part of growing up. However, in an educational system where you're more likely to take yearbook as an elective than personal finance, we are sending lambs to the credit slaughter. When tested on financial concepts, only a quarter of Americans between 23 and 35 demonstrated basic knowledge. Four out of five BNPL customers said they use the service to avoid credit-card debt. And now nearly a third of them can't afford the BNPL debt. One behind-on-her-payments Klarna customer told the BBC, "I wasn't too worried because my credit score was quite good. The next time I checked, it had nearly halved."

What happens when you convince a generation to spend more than it can afford? We've seen this movie before. Literally. *The Big Short,* based on Michael Lewis's book about the 2008 mortgage crisis, features Steve Carell and his hedge-fund lieutenants talking to mortgage brokers about home loans. "Do applicants ever get rejected?" The brokers laugh. "If they get rejected, I suck at my job." Carell asks if their clients have any idea what they are buying. "I focus on immigrants," one responds. "Once they find out they're getting a home, they sign where you tell them to sign. Don't ask questions, don't understand the rates." Someone adds: "Fucking idiots."

Sound familiar? Money-obsessed finance bros covering their eyes as they exploit financial illiteracy? Good times — as long as the lines on the graphs are all pointing up. But when the market turns, contagion spreads. U.S. job losses in 2008 were the worst in half a century. Millennials are still digging out of the economic blast crater. Now their younger siblings are wondering what that ticking sound is in their inboxes. It's the arrival of past-due notices from Klarna. Listen, because when this debt bomb detonates, the shrapnel could disperse far and wide.

Klarna racked up $700 million in losses last year, and 65 percent of it was from credit defaults. Affirm lost almost the same over the past 12 months, while its marketing expenses tripled to $427 million. Any hope of profitability depends on overextended consumers somehow making their payments *and* continuing to mash the BUY button. What's more likely is that the precarious finances of the 20-something generation are going off the precipice soon, and there's a big risk of collateral damage. The 24-year-old out there defaulting on his Klarna payments isn't going to ruin just *his* credit score. The 27-year-old who lost all her money trading options on Robinhood and is trying online gambling to get it back isn't going to be a leech on just *her* parents when she zeroes out. The 35-year-old mother who refinanced her home to buy bitcoin isn't going to cost just *her* daughter her college fund.

Even if it isn't the triggering event of a global crisis, the evisceration of the finances of a generation will suppress innovation and economic growth. Western capitalism once fueled the greatest increase in prosperity in history, giving us technological advances that would have seemed like magic a few generations ago. What are we doing with that abundance? Engineering ever more insidious ways to get young people to buy disposable clothes. Torched credit ratings and mounting debt deter people from starting families and businesses. Those are the building blocks of our society and economy, and without them, we will all pay later.