



POS Finance

Instantaneous & Flexible Financing



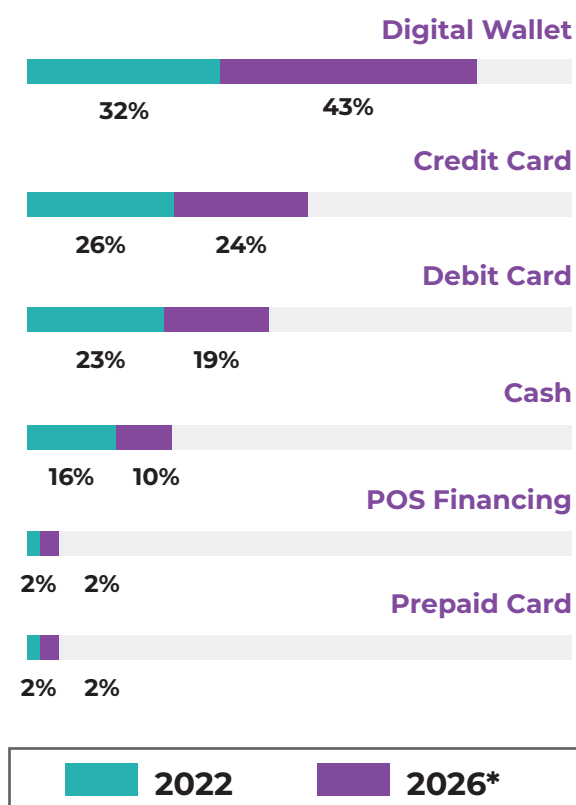


Background

Consumer credit is undergoing revolutionary changes riding on explosive growth in global e-commerce during the pandemic years. As consumers got adapted to new digital behaviors, delivering on those consumer preferences has become the new business battleground. There has been a sudden shift in consumer behavior with embedded finance and POS finance options on mobile apps and ecommerce platforms respectively. Consumers prefer digital self-service tools that allow them to choose the best finance option suited to their needs than personal interaction with a banker or loan specialist when requiring financing. Digital transformation and advanced technologies have unveiled the vast and seamless alternate credit options that are instantaneous and that provide greater transparency in making purchases by customers. POS finance is evolving by the fundamental changes in commerce, consumer behavior and rapid growth in technology.

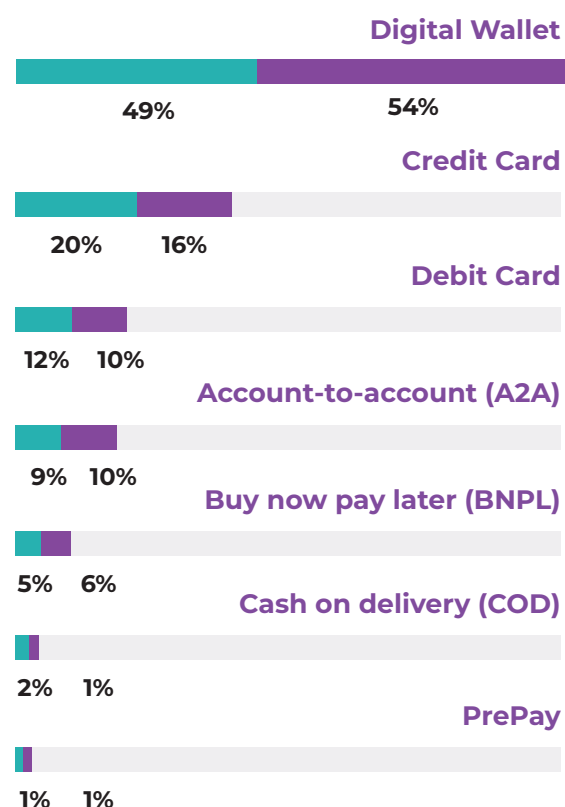
Global POS payment methods

Share of transaction value, 2022-2026



Global e-com payment methods

Share of transaction value, 2022-2026



Source: FIS Global Payments Report 2023



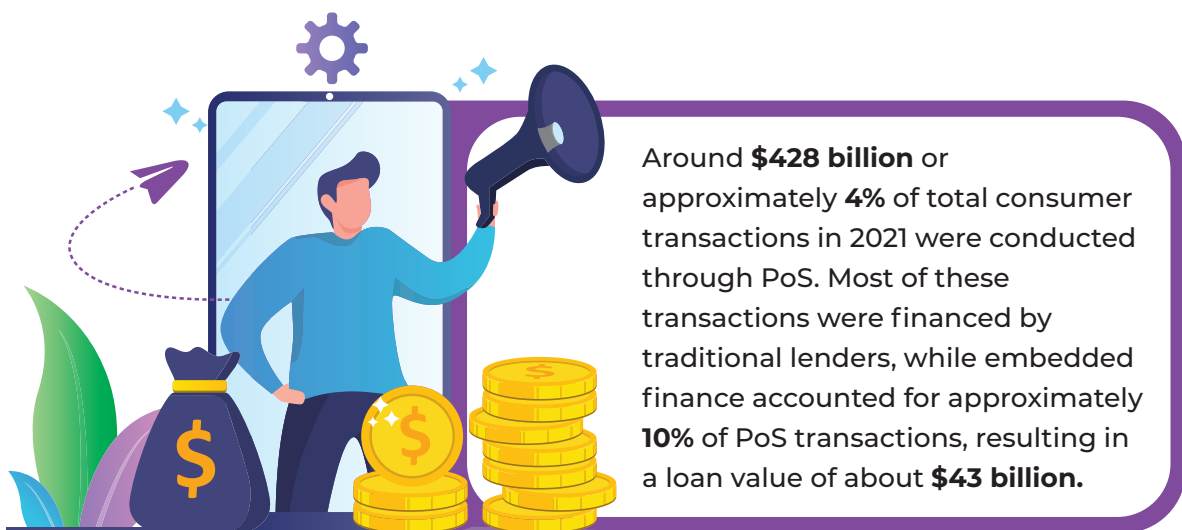
Introduction

Point-of-sale (POS) financing is a type of lending that allows customers to finance a purchase at the time of sale, typically at a physical or online store. POS financing is often offered by third-party providers that partner with retailers or merchants to provide financing options to customers.

The process usually involves the customer selecting a product, and then choosing a financing option from the available options, which can include installment loans, lease-to-own agreements, or revolving credit lines. If the customer is approved for financing, they can complete the purchase and make payments over time.

POS financing can be an attractive option for customers who want to make a large purchase but may not have the cash on hand to pay for it upfront.

Point-of-sale (POS) financing is becoming an increasingly popular way for retailers to increase sales and for customers to finance their purchases.



Source: Embedded Finance: What It Takes to Prosper in the New Value Chain - Bain & Company [2].



1. Types of POS financing options:

There are two main categories of POS financing: physical POS financing, which is offered at the point of sale in physical retail stores, and e-commerce financing, which is offered during online purchases. Both options allow customers to spread out payments over time, but the process and user experience may differ. Customers can choose from several types of POS financing options, including:

1. **Installment Loans:** These are traditional loans that are repaid over a set period of time, usually with a fixed interest rate. The loan amount is typically paid in installments, usually monthly, until the loan is fully paid off.
2. **Buy Now, Pay Later (BNPL):** BNPL financing allows customers to purchase an item and make payments over time, with little or no interest. Customers typically pay a portion of the total cost upfront, and the remaining balance is paid off in installments.
3. **Store Credit:** Some merchants offer store credit as a financing option, allowing customers to make purchases and pay them off over time. Store credit may come with special promotions or discounts and may have lower interest rates than other financing options.
4. **Lease-to-Own:** With lease-to-own financing, customers lease an item for a set period and make payments, with the option to buy the item at the end of the lease term. This type of financing may be a good option for customers who want to try out an item before committing to purchasing it.
5. **Credit Cards:** Credit cards are a common form of financing that can be used at the point of sale. Customers can use their credit card to make purchases and pay off the balance over time, with interest. Some credit cards offer promotional financing options, such as no interest for a set period of time.
6. **Split Payments:** which can be customized based on the customer's needs. Examples of split payment plans include fixed installment plans, flexible installment plans, deferred interest plans, and interest-bearing plans. Customers should carefully consider the financing terms and potential costs before choosing this option.

Each type of financing option has its own set of terms and conditions, interest rates, and repayment schedules. Customers should carefully consider their options and choose the financing option that best fits their budget and needs.



2. Embedded finance

POS Finance is a form of Embedded finance, and it has become an integral part of embedded lending. Embedded finance is a business model of offering financial services on E-commerce platforms to the consumers at point of sale without the intervention of Banks. Embedded finance offers a wide range of financial services like bank accounts, credit cards, Insurance, Investments, and lending products like Buy Now Pay Later (BNPL) to the consumers at the checkout phase.

According to a study from Juniper Research, the value of the embedded finance market was \$43 billion (about \$130 per person in the US) in 2021 and is highly likely to exceed \$138 billion – by 2026. [2] The market share of Buy Now Pay Later services is expected to be more than 50% of the embedded finance market in 2026.

Such lightning growth is the result of increasing availability of financial services APIs. POS financing companies go for barrier-free integration to generate additional revenue and create a financial ecosystem that will potentially be beneficial to all parties involved. Some renowned use cases of embedded lending are listed below.

- » Uber Money in the US offers debit cards along with digital wallets to their courier delivery employees and drivers. The company could provide 0%-interest loans through the app and allocate a percentage of their earnings for loan repayment for their contract employees.
- » Amazon Pay Later service provides a full-fledged BNPL model for purchases on Amazon India. Amazon offers this type of loan via Capital Float, a third-party lending platform, and via IDFC First Bank. The number of issued loans exceeded 1 million in less than a year.
- » Affirm, the next-generation BNPL market player from the US, generated Gross Merchandise Volume (GMV) \$15.5 billion) for the fiscal year 2022, representing an 87% increase.



3. Why is POS finance becoming more popular?

Point-of-sale (POS) financing is gaining in popularity as it offers customers a convenient and accessible way to finance their purchases while also providing merchants with a means to increase sales and revenue. With POS financing, customers can apply for financing options during the checkout process, making it a seamless experience that doesn't require a separate application or visit to a bank.

A recent report by Precedence Research states that the global buy now pay later market is experiencing a compound annual growth rate (CAGR) of approximately **43.8%** from **2022 to 2030**. The report also indicates that in **2021**, North America held the majority market share, representing over **30%** of global sales. [4]

According to data from the Federal Reserve, Point-of-sale (POS) financing makes up approximately **10%** of the total unsecured lending balances in the United States. [5]

A survey by The Strawhecker Group reports that point-of-sale financing in the United States has rapidly increased, with a total volume of **\$58.0 billion** in **2019**, up **23%** from the previous year. The report predicts that this market will continue to grow at a **CAGR of 20%** until **2023**, reaching a total volume of **\$129.7 billion**. [6]





The popularity of POS financing can be attributed to several factors:

- » **Accessibility:** POS financing is often more accessible than other forms of credit, such as credit cards or personal loans, which may require a higher credit score or longer application process.
- » **Fin tech Innovations:** Artificial Intelligence and dynamic scoring methods developed by lending -tech companies provide simplified and faster credit origination and processing which boosted the growth rate of POS financing significantly.
- » **Convenience:** With POS financing, customers can finance their purchase at the point of sale, without the need for additional paperwork or a separate application process. This can be especially attractive for customers making larger purchases.
- » **Increased Sales:** POS financing provides merchants with a way to increase sales by offering financing options to customers who may not have had the means to purchase otherwise. This can help increase conversion rates and average order value, as well as reduce cart abandonment rates.
- » **Higher customer loyalty:** By offering financing options, merchants can potentially increase customer loyalty and repeat business, as customers may be more likely to return for future purchases.

Overall, the growing popularity of POS financing highlights the importance of offering convenient and accessible financing options to customers in today's competitive retail landscape.





4. Factors impacting POS finance

1. Shifts in consumer and merchant awareness and preferences:

POS financing has been in existence for quite a long time, and examples of it include store credit cards, layaway programs, and in-store financing. Retailers have used these options to help customers make purchases and manage their finances, with some forms of financing involving interest and others offering little to no interest. The market is witnessing a positive trend in borrowers' preferences to deploy point of sale financing services more as they could get a line of sight to repay the balances comparatively at lower rates subsidized by merchants. To drive growth, emerging digital merchants rely on POS financing and hence they are more willing to integrate POS financing solutions on their platforms.

2. Intense competition among merchants and lenders:

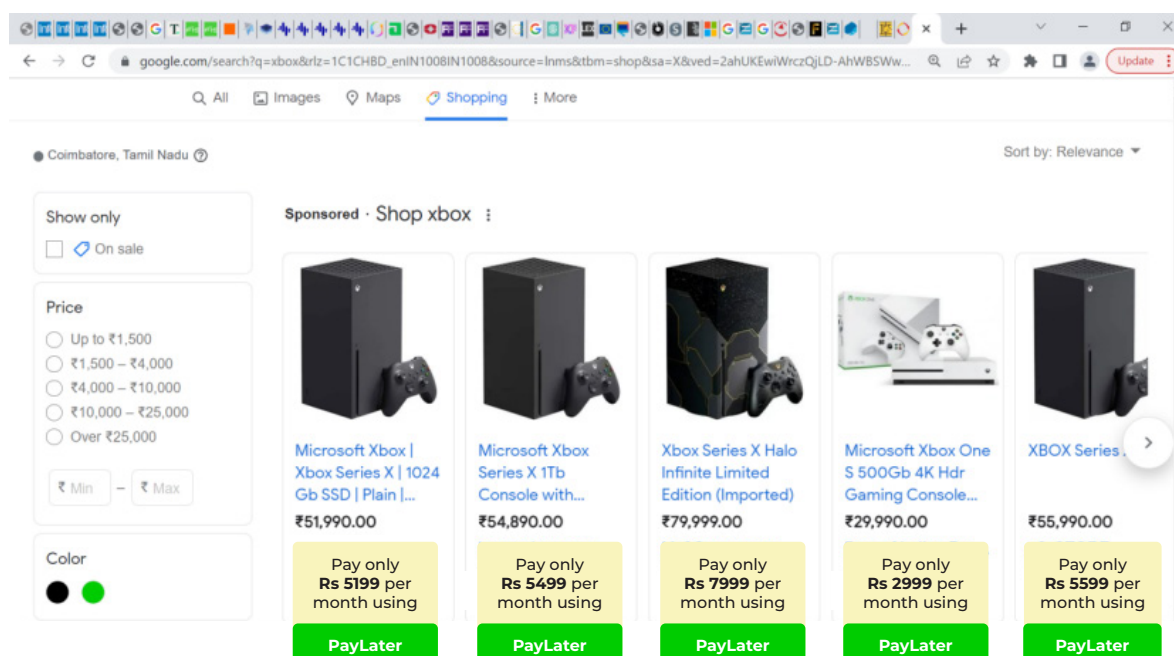
Along with the pace of consumer and merchant awareness, competition is also getting intense resulting in changing economic and risk models in POS financing. Most of the POS loans are subsidized by the merchant. New pricing models are being developed as merchants become more willing to bear interest costs. In luxury products like jewelry and other premium products, merchants offer huge subsidies in APR to capture a larger market share. POS lenders started partnering with smaller merchants and also underwriting the merchants as well as consumers, changing the risk models in POS finance.



3. Capturing market share: Earlier, the target for POS loans were lower prime or Higher Ticket segments e.g., loan for home renovation. Now greater shares of smaller tickets and higher segments are captured. Merchants have shown an increased willingness to pay "swipe fees" for various business-enhancing services, including improved authorization rates and end-to-end management of the point-of-purchase or point-of-sale financing journey. These fees vary across different channels like social media platforms and e-commerce marketplaces, with some as high as a double-digit percentage. While the benefits of BNPL, such as increased sales velocity and higher average order value, can apply to all types of merchants, those falling into the "high and medium willingness to pay" category are likely to offer more significant merchant subvention to BNPL providers.

4. Integration of POS lending into the pre-purchase phase of the consumer journey:

Consumer journey starts right from product research to checkout. Consumer adoption mostly happens when finance offerings is embedded earlier and is available throughout the purchase journey. Hence competition gets more intense as it becomes tougher for the competitors to displace lenders at the final phase of the point of sale.





5. Benefits of POS financing for merchants:

- » **Increased Sales:** POS financing allows customers to make purchases that they may not have been able to afford otherwise, increasing the likelihood of a sale and boosting revenue for the merchant. The Gross Merchandise Volume of the buy now pay later market in Sweden has experienced a surge of approximately 22% from 2021 to 2022, as stated in the 2022 Klarna Annual Report[7].
- » **Higher Average Order Value:** Customers who use POS financing may be more likely to purchase higher-priced items, increasing the average order value and overall revenue for the merchant. **As per Klarna's 2021 reports there is an increase in AOV by 45 % based on various POS finance opted by the customers [10]**
- » **Reduced Cart Abandonment Rates:** By offering financing options at checkout, merchants can reduce the likelihood of customers abandoning their cart due to high prices or lack of available credit. **There is an increase in check out conversion by 35% against the Cart abandonment rates of 70% in 2021 ,as reported by Klarna [10]**
- » **Increased Customer Loyalty:** Offering POS financing can improve customer satisfaction and loyalty, leading to repeat business and positive word-of-mouth recommendations.
- » **Competitive Advantage:** In a competitive retail landscape, offering POS financing can differentiate a merchant from their competitors and attract customers who are looking for convenient financing options.



6. Benefits of POS financing for consumers:

- » **Affordability:** POS financing allows customers to make purchases that they may not have been able to afford otherwise, by breaking up payments into more manageable amounts.
- » **Flexibility:** With POS financing, customers have the flexibility to choose financing terms that fit their budget and lifestyle, such as longer repayment periods or smaller monthly payments.
- » **Convenience:** POS financing can be applied for and approved at the point of sale, making it a seamless and convenient option for customers who want to finance their purchases without having to visit a bank or fill out a separate application.
- » **Potentially Lower Interest Rates:** Depending on the financing option chosen, customers may be able to secure lower interest rates than other forms of credit, such as credit cards.
- » **Improved Credit Scores:** Making on-time payments on a POS financing plan can help improve a customer's credit score over time, leading to better financing options in the future.





7. Implementing a POS financing program:

Implementing a POS financing program can be a complex process, but the following steps can help merchants get started:

- » **Research and Evaluate Options:** Merchants should research the different POS financing options available, including interest rates, repayment terms, and fees. It's important to evaluate the options and choose a provider that aligns with their business goals and customer needs.
- » **Partner with a Financing Provider:** Once a merchant has chosen a POS financing provider, they should work with them to set up the financing program. This may involve integrating the financing provider's software into the merchant's point-of-sale system, setting up promotional offers, and establishing the terms and conditions of the financing program.
- » **Train Staff:** Merchants should ensure that their staff is trained to offer and explain the financing program to customers. Staff should be familiar with the financing terms and options and be able to answer any questions customers may have.
- » **Promote the Financing Program:** Merchants should promote the financing program to their customers through various marketing channels, such as email campaigns, social media, and in-store signage. It's important to highlight the benefits of the financing program and make it clear how customers can take advantage of it.
- » **Monitor and Analyze Results:** Merchants should monitor the results of the financing program regularly to evaluate its success and identify areas for improvement. This may involve analyzing sales data, monitoring customer feedback, and reviewing the financing provider's performance metrics.
- » **Continuously Improve:** Based on the results of their analysis, merchants should continuously improve the financing program to better meet customer needs and achieve their business goals. This may involve tweaking the terms and conditions of the financing program, offering new promotions or incentives, or partnering with additional financing providers to expand the program.



8. Potential drawbacks of POS financing:

While POS financing can provide many benefits for both merchants and consumers, there are also potential drawbacks to consider, including:

- 1. High Interest Rates:** Some financing options may come with high interest rates or hidden fees that can add up over time. This can make it more difficult for consumers to pay off their purchases and may lead to financial hardship.
- 2. Debt Accumulation:** By offering financing options, merchants may encourage consumers to take on more debt than they can afford, leading to financial strain and potential default on payments.
- 3. Early debt trap:** POS financing can be risky if not properly managed, leading to an early debt trap. Customers especially young people can fall into this trap due to high interest rates, hidden fees, overuse, and missed payments. To avoid this, customers should carefully consider financing terms and their ability to make payments, read the fine print, understand any fees or penalties, and plan to pay off the financing amount as quickly as possible. The BNPL early debt trap has become a growing concern in the consumer finance industry. According to a survey conducted by LendingTree in the United States, approximately 40% of BNPL users reported missing a payment while 72% reported having to pay additional fees.[8] Furthermore, a report by ASIC, the Australian Securities and Investments Commission, found that one in five consumers who used BNPL services were struggling to make repayments, with some consumers accruing multiple BNPL debts. The report also found that the majority of BNPL debts were for amounts under \$1,000, indicating that consumers may be overspending on smaller purchases they cannot afford to pay back.[9] These findings suggest that the early debt trap associated with BNPL services is a growing issue that requires attention from regulators and industry leaders.
- 4. Limited Options:** POS financing may have limited options compared to traditional financing, including eligibility requirements, financing amounts, repayment terms, and merchant options. Strict eligibility requirements, limited financing amounts, fixed repayment terms and working with a limited number of merchants can restrict the types of purchases that can be made. To avoid these limitations, customers should carefully research and compare financing options before making a purchase. Factors such as eligibility requirements, financing amounts, repayment terms, and merchant options should be considered to find the best financing option for their needs.



- 5. Negative Reputation:** POS financing has a bad reputation due to practices such as misleading advertising, high interest rates, hidden fees, and negative impact on credit scores. Customers may find it difficult to pay off their financing amount and may end up in a debt cycle as a result. Customers often must read and understand financing terms, compare options, and plan to pay off the financing amount in a split second decisioning, which often is just a matter of checking a checkbox.
- 6. Declining revenues, owing to defaults:** The economics of POS lending are undergoing transformation due to the rise in competition. A significant portion, approximately 50-60%, of loans initiated at the point of sale are subsidized either partially or entirely by merchants. Buy Now, Pay Later (BNPL) is one type of POS lending which has experienced substantial expansion in recent years, attracting a high number of industry players. However, as competition intensifies and the market becomes more saturated, companies may struggle to entice new customers and sustain revenue growth. This may be exemplified by Klarna's reported full-year operating loss of 10.5 billion crowns (\$1 billion) in 2022, which marks a significant increase from 6.6 billion crowns in 2021. BNPL providers have faced challenges such as higher default rates and declining revenues. One reason for higher default rates is the lack of credit checks and strict eligibility requirements.

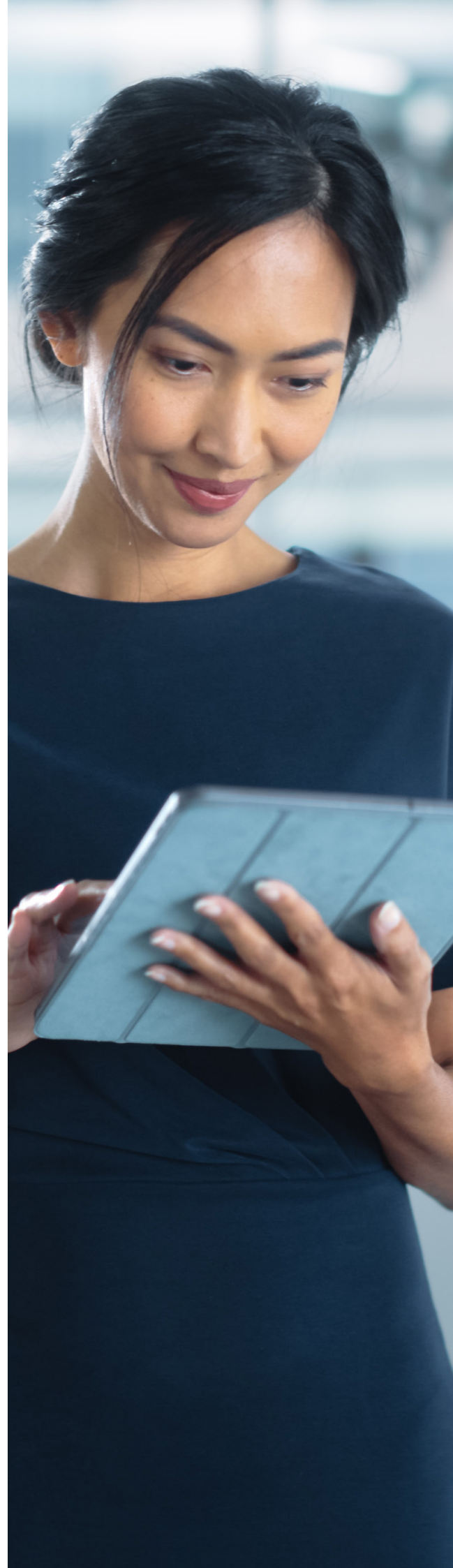


9. Conclusion:

POS financing is a growing trend in the retail industry, providing benefits for both merchants and consumers. By offering financing options at the point of sale, merchants can increase sales, improve customer loyalty, and differentiate themselves from competitors. Meanwhile, consumers can make purchases they might not be able to afford upfront and pay them off over time, with flexible repayment options.

However, it's important to consider the potential drawbacks of POS financing, such as high interest rates, debt accumulation, and complexity. Consumers should carefully evaluate the financing options available to them and ensure they can afford the payments, while merchants should be transparent and upfront about the financing terms and conditions.

Overall, POS financing can be a useful tool for both merchants and consumers when used responsibly and thoughtfully. By offering financing options that align with customer needs and preferences, merchants can build stronger relationships with their customers and drive growth for their business.





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