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How Buy-Now-Pay-Later is creating huge new financing opportunities in Africa

This is the Age of ‘Instantly’ and today’s consumers want everything **now** – except when it comes to paying.

“BNPL Gross Merchandise Values could rise five-fold by 2028”

A buy-now-pay-later (BNPL) craze is sweeping the world and Africa’s consumers are certainly up for it. Not surprisingly, banks, fintechs, financing companies, payment services providers, and merchants are considering how to get a slice of the action.

And that’s not surprising because BNPL is potentially big business – very big business. In Europe, the foremost player Klarna recently raised US$639 million in a funding round which valued the business at US$45.6 billion making it Europe’s most valuable start-up. Most of the world’s pioneering BNPL players are fintechs (Klarna, Affirm, AfterPay, Cashper, Divido, LayBuy) but global payment brands such as PayPal and even AmEx are also moving in.

With the right approach, BNPL means not just a new way of slicing up the unsecured loans market, but a way to massively expand it.

Nigeria, for example, is seen as ripe for an expansion of the BNPL market. According to a February 2021 report[1], BNPL payment is expected to grow by around 20% a year (CAGR) until 2028. The BNPL Gross Merchandise Value could increase from around US$ 200 million in 2020 to US$ 1,200 million by 2028 – a five-fold increase.

Challenging economic conditions in African countries such as South Africa and Nigeria could fuel further demand for BNPL as consumers seek new short-term credit opportunities.

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[1] Nigeria Buy Now Pay Later Business and Investment Opportunities (2019-2028) Databook

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While the development of 'pure play' (0% interest) BNPL products has been much slower in Africa than in some other regions, emerging alternatives to traditional credit scores could change that, allowing players in the market to offer interest-free options while maintaining appropriate standards of risk management.

What is BNPL?

Buy-now-pay-later is not a one-size-fits-all concept. McKinsey and Company[2] has identified five types of 'point of sale financing':

- Integrated shopping apps
- Off-card financing solutions
- Virtual rent-to-own (VRTO)
- Card-linked instalment offerings
- Vertical-focused larger-ticket plays

But the model which has caught the imagination of consumers and swept the world is the simple 'Pay in 4' concept. Instead of paying for an item or service outright at the time of purchase, the consumer pays in four scheduled interest-free instalments.

A wide range of products describe themselves as BNPL but the most common characteristics are:

- Short-term financing – weeks or months, not years
- Interest-free
- The financing is unsecured
- Items with low or modest ticket prices
- Offered for a specific time, place, or product (i.e. not a general line of credit)
- Offered or activated at point-of-sale (whether in-store or online)

There is no single shape to BNPL products and there is considerable overlap or conflation between 'true' BNPL products and other credit products such as personal revolving credit lines.

Consumers like BNPL because it advances affordability (or makes a higher number of purchases affordable at the same time) and – unlike traditional credit products – there are no interest charges. Many BNPL products are very

[2] Buy now, pay later: Five business models to compete. McKinsey & Company. July 2021. mckinsey.com/industries/financial-services/our-insights/buy-now-pay-later-five-business-models-to-compete

convenient – available at the time and point of purchase with minimal additional steps – and may not require a traditional credit check.

The BNPL business and risk models

Retailers are embracing BNPL for the simple reason that they bring in more sales and new customers. For online merchants, BNPL means not only bigger baskets but fewer abandoned ones. Although these benefits may be offset by the cost of offering BNPL, it may now be a case of 'play or go home' as BNPL becomes an option consumers expect to be offered.

> "BNPL is becoming an option consumers expect to be offered"

It's possible for merchants to run their own BNPL service but the most common arrangement involves partnering with a third-party BNPL supplier. These are often fintechs and some have been set up with the express purpose of supplying BNPL, but finance companies, payment service providers, neo-banks and – to a lesser degree – traditional banks have also entered the game.

The business model usually involves the BNPL provider charging the merchant a commission fee which is considerably higher than the transaction fee charged by debit/credit card providers. In return, the BNPL usually assumes all subsequent activities and risks including defaults and liabilities arising from fraud and so on.

Lay-bys (Africa's Pay-Now-Buy-Later tradition)

Africa has a long-established and prevalent tradition of lay-bys, also known as layaways. Under these agreements, a consumer can purchase an item by interest-free instalments. These are usually over a period of no more than three months, and often require a minimum down-payment of 20%. The store retains the item until it has been paid for in full before releasing it to the buyer. Rather than buy-now-pay-later, it's more like pay-now-buy later.

The lay-by tradition has followed shopping online. For example, Spredda – the Nigerian online marketplace – offers a lay-by option at checkout.

Lay-bys may currently be the only pay-by-instalment option available to consumers with no credit score, trust rating or ID. Fintechs such as LayUp (see below) are digitalising the payments process of brocks-&-mortar lay-by so that consumers no longer need to physically visit the store to make their payments.

It will be interesting to see what proportion of lay-bys BNPL manages to replace.

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Who's involved?

There are already dozens of BNPL brands active across Africa. Here is a sample.

Carbon Zero is a Nigerian player offering interest-free instalments over three months.

The Kenya BNPL start-up charges merchants a transaction fee and customers a monthly interest rate.

South African fintech LayUp Technologies is digitalizing the lay-by agreements market (shops agree to keep goods for up to six months while buyers pay in instalments – a sort of Pay-Now-Buy-Later).

Spreads purchase costs interest free across four equal interest-free payments, over six weeks at over 850 online stores (South Africa).

The South African PayJustNow allows shoppers to split payments over three months, with no fees or interest. It's a partners range from big international brands to small independent shops.

Nigerian company PayQart lets users pay for goods and services in instalments over a maximum period of six months. It charges both the consumer and the partner merchants.

In addition to the consumers, merchants, BNPL providers, financing organisations, and credit/ trust scorers, other players such as M-Pesa, mCash, and Remita are often needed to handle the repayment side of the equation.

Around the world, fintechs such as Amount, Jifiti, and Certegy are producing white label products which make it easier for organisations to quickly set up their own BNPL offering.

Boom or bubble?

One of the reasons (other than consumer demand) BNPL grew from nothing into a multi-billion dollar industry within the space of a few years is that in many places, BNPL sidesteps the regulators. Much BNPL financing is technically 'interest free', but the penalties for defaulting on repayments are sometimes punitive and frequently not made obvious to consumers. Unregulated BNPL providers have no obligation, for example, to be confident of the purchaser's ability to repay. In many countries there has been increasing demand for regulators to step in.

The huge potential of BNPL in Africa

The backdrop to BNPL

According to figures from global payment services provider Worldpay from FIS[3], many sectors in the Middle East and Africa (MEA) are set to enjoy a period of significant growth. For example:

- E-commerce is expected to grow by more than 18% annually through 2021-2024 with Nigeria seeing the fastest growth at 24%
- When it comes to e-commerce payments, digital wallets are set to gain most ground, growing 45% to account for more than one fifth of e-commerce spend by 2024. The gains will largely be at the expense of COD (currently the second leading payment option after cards).

While the COVID-19 pandemic had a devastating impact on bricks-and-mortar stores in many parts of Africa, these establishments are also dealing with massive changes in payment preferences and habits. Cash payments at point-of-sale (POS) fell by over a quarter in 2020 in the MEA region.

Some parts of Africa have seen even more dramatic changes. In 2019, cash payments accounted for 91% of POS transactions in Nigeria. A year later, that figure was 69%. Meanwhile, the use of mobile wallets is increasing and are expected to double their share of transactions by 2024.

BNPL potential in Africa

There are good reasons for believing BNPL is on the verge of a boom.

1. **BNPL is generally more popular with younger people** and the population of people in the continent is heavily skewed in this direction. The African median age is 20 (18 in Nigeria).
2. **With many economies in the doldrums, the offer of BNPL becomes impossible to decline.**
3. Traditional credit is accessible by a tiny minority – around 5% in Nigeria, for example. **There is a huge market for services which can access people outside this select group**.
4. Finally, there's the increasing **availability of 'alternative' sources of credit or 'trust' scoring**.

[3] The Global Payments Report. Worldpay from FIS. 2021. offers.worldpayglobal.com/rs/850-JOA-856/images/1297411%20GPR%20DIGITAL%20ENGLISH%20SINGLES%20RGB%20FNL11.pdf

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The rise of alternative scores

In much of Africa, loans are difficult to come by. Many banks have no appetite at all for retail loans. Digital lenders are now rushing to fill the gap and instead of looking at clunky credit scores, they are taking other available data and using tools such as algorithms and artificial intelligence (AI) to assess trustworthiness.

A consumer's smartphone data is one very rich seam of data. GPS data can reflect how regular a person's habits are; call records can reveal what kind of company they keep. Access to your mobile wallet data helps compile a picture of an individual's spending and top-up habits.

The idea of scoring 'credit-invisible' markets has caught the attention of global players. For example, credit score specialists Experian recently announced a partnership with FinScore (see panel) which delivers telco data credit scoring to unbanked and underbanked people in the Philippines.

Alternative approaches in Africa include fintechs such as CARMA, a credit data marketplace designed to help lenders make loan decisions by accessing each other's customer records. Another player is Migo which builds algorithms to help lenders quantify the risk involved in lending to low-income customers.

How does telco data scoring work?

Telco data can be used to assess an individual's credit worthiness without needing to access credit history. FinScore does this by analysing more than 400 telco variables.

These include data and voice usage, top-up patterns, location, and SIM age.

Companies use machine learning or AI on the data to produce alternative credit assessment scores which have proved highly reliable.

Although some may feel queasy about the flow of personal data or the lack of transparency, these new approaches do potentially offer social value: They open up new sources of credit for people who previously had access to none. They present an opportunity to end reliance on informal loans and the unlicensed money lenders who charge up to 30% a month.

Who wins?

Amazingly, the answer could be 'anyone with an appetite for developing new products based on unsecured lending'. The size of the market is not a limiting factor, that's for sure. For rural banks, finance and lending companies, it's not such a big stretch from what they are doing now to what's involved in BNPL. A little rebranding may be all it takes, plus the ability to hook into the new breed of credit score/trust services via APIs. What's changing is the demand – from consumers and from merchants – both online and in bricks-and-mortar stores.

With commercial banks lending only to the most affluent sliver of the population, the field is wide open to providers with the right appetite for risk or, perhaps more importantly, the imagination to embrace the new ways of credit scoring that promise to mitigate the risks of uncollateralised loans.

The risk to the industry's reputation and to society at large lies in BNPL advancing without mitigating the risks. In Kenya between 2014 and 2017, a shocking 2.7 million people (about 10% of the population) were blacklisted on the country's TransUnion credit reference bureau for failing to repay digital loans - 400,000 of which amounted to less than $2.

Want to launch a BNPL product? Here's what you need from your core platform

Scalability

BNPL is a rapidly growing market with huge potential. Instafin, Oradian's cloud-based core banking platform, allows for limitless, uninterrupted growth. And our SaaS pricing model means you only pay for what you use. Instafin helps you grow, and grows with you.

A reliable loan management system

A robust and flexible loan management system such as Instafin's is essential. It's vital to ensure that the entire loan lifecycle is handled as simply, efficiently, and effectively as the CX at the point-of-sale. Without it, customer relationships will turn out to be short-lived.

Speed to market

As we've seen, behind the simple fundamental concept of BNPL lie endless variations. To compete in this market, players must be willing and able to develop new loan products and take them to market rapidly. Instafin vastly reduces the amount of time it takes to do this.

Fast flexibility

The key to staying competitive is being able to adapt fast to an ever-changing market. The most reliable credit/trust scoring services of today may not be those of tomorrow. It's only possible to adapt and change quickly through a core system's deep and open APIs.

Limitless interoperability

As with most modern financial products, BNPL involves multiple partners:

- The BNPL provider
- A financing company
- Online and/or offline retailers
- Traditional or alternative credit/trust score providers

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- Repayment channels

Linking between multiple (and potentially changing) partners in a process that is seamless to the customer requires agility, flexibility, security, and speed. This is a combination that can only be provided through open APIs.

For example, compare the customer experience involved in being asked to upload bank statements as proof of income with simply requesting permission to access bank statements through an open banking API.

Of course, open APIs are also an essential part of the repayment process to seamlessly allocate payment made via a variety of channels such as M-Pesa, mCash, Remita and so on.

Instafin is designed to connect with the ever-evolving financial ecosystem using Open APIs, making it quick and easy to connect with – for example – the alternative credit scoring services of today and tomorrow.

Instafin is future-proof.

Your next steps

Do you need a solid platform on which to run your BNPL loans?

Are you a financial institution looking to launch new BNPL products?

Then we can help you.

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Let's grow! Start your journey here:

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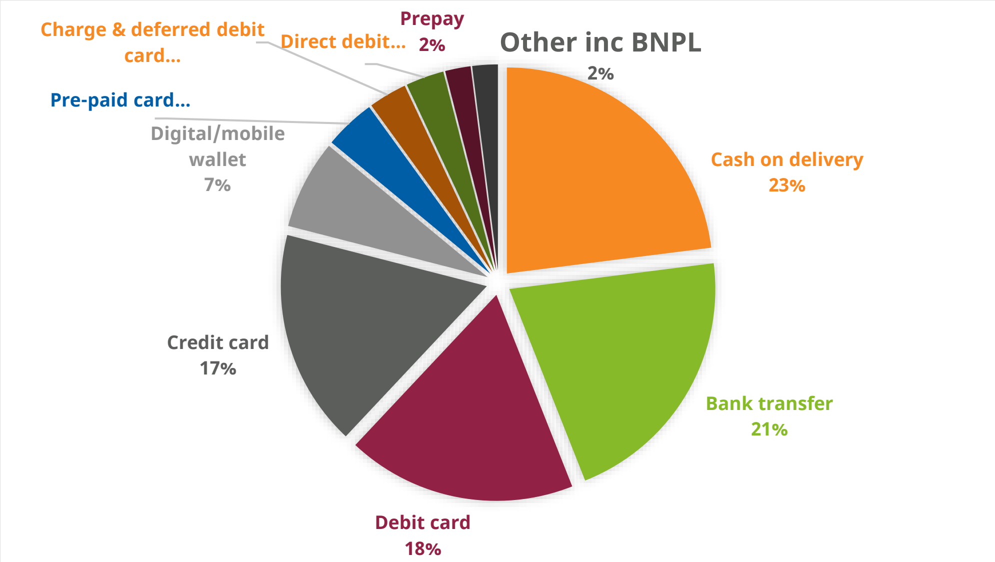
Source data

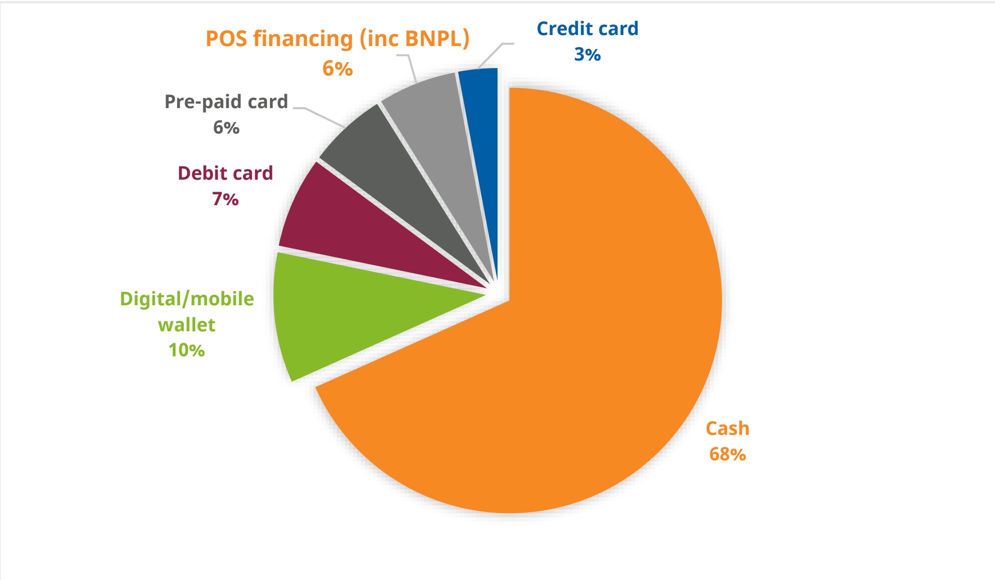
2020 e-commerce payments mix in Nigeria

Source: Worldpay from FIS Global Payments Report 2021



2020 point of sale payments mix in Nigeria

Source: Worldpay from FIS Global Payments Report 2021



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