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Presentation Participants

Affirm

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Jefferies

John Hecht, Equity Research Analyst

Turpin Senou, Sales & Trading

Presentation

John Hecht

Okay, well, welcome to first of all, Rob. Thanks so much for being here. Good to see you and sorry I can't be across the pond with you. But I'm John Hecht and I'm the senior analyst at Jefferies. I cover Affirm. As we all know, Affirm is a point-of-sale finance company that predominantly engages in buy now pay later type of transactions and transactions processing. It's a technological based platform that allows merchants and consumers to seamlessly engage in transactions. And in some cases, engage in services around transactions like financing of the transactions and all the settlement associated with transactions.

Affirm's been -- it's the largest buy now pay later in the U.S. Its key partners include Amazon and Shopify. It's currently entering into the U.K., so we'll get an update on that today. The company has very attractive growth, top line growth in the mid 20%, customer growth over 20%, and then it's been -- we've been seeing a very attractive expansion of operating margins and earnings power. The company has also done a remarkable job in managing expenses and managing credit risk through what we perceive to be as a somewhat challenging credit cycle the last two or three years. So it's done a very good job.

And most importantly, it's growing fast and it continues to gain momentum and gain market share in the U.S. where the option of buy now pay later transactions, it's still very rapid. So with that, I want to introduce Rob. Rob is Affirm's Chief Financial Officer. He's been with the company a few years, but just recently was promoted to this title. He's been Chief Financial Officer at Tile and in the same role at Spark Networks. So a very good, extensive background in this type of role and high growth company. So again, Turpin and I will manage this fireside chat here for the next 30 minutes or so. We'll go back and forth trying to address all the key topics and questions for Affirm.

But towards the end we may offer an opportunity for people in the audience to raise their hands as well. So if you have a question, think about that and we'll call on you at that point in time. So, first, again, welcome, Rob. First is the key take from the quarter. You guys recently reported a strong quarter. Maybe can you talk about what were the positive surprises and other worthy call outs from the last quarter of operating trends?

Rob O'Hare

And thanks for having me, John, and thanks for the lead in and the intro there. The third quarter, we have a June fiscal year so our third fiscal quarter, which was the March quarter, it was a really strong quarter, I would say, across the board. We grew our consumer, our active consumer base, by more than 20%. We also grew the number of active merchants on our platform by more than 20%. So those are really important leading indicators of the size and health of our network.

And the growth in the network translated to our third consecutive quarter of accelerating GMV growth. We grew GMV 36%, which was faster than the same period in the prior year. So we're really proud of those stats. And again, I think it's a testament not only to the strong relationships we have within our merchant base, but also just the increasing interest that consumers have in our category. The category itself, we believe, is growing about 25%. So we're a clear market leader growing slightly faster than the market at large, but it's great to have those tailwinds in terms of consumer adoption and that's ultimately a big function of our growth.

Looking at the P&L, we grew revenue in line with GMV, our measure of transaction profit, revenue less transaction cost grew north of 50% in the quarter and the strong growth there translated to really nice adjusted operating income as well. We had about a 22% margin in the quarter. That's about nine points of margin expansion on a year-over-year basis. So all of the growth that we've seen for the last several quarters is really helping to drive a nice scaling in terms of profitability as well.

And then lastly, we're really proud of the growth that we saw within Affirm Card. Affirm Card, for those of you that haven't used the product, it's our direct to consumer offering. It has the functionality of a debit card, but it has the capabilities of Affirm financing embedded as well. And that product grew to 1.9 million active cardholders, so just under 10% of our active consumer base. And it grew to be about 9% of our GMV, so north of 100% growth rate in the quarter as well.

So really a product that we're very excited about and a product that continues to scale really, really nicely. So we're really proud of how we showed up this quarter, strong growth leading to strong profitability, but also doing, I think, really important things to expand the network.

John Hecht

Okay, that's a good kind high-level intro. We'll get into some of those topics a little bit more deeply. But you did talk about GMV upside and good GMV trends overall. Can you talk about where you're seeing an upside? Is there certain channels or transaction types or transaction characteristics that you're seeing? Or has it generally been fairly broad in terms of the momentum there?

Rob O'Hare

Yes, I hope it's not an unsatisfactory answer, but the growth actually really was very broad-based. We had two categories in particular, general merchandise and consumer electronics that led the growth from a category perspective, and general merchandise happens to be our largest category as well. But otherwise, we saw really strong growth in almost every industry vertical that we track. You can also look at our growth in the quarter based on product type. We do a mix of loan products. We do pay in four loans, which are also common amongst our competitive set, but then we -- about 85% of our business is done through monthly installment loans that are three months or longer.

And each of those loan products grew really nicely as well. We saw the strongest growth, growth of about 44% within our monthly 0% installment loans. We think that's a pretty differentiated product in the industry. It's not something that our competitors are doing at scale, and it converts really, really well for our merchants, and it's a product that our consumers really like.

It gives them, obviously, the low cost of borrowing through a 0% loan, but we're able to extend the term lengths beyond a pay in four loan and go out three months or longer. So we're really happy with how the loan product is shaping up in terms of mix and ultimately it's that mix that helps drive some of the profitability that I mentioned that we demonstrated in the quarter.

John Hecht

Okay. And then just touching on margins in the quarter, your product level margins or the gross margin, or we call it the RLTC, Revenue Less Transaction Cost, that has trended nicely, but also had upside relative to our expectations. Similarly, but I think from different sources, the operating income margin has also trended nicely. Maybe you can take us through what you, in terms of the product level mix, or efficiencies are scaled, what you're doing to enhance margins there, and then similarly at the operating at some level.

Rob O'Hare

Sure, good question. In terms of the RLTC margins, we've established long-term or a long-term framework that we want to be between 3% and 4% on that metric as a percentage of GMV. And in three of the last four quarters, we've been slightly above the 4% mark. So, we're operating at or above the high end of what we think the long-term range for the business should be. And really what drives the RLTC take rates in a given quarter is going to be our loan product mix. And in the third quarter, we chose to lean in and had outsized growth, as I mentioned, in our monthly 0% loans.

Those loans are nicely profitable for us and they tend to attract a borrower from the higher end of the credit spectrum versus our interest bearing product. But because we had slightly more mix of those loans, we feel like that's a good way for us to manage the overall profitability while also maintaining focus on what we believe is a pretty important and large market opportunity in the U.S. So we want to make sure that we balance growth with profitability and doing a bit more on monthly installment loans that are 0% APR, that's a way to make sure that we have a wide aperture and are putting loan products in front of borrowers of all types that are going to resonate with those borrowers.

Turpin Senou

Customers are obviously at the core of what you guys do, and new customers growth has been very strong, about 20%. Can you talk about the evolution of customer acquisition? And also if you can specifically talk about the differences between existing customers and new customers in terms of spend and engagement, for example.

Rob O'Hare

Really the lion's share, almost all of our customer acquisition comes from our merchant partners. We want to make sure that we're visible and as up funnel in the purchasing decisions of a consumer as they're navigating our merchants at our partners' sites. Most of what we do is at ecommerce today, so getting prominence on the product display page is really important for us. We want to be as up funnel as possible. We really don't have any sort of scaled direct to consumer marketing efforts, so point of sale really is the primary tool for user acquisition and for network growth from a consumer perspective. Sorry, could you repeat the second part of the question?

Turpin Senou

Yes, in terms of the differences between new customers and existing customers in terms of spend and engagement with you guys.

Rob O'Hare

Yes, I mean, when you look at the data on a cohort basis, because we have very large coverage of U.S. e-commerce, we've seen that new cohorts of consumers are transacting more frequently and therefore also spending more with us. You can see that also in our frequency metrics. Our frequency grew to north of 5.5 transactions per user per year while we're also growing the consumer base at roughly 20% clip. So, we're seeing really nice uptake and very strong performance on a cohort basis as we've continued to grow the network.

John Hecht

Okay. Thanks very much. Yes, you talked about, Rob, just general expansion of the TAM, but then also we noted that Affirm has been gaining share in the current environment. Maybe on the TAM, yes, I'm sure there are certain products you guys believe you're taking share from like credit cards. Maybe talk about that. At the first part of the question, let's talk about where do you think buy now pay later is really taking share from? And then you're growing faster than the market -- within the market who are you taking share from amongst your competitors?

Rob O'Hare

Yes, good question. I think absolutely we're taking share from credit cards. I think that is the largest addressable market for us. There's roughly \$1.2 trillion of revolving credit card debt outstanding in the U.S. and there's roughly \$4 trillion of annual credit card spend in the U.S. So, buy now pay later, Affirm in and of itself, I mean, we're a very, very small portion of the broader, what we would argue consumer credit market if you're including credit cards in the picture.

So, obviously the category Affirm itself is growing multiples of what credit card growth rates are and so, we think that's again, a testament to the fair and honest financial products that we put in the hands of our consumers and consumers discovering Affirm at stores and merchants where they're already shopping and having a good experience and wanting to repeat with us. So we think we have a nice flywheel and again I think it's inherent to the ways that we treat the consumer and that's a really important -- internally that's incredibly important to us that we never charge a penny of late fees and that we are aligned with the consumer and don't profit if the consumer were to stumble, right?

So there's no ability to revolve, there's no late fees in our ecosystem and that's incredibly important to us and I think that's helped us grow the business nicely. I think that resonates with merchants, which merchants I believe are increasingly aware of the financing products that are being pushed to users from their surfaces and they want to make sure that those financing products do right by the consumer. So I think the combination of all of those things is helping us to grow faster than even the BNPL industry, which is very growthful at roughly 25% a year.

Turpin Senou

Rob, so how competitive is the market now? Any update you can give us there? And obviously, we can't talk about competition without talking about Klarna. Have they -- anything you've noticed differently from them given the IPO process that they've started?

Rob O'Hare

Yes. I mean, the market continues to be competitive. I would make a point that most of the competition we see tends to cluster around the pay in four product in the U.S. You look at our mix of loan products, it's about 15% of what we do. When you look at our competitors, it tends to be the large majority of what they're doing. So that really is the most competitive of the competitive surfaces within the industry. We typically go to market with merchants with a product that we call adaptive checkout, which allows us to change the mix of loans that are offered to the consumer on behalf of the merchant. And typically we put three options in front of a consumer.

And so we can set up a program where one of those options is a pay in four option, but the other two might be monthly installment options, either 0% or interest bearing options. That allows us to craft a program that works for the merchant in the context of what the merchant's objectives are for bringing on a financing partner. Sometimes, to be honest, that's cost of acceptance. Some merchants are laser focused on getting their cost of acceptance sort of down or in line with what they're paying for credit cards. But in some cases, merchants are really laser focused on conversion.

And by being able to extend our financing offerings and doing longer terms than what our competition typically does, that helps us show up well if that's the rubric that the merchant is applying. So really we pride ourselves on creativity and the flexibility that we can bring to our financing programs. And I think that allows us to show up well and really meet the merchant wherever they're at in terms of their margin structure, in terms of the goods that they're selling.

And then in terms of Klarna, I think Klarna's been a competitor of ours for the entirety of my tenure at Affirm. I've been here almost five years. They've grown the business in the U.S. The U.S. is an expansionary market for them. We bump into them in RFPs. We're aware of them. I can't comment on how a financing event like an IPO is going to dictate their near-term strategy. But yes, I mean, we definitely bump into them in the market.

John Hecht

Okay, and you -- I want to turn to the consumer now. I think that's a big topic, just spend trends, credit trends, how are they considered? It seems like in the U.S., predominantly, the consumer's been more

resilient than maybe we would have expected. How do you guys see spend trends, payment trends, and maybe just give us kind of an update of the flavor of the consumer from your perspective.

Rob O'Hare

Yes, we called out in the last quarterly call that we did see accelerating growth over the course of our March quarter. And so March was the highest growth month that we had in the quarter and we grew GMV about 40% in that month. It's really hard for us to ascertain was that pull-in from the tariffs? I think that's one of the theories that's out there. Or was it just a change in consumer engagement, maybe partially driven by the 0% programs that we were leaning into at the time. Those convert really well with consumers.

For what it's worth, we saw that growth continue to be at roughly the 40% level in April as well. We showed that on the last call. We really haven't given an update beyond that, but suffice it to say, we did see accelerating growth over the course of Q3, and we saw strong growth in April. We have guidance out for GMV in the quarter that is at the 34% level. So we did bake in some conservatism that the growth that we were seeing in April would not subsist, but we really haven't given an update much beyond that.

I think whenever we see a change in consumer purchasing patterns, I think we're trained at Affirm to make sure that we're not changing the credit profile of that incremental volume that is coming in. And the good news is that's been the case for us. We've seen credit outcomes continue to be right in line with expectations. We're seeing delinquencies that are in line with past years. So, the consumer from a credit perspective, despite maybe some outsized demand, the delinquencies are right in line with expectations that we're seeing really strong credit performance.

John Hecht

And then consumption trends, has there been a shift to or from discretionary worth noting or has it been fairly stable the past few quarters?

Rob O'Hare

No. I mean, as I mentioned, really we saw growth north of 20% in literally every category with the exception of sporting goods. And I think there's some idiosyncratic things about our sporting goods portfolio that lower growth there makes sense to us. So yes, so the growth has been very broad based as we outlined in the Q3 results.

John Hecht

Okay, and turning to funding balance sheet consideration, just to touch on that briefly, maybe first question on that is talk to us about how interest rate impacts the business. Can you kind of give us sort of some high level framework to think about sensitivity to changes of rates?

Rob O'Hare

So, when you look at our loan book, our average term length is about 12 months, typically, and our weighted average life, because our loans pay down on a monthly basis, our weighted average life is about five months. So the relationship between those two numbers is 0.4. And so we've established a framework externally that if you think about a one-point movement in rates in either direction, the impact to our funding costs should be four-tenths of that movement in rates.

So it's important to remember that the duration in our loans is quite short, and that insulates us a bit from movements in rates. We also fund the business through a handful of different funding channels. Some of those funding channels are floating rate debt instruments. Some of them tend to have a fixed component

or even a more episodic repricing that's reflective of rates, but not immediately. So that four-tenths movement for any change in rates, really you need to think about that over maybe a one-year or even a two-year time horizon. So I think we're a lot less sensitive to rates than it may appear from our business model alone. So yes, that's how we think about movements in rates.

John Hecht

And then funding markets. Like you've got a lot of capital raising within private credit. It seems like the asset-backed securitization markets are relatively strong now. You guys have announced some good off-balance sheet funding partnerships, like with Sixth Street. Talk about how these constructed funding markets. Do they impact your thinking or your strategy in terms of which way you're going to take the balance sheet or is that just a function of what's in the market at that time?

Rob O'Hare

Yes. No, we have an amazing team within Affirm that we call the capital team that owns all of those funding relationships for us and really does an amazing job of making sure that funding never has been, never will be a constraint to growth in the business. So we're really fortunate to have that team and they've had an amazing last year with some of the large partnerships, really strong execution on the ABS markets as well. So yes, we ended the March quarter, I think with \$23 billion of funding capacity, which is a high watermark for us.

But maybe more importantly, we were at, I think 59% utilized within that funding, which is a low watermark for us, which is a really great number to have too, especially as we're seeing this accelerating growth and outsized growth in our business. So yes, we're really proud of the capital markets team. They've had an amazing run over the last year and I think there's a lot of growth to come. On your question around, does it impact the on versus off balance sheet? For those of you that didn't see it, the Sixth Street partnership is quite large. It's also a three-year relationship. It's a \$4 billion commitment with a three-year time horizon.

And so it's the largest forward flow relationship that we've ever brought into the platform. And so on the margin, that may mean that we're slightly more off balance sheet with our funding just because we do have this new large partner that wants to put money to work with us. But other than that, we're always looking to add capacity across all three of our funding channels. As we add more capacity, we're able to -- or as we add more volume and collateral, we're able to do larger ABS deals as well. So, I think there's been nice growth across the board and it won't really change our biases in terms of on versus off balance sheet.

Turpin Senou

Rob, there is obviously a new administration in the U.S., just in case anybody didn't notice that. We've all felt it one way or the other. So my question is on regulation. Is there any update on regulation you can give us or any changes coming up that you can talk about?

Rob O'Hare

Really, I mean, nothing to report. I mean, there has been some turnover at the CFPB with the change in administration in the U.S. We don't really look to the CFPB to set the product roadmap for us and we want to make sure it's a huge part of our value proposition to both merchants and to consumers that we treat the consumer well, that we're transparent with our products. And so I don't think that we've ever been quote, unquote -- close to the line -- in terms of how we've created products that we put in the hands of consumers.

We want to align with consumers. We have a business model that does that by not ever charging late fees and not having compounding or revolving interest in the product. So, again, we're of course aware of the

regulatory environment and there's been some changes with the new administration, but it doesn't really change our roadmap or change the product set that we want to offer.

John Hecht

Okay. We've only got a couple of minutes left. So if anybody in the crowd has a question, go ahead and raise your hand and Turpin, I'll let you – let me know if anybody is raising their hand because I can't see the audience.

Turpin Senou

Yes, there's one.

Unidentified participant

Thank you very much for your presentation. I think I just want to get a better understanding of two parts. One is, as we really alluded, there's a lot of competition. How easy it is for Affirm to write in any sort of clause that if you merchant only use Affirm, then we are your exclusive partner. You can't take on any, so say Klarna or say Afterpay as an additional BNPL option. And then I want to focus on the time discussion that you previously talked about. I recognize that you're taking market share from credit cards. How many of this volume do you think is actually, I guess, tackable for Affirm? Because I assume there's a good chunk of credit card deals that are people say, oh, I can get a good miles or good bonuses from these credit cards, but I'm paying it down every month, and therefore I will only use this for a working capital option, not really an installment type of payment.

Rob O'Hare

I'll take them in order. In terms of the merchant contracts and pushing for exclusivity, I would say the merchant engagements we have, we have 350,000 different merchants that are active with us. They really take all the forms you might be able to imagine. So we certainly have contracts that have periods of exclusivity that can range from one year to three years to maybe even five years in some cases. And then we have integrations with merchants that maybe started as an exclusive, but the exclusivity's gone and we're earning our prominence with that merchant by showing up well and driving conversion for them.

We also, increasingly, we're winning deals that are what we call side-by-side deals where maybe the merchant started with a competitor for whatever reason, but now that the exclusivity has lapsed, we're able to come in as a second provider of financing. And because we have a different product set than most of our competition, we're able to drive real incrementality even as a second provider for those merchants.

So, we really -- I helped lead our pricing efforts that are at the table for a lot of these merchant discussions and we really pride ourselves on being as flexible and as creative as we can be and understanding the merchant situation and putting the right offer in front of the merchant, that makes sense for them. If exclusivity doesn't make sense for whatever reason, because maybe they have an incumbent provider, we're not wed to that approach. We love exclusivity where we can get it, but it's not the only way that we engage with merchants.

And then on your question about how much of the credit card spend is addressable. Again, I think time will tell there. I think we're not seeing any sort of slowdown or saturation in our business where we're seeing accelerating growth, quite the opposite of a saturation. And that tells us we're on the right course. And we are seeing a deepening of frequency when you look at our overall transactions per user per year versus what we're seeing on Affirm Card. Affirm Card is running at roughly 20 transactions per user per year versus five and a half times for the user base at large.

So again, that tells us that we have a product that resonates, that allows for consumers to make plans and predictably plan their financial lives on a monthly basis. And we're doing it in ways that align with the

consumer and don't have some of the financial penalties that exist in credit cards. So we think that's a better experience for consumers and we also think we're incredibly early in the market opportunity. So we try to take the long view in terms of how much of that, maybe \$1.2 trillion of revolving spend we can penetrate and we're really optimistic about our chances there.

John Hecht

Great. The session actually, we're at the end of our time. And Rob, I don't want to put you on the spot, but I didn't really get to ask about all your new growth endeavors, which includes the card product that you mentioned, direct to consumer, entering the U.K. and maybe some other European markets, and then the Apple Pay partnership. Maybe just since we have a limited time, I'm wondering how, like maybe just give us the state of the union on those and what kind of KPIs or growth objectives we might be looking at over the next couple years.

Rob O'Hare

Yes, I mean, I think all of those are incredibly important. And the wallet partnerships in conjunction with card, we think that's a really elegant way for us to play in store with buy now, pay later. And no one has really cracked the code in terms of in-store commerce yet. And we think there's an immense opportunity there and we think a form factor that consumers know, like Affirm Card, we think that's a really elegant way to do it, along with the companion app that's a part of card. Same is true with the wallet experience.

And so we're really excited for the wallets to start to move out of just e-commerce and start to show up in-store as well. So I think that's an immense opportunity in the U.S. and there's no reason why that opportunity can't work in the new markets that we're also very excited about. So, yes, we've been on record to say, the U.K., we launched with a small number of merchant partners in November. We're excited to get going with Shopify in the not too distant future.

And we also are looking to expand in continental Europe and also looking to go to Australia in the long term too. So yes, we're really excited about taking the Affirm brand out of just North America.

John Hecht

Alright. Well, we've gone up a little over our limit. I really want to thank you, Rob. And Turpin, thanks for co-hosting this with me and thanks, everybody, for participating. Have a good evening.

Rob O'Hare

Thanks, John. Thank you.

Turpin Senou

Thank you.