LUISS

Student: Line Voksoe

Student ID: 742741

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Luiss Guido Carli University, Rome

Buy Now, Pay Later: How consumers handle risk by choice of payment option in online fashion retailing

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Supervisor: Giacomo Sillari

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Chapter 1 - Introduction

1.1 Introduction to Topic

The customer purchase journey continuously evolves, and it is increasingly moved to online platforms. E-commerce companies continue to adapt their services to consumer demands and there are an increasing number of offerings available to customers opting to purchase online. As such, consumers have many choices to make when it comes to purchasing online. Among others, there is a growing number of payment options available and one that is been increasingly adopted by both consumers and retailers in the latest years is the payment solution known as Buy Now, Pay Later.

Buy Now, Pay Later (hereby referred to as its acronym BNPL) is a payment solution provided by an increasing number of retailers, primarily online. As its name states, BNPL allows the customer to buy a product immediately but delays the payment until later. The sum is paid upfront by the BNPL provider, thus involving little financial risk for the retailer (although having to pay a fee) (Fisher, Holland & West, 2021). Different BNPL service providers offer the customers different purchase options. However, most of them involve that the customer either pay in installments (For instance four installments where each is paid every second week) or delaying the payment into a given future date (Such as 14 days, 10 days, 30 days). The availability of the specific payment type varies based on geographical territory and service provider.

Many companies used deferred payments as an option to please risk-averse and convenience seeking consumers (Deufel & Kemper, 2018), as deferring payments give customers the option of trying the product before actually buying from it (in the sense that money is withdrawn from their account). As such, the BNPL payment option mitigates the pain of paying (experience of feeling negative emotions when purchasing due to loss aversion) while giving consumers the instant gratification of making a purchase right away. As long as the amount due is paid within the specified timeframe, it is interest-free and often free of charges, in several ways being more beneficial than the traditional credit card. As mentioned, BNPL is primarily provided by online retailers, and thus they are the primary customer of such providers. However, in some countries like Australia and the US, these providers are working on developing the feature in physical

stores as well (Fisher, Holland & West, 2021; Marks, 2021). The number of providers offering BNPL is increasing, yet the most prominent players include Klarna, Afterpay, and PayPal Credit (Grand View Research, 2021).

1.2 BNPL Growth

BNPL has experienced substantial growth in recent years, with solid consumers and retailers adoption. From 2020 to 2021, adoption of BNPL increased with 18% in the U.S. (FinTechtris, 2021). Because of its expansion to new markets, for instance, in Asia and the Middle East, the global market volume of BNPL is expected to double in the next four years (FinTechtris, 2021; TSG, 2021). The increased adaption of BNPL can partly be attributed to the general and consistent growth of e-commerce sales worldwide, as BNPL is mostly adapted by online retailers. In recent years, e-commerce sales revenues have made consistent annual growth (McKinsey, 2021). In 2021, retail e-commerce was estimated to be worth 4.9 trillion U.S. dollars, and global e-commerce sales reached $876 billion in the first quarter of 2022, up 38% year-over-year (Verdon, 2021). The growth is expected to continue, with 2025 sales predicted to be 7.39 trillion U.S. dollars (Statista, 2021). The Covid-19 pandemic has made consumers more comfortable with e-commerce, as it became an even more convenient option due to physical stores closing or consumers avoiding visiting them due to fear of getting infected. With the pandemic, online retailing has only continued to grow its momentum, with 71 % of consumers reporting that they have purchased more items online since its beginning (C+R Research, 2021).

1.3 Managerial Relevance

The managerial relevance for such insights is increasing with the growth of e-commerce and the adoption of BNPL. Gaining insight into why consumers select BNPL is firstly relevant for online retailers and BNPL service providers. Online retailers can use BNPL as a risk mitigation strategy for the consumer. BNPL service providers can use it as a strategic advantage to sell to their prospective customers. However, the relevance of such insights goes beyond these. As the adoption of BNPL goes beyond its traditional service providers (e.g., Klarna), it has also altered the fintech market with credit card issuers adopting similar features. A recent example is American Express with its Plan It feature (Doyle, 2021), granting its customers more "flexibility to buy what you need – or want – while still earning

rewards". In line with this development, payment options are of increased importance and the founder of the 4Ps of marketing, Philip Kotler, has even stated that "Payments have become an important element of the selling proposition and should be considered the 5th P of marketing" (Shevlin, 2021).

With the growing number of payment solutions available, it becomes an increasingly important part and touchpoint of the customer purchase journey. Hence, it is crucial to understand why consumers choose different payment options, in which BNPL plays a relatively new major role. With this, marketers can influence consumers' purchase likelihood by offering different payment options like BNPL, and further insight into BNPL is thus essential. With the growing number of payment solutions available, this interest in understanding the consumer decision process when it comes to these should be growing as well, outside the field of marketing. Lastly, risk is a negative influencer of the customer purchase journey, making it less pleasant for consumers, and if BNPL can make this experience perceivably more reliable for the consumer, it is an important insight into this body of literature as well. Previous research has emphasized that it is crucial for businesses to offer flexible payment channels to meet their customers' expectations, as 83% of customers want retailers to implement alternative electronic payment options, such as BNPL (Global Payments Inc, 2021). This is especially true for generation Z, which is one of the most important customers for BNPL and in online retailing in general (Bien, 2021). These expectations are related to the desire for consistently improved user experience innovation and convenience, which is an important competitive advantage in e-commerce (Wood, 2013).

1.4 BNPL Consumer Behavior

The reasoning behind consumers choice of BNPL have been explored in some empirical research already. As mentioned initially, consumers like to delay payments because the pain of paying gives negative emotions. Still, BNPL allows consumers the instant gratification of buying themselves something new. Furthermore, consumers have reported using BNPL because they cannot otherwise afford it. In fact, 59% of respondents in data collected by C+R Research (2021) say they purchased an "unnecessary" item that they otherwise could not afford. Other reasons include being more convenient and flexible, lower interest rates, and an alternative for maxed-out credit cards. The most common items purchased through BNPL are clothing (accounting for 47% of the respondents purchases) and electronics (44%). Further

insights into why consumers choose BNPL are relevant for policymakers as well, as it has been tied to consumer debt and overconsumption of products. BNPL has been criticized for encouraging consumers to take on debt they might not afford, thus being tied to increased consumer debt. In fact, over the past two years, 43% of BNPL users have made late payments (Shevlin, 2021).

Additionally, 55% of consumers say they tend to spend more with this service than with other payment methods, which is backed up by several data sources (Lake, 2021; Wiles, 2021). Still, most consumers prefer BNPL to credit cards, even though 66% also deem BNPL as financially risky to use. Despite some skepticism, with the increased adoption of the service, it is likely to decrease over time. Among those who have used the service, 85% plan to continue doing so in the future (TSG, 2021). BNPL is tied to overconsumption, especially clothing, because consumers tend to order more when seeing this option at checkout (Gifford, 2020). Further, if associating BNPL to decreased risk, consumers can allow themselves to order items they otherwise would not because the perceived loss of them not fitting is more minor. Overall, new insights about BNPL are relevant across various sectors.

There are demographic data collected on the BNPL consumer. The BNPL consumer is more likely to be a Gen Z or Millennial (Gen Y) female (Bien, 2021) early in their career. Gen Z and Gen Y have a larger tendency to employ different payment methods when purchasing online and have a higher credit card use, which BNPL has become the main competitor of (PYMNTS.com). According to Roy Morgan (2019), women are twice as likely to use the service than men. Men, however, are more likely to use other contactless/cardless mobile payments. Still, BNPL is being adapted by a wide range of consumers of all age groups. However, the payment option is more dominant among those 18-29, 30-39, and 40-49 (Fisher, Holland & West, 2021), i.e., those age groups that are more comfortable with technology and, more specifically, fintech. Still, psychological factors as perceived risk has not been explored in research about BNPL. It is widely recognized that consumers deal with uncertainty when purchasing online and should thus influence the choice of payment method. Consumers are often encouraged to use their credit cards for purchasing online products, yet the same cannot be said for BNPL. Arguably, consumers have a different relationship with their respective banks rather than an external service provider (which is the case for many BNPL customers).

Because consumers view online retailing as having some uncertainty, it can be deemed a safer solution to delay payment until the item is received. As previously listed, convenience, ease of use, and consumers not being able to afford to pay right now are explored reasons behind the choice of BNPL. A BNPL report by Bain (2021) found the option to "try before you buy" as an advantage that consumers value with the services, which can be viewed as a risk mitigation method as it delays the loss of potentially buying something you do not want to keep. Still, risk mitigation in itself has not been explored or mentioned as a direct advantage of BNPL, and in some reports, no such method (as try before you buy) is included. Thus, it is interesting to assess how perceived risk and the mitigation of such risk affect the choice of payment options online. It is especially relevant online, as consumers cannot directly try or experience the product beforehand. Research has been devoted to credit cards previously, as this has been a payment option available to consumers for several years. Even though the motivation for credit cards can in some scenarios be the same for BNPL, BNPL offers features that distinguish them from credit cards. Notably, they are interest free (as long as you pay within the given time frame), and they are often offered by third-party providers (not the consumers bank). For this study, it would be relevant to look into such a third-party provider (e.g., Klarna), for the clothing industry as this is the most used category for BNPL and for e-commerce in general (Statista, 2018). Hence, making the study increasingly generalizable.

Chapter 2 – Literature Review

In academic literature, BNPL is a concept yet to be widely explored, although it has increasingly caught the interest of researchers (Garcia Alvarez, 2021). Especially the link between consumer debt among young people and the payment solution has been explored in the literature. Other online payment solutions that have been around longer have been widely explored, yet research is often focused on the benefits of credit card payments (e.g., Chakravorti & To, 2007). As BNPL distinguishes itself from other e-payments and is an increasingly adopted and in-demand payment solution, often being preferred by consumers to credit cards, there is a need for further research on the topic. Firstly, as there is no actual money withdrawn from the customer’s credit card, it delays the perceived monetary loss (Prelec & Loewenstein, 1998; Bornemann & Homburg, 2011). In the case of temporal distance as with BNPL, the loss of money becomes more abstract and can mitigate the pain of paying associated with a purchase (Soman, 2001). This factor can partly explain why

consumers overspend with BNPL, as the actual loss of money is delayed and thus seen as having less consequences. Another factor that plays into this is the installment feature making the purchases more manageable. Secondly, there is often no interest charge with BNPL, as there often is with credit cards. These differences have proven to have important implications for consumer behavior, given the rapid and increasing adoption of the service.

As discussed, BNPL is mostly adopted by online retailers and mostly relevant in an online setting ; thus the online retailing environment will be the focus of the study. As shown in the following review, consumer perceptions and behavior differ in an online setting, and thus it there is the need for a review on this specific setting (e.g, Wolny & Charoensuksai, 2014; Dokulil et. al, 2020). The same can be said for high and low involvement purchases, as the amount of time, effort, and resources the purchase requires shape consumer behavior in many ways (Mittal, 1995; Bloch and Richings, 1983; Jain, 2019). The review will specifically focus on risk perception and risk mitigation in an online setting and distinguish between high and low involvement purchases. Further, the concept of temporal distance and its effect on risk will be discussed, as well as hyperbolic discounting and how consumers use this as a way of valuing losses now as graver than losses later. Trust is shown to decrease perceived risk and is thus also discussed. Because many online retailers do not have a physical presence and rely solely on e-commerce, and are not well-known brands, risk management is imperative in e-commerce and especially for the online marketer (Grabner-Krauter & Kaluscha, 2003). Lastly, other potential psychological factors behind the choice of BNPL are discussed, such as hedonic framing.

2.1 Perceived risk in online retailing

In online retailing, consumers face even more uncertainty than in traditional purchases. There is uncertainty in online transactions because the quality of the product cannot be ascertained by the consumers before receiving the product (Wolny & Charoensuksai, 2014). When purchasing in-store, consumers can feel the product and bring it home immediately, and this mitigates some of the uncertainty regarding the purchase (Van den Poel & Leunis, 1999; Grabner-Krauter, 2002). Such information asymmetry can lead to uncertainty and increased risk perception on the consumers' side (Akerlof, 1995; Dokulil et. al, 2020). The more the actual purchase experience differs from the purchase goals the higher the perceived risk (Dowling, 1986). As consumers often purchase online for ease of use and convenience, as

well as enjoyment (Chiu et. al, 2012), the more the experience differs from these – the higher the perceived risk of the transaction. Various literature has deconstructed perceived risk and assessed its impact on consumer behavior, both offline and online.

Cunningham (1967) defined it as the probability of a loss and the subjective feeling of unfavorable consequences. Forsythe & Shi (2003) defines perceived risk in specifically online retailing as "the subjectively determined expectation of loss by an internet shopper in contemplating a particular online purchase". Several studies have shown that perceived risk is considered the most impactful negative psychological influencer of online retailing behavior (e.g., Ariffin, Mohan & Goh, 2018; Mortimer, Hasan, Andrews & Martin, 2016; Wu & Ke, 2015). A study by Van den Poel and Leunis (1999) used purchase intention as the dependent variable and found overall perceived risk to especially affect this variable. Still, in regard to perceived risk in online retailing, research has mostly focused on the idea of risk perception towards privacy and getting consumers' personal information stolen or misused (e.g., Miyazaki & Fernandez, 2001). Hence, on how it is risky to use online payment methods and not on how these methods can be used to mitigate risk. As such, it is important that the payment provider is trusted with the personal information of its customers.

Jacoby and Kaplan (1972) found five relevant components of perceived risk for consumers: financial risk, physical risk, performance risk, psychological risk, and social risk. In sum, these become the overall perceived risk. In reviewing these, it is arguably financial risk (risk of losing money) and performance risk (risk that there is something wrong with the product) which is the most relevant for clothing in online retailing. Bitner and Zeithaml (2003) assume that financial risk often occur right after the customer makes an online order. As such, with the option of paying later, this risk is mitigated or delayed until a later time because there is no actual loss from the consumers' side until they can properly assess the product (Consequently mitigating the perceived performance risk). Performance risk is related to the product not being as expected (e.g., size too small or product being faulty).

Concerns related to self-image and how others think of you are also related to clothing (psychological and social risk), but these are more present in the post-purchase stage where the consumer uses the product. Physical risk is related to the product having a negative health impact and is not as relevant for the clothing industry. With the introduction of e-commerce, researchers have extended the different categories of perceived risk into an online setting.

These include non-delivery risk, convenience risk and return policy risk (Wai, Dastane, Johari & Ismail, 2019). Especially the possibility of delivery failure and financial risk were strong determinants of perceived risk and thus negative influencers of purchase intention (Wai, Dastane, Johari & Ismail, 2019; Ahmed, Ali & Top, 2021). Risk perception also greatly depends on past experience (Siegrist, 2019), and consumers that have less experience with e-commerce will also experience it as riskier (Mainardes et. al, 2019).

2.2 Differing risk in high and low involvement purchases

Purchases differ in terms of complexity and how much thought the consumer put into it and are classified as either low or high involvement purchases (Mittal, 1995). Among other factors determining degree of perceived risk, it can vary from product category to product category. Partly due to risk perception varying for low or high involvement purchases because the amount of effort and resources put into them vary. BNPL is mostly used to purchase clothing, which is commonly considered a high-involvement product (Solomon, 1986; Jensen & Hansen, 2006). The second most purchased category is electronics, which is also considered as such due to the higher price and longer life span. According to Kahneman (2011), such higher involvement leads to a more thoughtful decision process, known as system 2. Hence, consumers consider the risks and possible negative outcomes of the purchase more. Another characteristic of high involvement purchases is that they are riskier (Bloch and Richings, 1983; Jain, 2019), also expressed through the perception of consumers (Pires, Stanton & Eckford, 2004). For the choice of payment method, this is done in the purchase part of the customer journey and consumers will weigh the advantages and disadvantages of each payment option more if the product(s) are considered high involvement.

Although clothing is not as a high involvement product category as for instance automobiles, travel, and housing, they still require consideration (e.g., considering which size to buy and reading reviews attempting to assess quality of product) and often involve financial risk. Especially for BNPL purchases, they are found to include clothing items that customers otherwise could not afford. The higher involvement required for the purchase, the greater the effect of perceived risk on purchase medium should be (Heijden, Verhagen & Creemers, 2003; Jacoby & Kaplan, 1972). Hence, perceived risk has a direct influence on the choice of channel and a way to mitigate risk among consumers. However, other factors also determine choice of channel, such as price, availability, and convenience (Verhoef et al., 2007). Hence,

consumers choose based on not only risk, and has to mitigate it otherwise if the other factors are stronger determinants of consumer choice.

2.3 Risk mitigation and uncertainty reduction

As discussed, consumers experience higher risk related to online purchases, and especially for high involvement purchases. Companies have sought to reduce perceived risk by adopting 'risk relievers' (Ross 1971), and it is relevant to look into how consumers mitigate such risk themselves in an online environment. Risk perception determines the act of risk aversion in consumers, meaning that they employ risk mitigation methods in situations perceived as risky. Theories on uncertainty reduction state that the experience of uncertainty is an important motivation to seek information as a means to reduce this perceived uncertainty (Berger & Calabrese, 1975; Kramer, 1999). In the previous section, it has been argued that part of the potential risk in online retailing involves a potential loss. The prospect theory state that consumers make decisions on potential gains and losses, and not on the eventual outcome (Kahneman & Tversky, 1979), meaning that they in a lot of situations act either irrationally risk-averse or irrationally risk-taking. Further, losses loom larger than gains in decision making, and it is thus more important to the customer to avoid these. As such, given the rather small chance of delivery failure or not getting refunded if something goes wrong with the delivery, consumers can act irrationally risk-averse by not paying for products upfront. Hence, the prospect theory is relevant for BNPL as well and can arguably make consumers choose it over other payment solutions as a loss aversion method. In line with prospect theory, the higher risk perceived by the consumer, the more likely they are to employ such risk mitigation methods. Hence, if the retailer is perceived as less trustworthy, consumers should have a higher propensity to choose BNPL. Furthermore, perceived beliefs about the outcome of our behavior are predictors of behavioral intentions (Ajzen, 1991), and in the case of a potential loss, we will alter our behavior to mitigate this risk. Hence, if consumers perceive risk at the point of choosing payment solutions, they will choose one that reduces the uncertainty with the transaction.

Furthermore, it is researched how consumers reduce uncertainty about online transactions through information search. Webrooming is also a risk mitigation method consumers use, where they examine the products physically before purchasing it online (Flavian et al., 2020). It is found that the higher involvement the purchase is, the higher the need and intention to engage in such methods. However, not all products are found in-store, and it can still be

difficult to assess the reliability of the retailer if they are not a well-known brand (Grabner-Krauter & Kaluscha, 2003). With the decline of physical retailers and growth of e-commerce, such webrooming may be increasingly difficult, as many products cannot be ascertained physically. Thus, consumers need to take other measures to reduce uncertainty related to their purchase. Such methods in an exclusively online environment include learning about product features, reading reviews, alternatives, price, quality, delivery, return policy, and retailer trustworthiness (through sites such as *Trustpilot*). A favorable return policy lessens the perceived risk of online purchasing, and thus encourage consumers to purchase (Wood, 2001). Furthermore, studies have been performed on website structure and design and find that consumers trust websites that score higher on these (Karahanna et. al, 2013).

In review of the relevant literature on risk mitigation in online retailing, it is clear that an aspect that has not been widely explored is the choice of payment solutions in online retailing as a means of reducing uncertainty. Arguably, the presence of being able to pay later removes some of the potential loss perceived by the customer. Further, customers should choose the payment method that reduces the uncertainty of the transaction. Hence, BNPL can work as a loss aversion/risk mitigation method in the case of uncertainty. In a recent study on the choice of payment method, Jang, Miao & Chen (2021) found that pay now options are avoided by consumers if they feel higher risks related to the purchase. Hence, they use it as a type of risk mitigation method. Temporal construal theory state that distant future situations are construed on a higher level than near-future situations (Liberman & Trope, 1998). Research shows that it has important implications in decision making, as it affects how people perceive a certain event (Trope & Liberman, 2010). Hence, the implications are more abstract and thus the monetary loss may feel less concrete for the customer in the case of delaying payments. For research on credit cards, in which BNPL has many similarities, it is shown that people are willing to pay more because of this temporal distance between payment and consumption (Cheng & Chen, 2016). Temporal distance has implications for BNPL because the time between the purchase and the actual transfer of money is longer.

Research related to decision making found that people often take less risk related to near-future events (lower temporal distance) and in general feel less confident about them (Gilovich, Kerr, & Medvec, 1993; Nisan, 1972). The study by Jang, Miao & Chen (2021) is one of the few assessing the choice of payment method as such a way to increase temporal distance of the payment event. The research was set in the travel industry, which is both

higher involvement and often higher temporal distance to the purchase moment. Hence, it is interesting to look into how this proposed effect works in lower involvement products such as clothing, and where the realization of the purchase is more present in time (higher degree of instant gratification). As such, in the case of purchasing clothing online, as the delivery time frame is often shorter than for a travel. Jang, Miao & Chen (2021) argue that their research is the first to study how consumers perceived risks from different payment options are influenced by temporal distance (as is the case with BNPL). Furthermore, the majority of studies have been focused on how temporal distance influence consumer attitude and behavioral intent (e.g., Kim et. al, 2016). As such, little research has been performed on how temporal distance affect perceived risk of consumers.

Another construct related to how consumers view time in transactions is hyperbolic discounting. Hyperbolic discounting means valuing benefits that are more present in time, rather than in the future (Soman, 2011, pp. 69; Kahneman, 2011, pp. 64). Consequently, costs that are paid in the future are not felt as deeply as costs that are paid now. For BNPL, this could imply that consumers use hyperbolic discounting by avoiding potential costs of problems with their online purchase (delivery failures or faulty items) and putting it off in the future (late-payment fees). As such, consumers would rather suffer a potential financial loss of not being able to pay of their "debt" in time (and thus paying interest fees), rather than paying for an item they end up not wanting, that does not arrive or is otherwise faulty. Hence, the value of risk mitigation is perceived as higher than the value of avoiding interest fees or other financial risk connected to BNPL. Hyperbolic discounting has been widely applied in terms of risk, and especially in terms of environmentalism and obesity. Yet, it is not widely applied in a setting such as online retailing or in terms of payment solution adoption. Still, as argued, it can be applied to explain in part why consumers choose BNPL as they value the benefits of buying now and paying later with little risk rather than higher risk (as is felt by the consumer in online retailing) now but less risk later (by for instance avoiding interest fees or not being able to pay a potential growing consumer debt).

Trust in the online retailer can overcome the barrier of risk (Harridge-March, 2006), and ensuring that trust is stronger than risk is imperative for e-commerce companies (Grabner-Krauter & Kaluscha, 2003). Conversely, lack of trust leads to transaction aversion, especially in online economic exchanges (Hoffman, Novak & Peralta, 1999; Cases, 2002; Ha & Stoel, 2009). Hence, in case of the consumer not trusting the online retailer, they adhere from

purchasing from them. According to Lee, Park, and Han (2011), if the unknown retailer is related to trusted sources, trust is transferred from the trusted source to the unknown retailer. Hence, if a trusted BNPL provider is present at the checkout process at an unknown retailer, consumers may trust the retailer as well. Hence, to ensure generalizability, the trust of the BNPL provider should also be assessed and kept constant in the following study. In an actual online purchase process, the BNPL provider would be present at checkout.

A study by Karhanna et. al (2013) used well-known brands in their study and argued that the role of trust may have been reduced as dealing with brands with good reputations can lead to lower uncertainty. Erdem & Swait (2004) defines brand credibility as the perceived believability of whether a brand has the ability and willingness to continuously deliver what is promised. In a fashion e-commerce scenario, this includes the products being true to size, being delivered within the promised time frame and the return policies working as stated on the website. In other words, the consumers trust the retailer to the extent that they believe the customer experience will be as expected. Trust is found to be a critical success factor in e-commerce (Eastlick, Lotz & Warrington, 2006; Beldad, Jong & Steehouder, 2010). Aaker (1991) argues that credible brands hold lower risks together with higher perceived quality and lower information costs. Similarly, studies have found that brand credibility decreases perceived risk (Erdem & Swait, 1998; Baek & Kim, 2010). Simultaneously, the authors argue that perceived risk is positively associated with information costs. Hence, how much a customer needs to search for information about the brand and its products. The more uncertainty, the more risk, and the more need for information search (through for instance *Trustpilot*, which gives a score based on how trustworthy others find the online retailer).

2.4 Factors affecting choice of e-payment

Although studies have been made in an online retailing setting, how payment method choices are made online remain quite unexplored in the literature (Deufel & Kemper, 2018). Because it is easier to abandon a website than walking away from the cashier at a physical retailer, customers are more sensitive online with respect to payments. Also, it is easier to search for alternatives. The "online purchase decision-making is a dynamic and highly flexible process" (Karimi, Papamichail, & Holland 2015). As such, the consumer decision process is intricate and needs thorough examination, especially regarding what factors cause certain behavior and how to influence these. According to Grüschow, Kemper, & Brettel (2016), consumers search

for payment methods that are convenient and will be of the lowest cost to them personally. Although BNPL may induce more costs over time if the payment is not done in time, the perceived cost at the time of the transaction is less because there is no money drawn from the customer's account at the time of transaction.

Age has been an identified factor in choice of e-payment, as younger consumers tend to trust e-commerce more and demand more flexible payment solutions (Joines, Scherer & Scheufele, 2003). Security and trust in the payment systems are also important factors for adoption, also among younger consumers (Barkhordari, et. al, 2016). The main customers of BNPL, Generation Y and Generation Z, are known to use a variety of payment methods when purchasing online and to perceive it as less risky than older generations. As BNPL is more widespread in certain areas, its perceived risk and also the adoption of it should depend on the geographical area – especially as younger consumers are heavily influenced by word-of-mouth. Deufel & Kemper (2018) found that habitual behavior is a strong determinator in choice of deferred payment. Whether or not the BNPL offer comes from a third-party provider or directly from the retailer also has an effect, as 59% of all US consumers surveyed by PYMNTS (2021) said they would use it from third-party providers, but only 20% would use a direct retailer-offered solution.

In the choice of payment method, consumers are influenced by the framing of the method (Plous, 1993; Ganzach & Karsahi, 1995). For instance, *try before you buy*, clearly has a positive framing which signify to the customers that they are able to physically examine the product before committing to the purchase. Similarly, *buy now, pay later* signify to the customer that they are able to experience the instant gratification of buying and delaying the loss and the pain of paying until later. Hence, positive framing makes the payment option more salient to the customer. Furthermore, hedonic framing suggests that one loss split up into smaller losses are more salient to people. Hence, maximizing the perceived gains and minimizing perceived loss. By paying in installments, BNPL can be desirable to people because the monetary loss is perceived as less. As mentioned, losses loom larger than gains, and such framing is effective in minimizing perceived loss for the consumer. In presence of risk and uncertainty, the customer will seek to reduce loss and BNPL is thus a way to reduce the monetary loss of purchasing online.

Additionally, whether or not the payment method is the default option may be an influencing factor. People stick to defaults for many reasons, partly because it is viewed as a norm and because it allows us not to make a decision, which is something customers want to avoid (Soman, 2011, pp. 69). This should especially be true for the online purchase journey, as it is characterized by convenience and ease of use for the consumer. Customers usually stick to default unless it is seen as particularly disadvantageous. As such, if the consumers perceive the purchase as riskier, they should be opposed to choosing payment options that are viewed as risky. Still, whether or not a given payment method is the default option should have an effect on the customers propensity to choose it. Hence, if the online retailer has BNPL as a default option, or vice versa, this can potentially mediate the effect of perceived risk as the customer adheres from actively choosing. In the framing of BNPL, customers sometimes are presented with the option to pay at a certain date, and other times in a specified time frame. For instance, customers can pay at "31st of August" or "4 installments every two weeks". The date/delay effect refers to the difference in these descriptions, consistently finding that consumers discount outcome less steeply when the future time is describes as a date compared to the number of days, weeks, or months (LeBoeuf, 2006; Read et. al, 2005). Hence, what type of installment BNPL use and how it is framed also impacts how salient it is to the customer.

In summary, there is sparse research on BNPL and especially the way this payment method affects purchase behavior in various settings. Reviewing the psychological construct around the choice of payment method, gaps has been identified in how consumers use this as a risk mitigation and uncertainty reduction method, although several literatures suggest that it can work as such (e.g., Gilovich, Kerr & Medvec, 1993; Nisan, 1972; Jang, Miao & Chen, 2021). Payment method is an important part of the purchase stage of the online customer journey and has recently been called the *5th P in marketing*. Especially for high involvement purchases, this choice is all the more important as previous literature have shown these to be perceived as riskier by the consumer. It is established in the literature that risk perception affects consumers online purchasing behavior. With respect to research on temporal distance, little is dedicated to how temporal distance affects risk perception and risk mitigation methods in online purchases. Higher temporal distance of the transaction outlay with the "pay later" option has been shown to be preferred by consumers if they perceive higher risk related to purchasing in the travel industry. Still, studies up to year 2021 reveal a gap in knowledge on how temporal distance affects perceived risk, which is a topic involved with BNPL.

To conclude the literature review, knowledge areas yet to be fully explored include a more in-depth analysis on how risk perception affects the choice of payment method, and how consumers try to mitigate loss perception through the purchase stage of the consumer journey, increasingly important with the wider array of choices consumers have. One of the concepts worth to be investigated is how the delay in payment may induce or make more prone the consumer to take more risk, as there is a lower potential loss perception. The research gap that the study aims to fill is the lack of full understanding of how the choice of payment methods may be affected. More specifically, how consumers delay payment as a means of risk mitigation in cases of higher perceived risk purchases. As BNPL is becoming increasingly adopted and is still sparsely researched in a consumer behavior setting, this study will focus on it as the center of the analysis. As BNPL differs from other e-payment methods, results from previous studies on online payment options are not necessarily generalizable to it. Moreover, because the most purchased product category with BNPL option is clothing, and consumer behavior differ based on the product category, clothing will be the product category investigated.

All this considered, this study aims to address the following research question: *How does risk perception affects payment choices, more specifically BNPL, associated with online purchases of clothing items?*

Chapter 3 – Conceptual Framework

3.1 Risk perception

According to the Forsythe & Shi (2003) definition, perceived risk in online retailing is "the subjectively determined expectation of loss by an internet shopper in contemplating a particular online purchase". Hence, there is a direct link between the risk perception and the expected loss of the consumer. For the transaction setting, consumers experience increased perceived risk in online settings compared to physical ones. There is uncertainty in online transactions because the quality of the product cannot be ascertained by the consumers before receiving the product, thus increasing the perceived risk (Wolny & Charoensuksai, 2014). Furthermore, the level of involvement affects perceived risk. This variation in risk is derived from the variation in the amount of effort and resources put into the purchase. The more effort

in terms of time and money put into the product, the bigger the loss if it did not live up to the customers' expectations, and vice versa.

For the expected loss, the customer worry that the products they purchase online may not provide the expected benefits or that they will have unexpected faults (Glover & Benbasat, 2010). In the clothing category, this include the product not being as displayed, arriving faulty, or not having the expected or correct fit, among others. Performance risk involves the perception that the product purchased may malfunction and may not perform or function as it was designed or originally expected, which may result in failing to meet the desired benefits of the consumer (Jacoby and Kaplan, 1972. Almousa (2011) found this to be a significant perceived risk by consumers in the only clothing product category. Alongside performance risk, financial risk, the fear of monetary loss or credit card fraud was a significant risk perceived by consumers, and strong determinator of purchase intention where an increase in financial risk leads to decrease in purchase intent.

Perceived risk differs based on experience with online retailing and personality type. Most BNPL customers are Millennials or Gen Z, which are customer segments typically comfortable with technology and purchasing online. Older generations less comfortable and experienced with online retailing will be more skeptical of it. For personality types, consumers will differ in risk aversion. In addition, women are known in the literature to be more risk averse than men (Byrnes, Miller, & Schafer, 1999). Consumers with higher risk aversion perceive higher significance of losses (Pizam et al., 2004). As such, risk averse consumers are more skeptical of online retailing and take larger precautions (Hanoch, 1977; Masiero et al., 2020). Risk averse consumers will to a greater extent use brand affect and brand trust as a risk reliever (Matzler et. al, 2008). Other methods include following tbe crowd, choosing the option adopted by ones peers, which has also been shown in online retailing (Rejikumar et. al, 2021). Furthermore, consumers rely on return policies and previous purchasing experience to reduce their perceived risk in online retailing (Kim, 2010; Roselius, 1971).

3.2 Payment method

A payment method is a way that customers pay for a product or service (Heegard, 2021). BNPL is a payment method, mostly used in an online setting. Online, consumers are offered a variety of payment methods. According to Grüschow, Kemper, & Brettel (2016), consumers

search for payment methods that are convenient and will be of the lowest cost to them personally. Schuh & Stavins (2011), name several factors determining consumers choice of payment method. Firstly, there is cost associated with the transactions, such as service and interest fees. As discussed, this factor is one of the reasons many consumers now prefer BNPL over namely credit cards. Secondly, there is convenience which refers to whether consumers can save time. Thirdly, security which is defined as security against permanent financial loss or unwanted disclosure of personal information when a payment method has been stolen, misused or accessed without the owner's permission. Fourth, a payment method is often chosen out of preference and habits. That is, the consumers often choose the payment method they usually choose (Cruijsen, Hernandez & Jonker, 2016). Swiecka, Terefenko & Paprotny (2021) named several factors influencing customers choice of payment method. Regarding characteristics, cost of use, convenience/ease and safety are named. For transaction specific settings, the place of purchase, amount of the transaction and type of goods/services purchased. Other criteria involve demographics, personal economy, and others (including habits and possibility to make payments at all times.) Different payment methods have been shown to affect the buying behavior of customers (Ferrao & Ansari, 2015).

Higher transparency of the payment (where cash is the least transparent and credit cards are known to be more transparent), makes the actual exchange of money more abstract for the consumer (Soman, 2003). A payment method that simplifies the payment process will make it more difficult for the customer to see to what degree they are actually spending money (Ariely & Kreisler, 2018). BNPL is known for simplifying the payment process, at least at the point-of-purchase, as it often involves little effort from the customer at that time other than choosing the option. Furthermore, it shown that customers feel less "pain" when there is a time gap between the time they consume the product and when they actually pay for it (Ariely & Kreisler, 2018). Hence, the actual monetary loss is felt less deeply. Because of this, deferring payments can be used as a mitigation method where consumers fear a monetary loss, i.e., they experience higher perceived risk of the purchase. Based on this, the following hypothesis is formed:

Hypothesis 1: Consumers that perceive higher risk related to the online purchase, will have a higher propensity to choose BNPL. On the contrary, consumers that perceive a lower risk will have a lower propensity to choose BNPL. Thus, a positive relationship between risk perception and BNPL choice as payment methods, is likely to occur.

3.3 Trust

Brand trust is defined as the willingness of a consumer to rely on the ability of a brand to perform as entitled (Chaudhuri & Holbrook, 2001). The brand works in the best interest of the customer and enhances the reliability of the transaction. For e-commerce, this include the product being delivered as it is expected by the customer, and the potential losses described in the previous section are mitigated. In the clothing category, brand trust is particularly important because a customer is often unable to evaluate the quality and fit of the garment prior to the purchase (Jones & Kim, 2010). Antecedents for brand trust found in the literature include several brand characteristics such as perceived merchandise quality (Alan & Kabadayı, 2014), brand reputation and brand predictability (Lau & Lee, 1999). Furthermore, past experience where the customers' expectations have been met also positively affect brand trust (Lau & Lee, 1999). As clothing is assessed to be a high involvement product category, brand trust is more significant (compared to low involvement) as studies have shown this to be more important in the higher involvement product categories. Also, brand commitment increases for high involvement product categories (Amine, 1998).

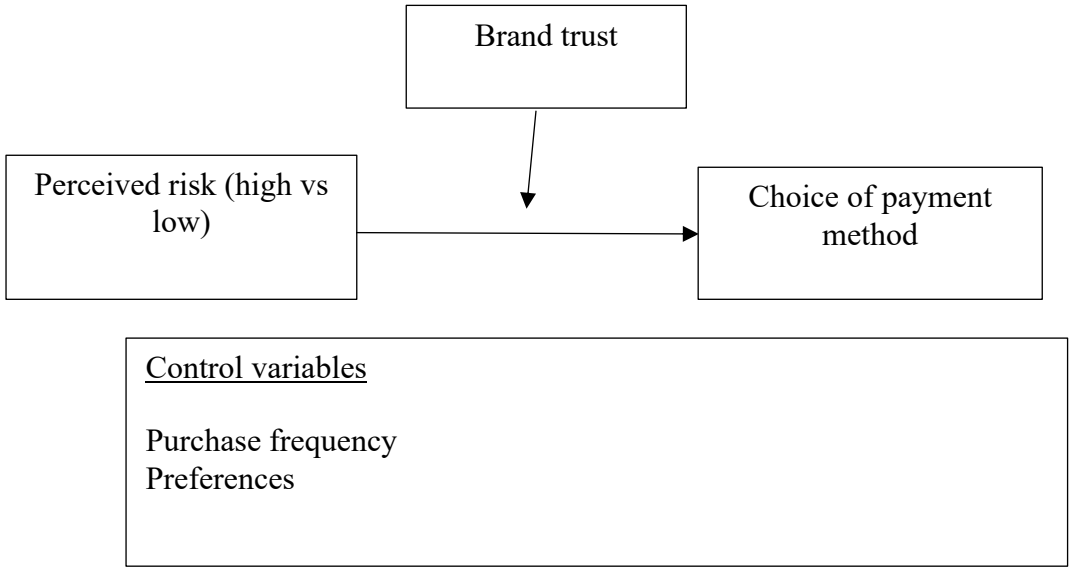
Studies have found risk taking and uncertainty to be negative influencers of for trust (Detusch, 1958; Coleman, 1990). In cases of higher trust of the online retailer, consumers are more willing to take risk when purchasing from these, than with online retailers they do not trust. Customers feel to a greater extent that the online retailer will deliver what is promised. Brand trust plays an essential role in helping customers resolve risk perceptions and uncertainty in e-commerce (Lai & Tong, 2013). Jones and Kim (2010) also found that trust increases purchase intention.

All this considered, it is hypothesized that choice of BNPL will be negatively associated with higher brand trust (in this case, in the online retailer). Customers that trust the online retailer to a higher degree will have a lesser need to defer their payment as it is perceived as less risky.

Hypothesis 2: Higher perceived risk in an online retail setting decreases the trust consumers have in the brand thus, leading to BNPL as the payment option for transactions.

With the relation and link between the above variables, the conceptual framework is expected to work as described below. The independent variables are the degree of uncertainty which affects perceived risk, and the payment method is the dependent variable. In this case, BNPL is the focus payment method, so the dependent variable becomes choice of BNPL. Trust in the brand works as a mediator for perceived risk (the greater the trust, the less perceived risk, and vice versa). The mediator, brand trust, is supposed to transmit the causal effect of X to Y (Agler & De Boeck, 2017). There are two variables to control for:

- **Purchase frequency**: Higher purchase experience might lead to higher propensity to use deferred payment, as frequent shoppers are known to be more attracted to this payment method (Constantinovici, 2021).
- **Preferences:** Arguably, the preferred payment method can be chosen regardless of the risk perception of the customer, and it is therefore important to control for. For instance, a customer may choose BNPL out of preference and not the risk associated with the purchase.



Chapter 4 – Methodology

4.1 Research design

The aim of the research is to gain a deeper understanding and generalizable results regarding the hypothesized interaction between the variables in the conceptual framework. Namely, the interaction between the independent variable risk perception and the dependent variable of payment method, and the mediating effect of brand trust. In addition, it is relevant to control for online purchasing experience as well as preference in payment method. Hence, a quantitative survey is appropriate (Malhotra, 2019). See appendix 1 for the final survey that was distributed.

There are certain limitations using an online survey to be aware of. Firstly, it can be difficult to mimic a natural setting, such as purchasing products online. However, the main purpose of the study is to first and foremost test if the variable of risk perception has the predicted effect on payment method, and if brand trust has a mediating effect. As such, if the proposed effects are present in the sample, further research should be conducted to test if the same effects happen in a more realistic setting. Secondly, with surveys there is the possibility of *nonresponse bias*, where the more eager participants are those taking and completing the survey, skewing the results (Baxter, Courage & Caine, 2015).

4.2 Data collection

Both the pretest and the main survey questionnaire is developed using online survey tool *Qualtrics*. Respondents to the survey were collected through a mixture of convenience and snowball sampling, as the survey was distributed through social media, and many were encouraged to distribute it further to their networks (Malhotra, 2019). As the target of BNPL is Gen Z and Millennials, distributing to these groups can lead to valuable insights into the use of this payment method and online retailing behavior in general. Other than this, the survey does not target any specific demographic group. Nevertheless, demographic questions (age, gender, educational background, and employment) were added to the survey as these questions provide context for the collected survey data, allowing to describe the participants and better analyze their data (Allen, 2017). Through social media, the survey was distributed to a variety of nationalities, yet the survey did not control for geographic region as most will likely be from the Western World and little literature has shown difference between these groups in terms of online retailing behavior.

This sampling method has several advantages, namely that it is cheap, convenient, and efficient. Still, there are limitations as with any sampling technique. Firstly, there is the possibility of *over-representation* of these groups. To be representative of the entire population of purchasing products online, it is essential to have a variety of age groups represented in the sample, older age brackets included. As such, the study aims to get a representative sample where several age groups are presented, to generalize it to the general population thus producing higher external validity. Therefore, the survey is also distributed among those in the higher age brackets. Secondly, there is the possibility of self-selection bias. However, as it is the least expensive and time-consuming of all sampling techniques, the study proceeds with this option. The sample size ended up consisting of **202** respondents, after data cleaning. These respondents were evenly distributed in both conditions, ensuring that they had over 100 respondents each.

4.3 Pretest

In the survey development process, a pretest was conducted on a smaller sample of respondents (n = 47). The pretest simply tested if two different scenarios created different risk perceptions, as the scenario described had not been empirically tested although based on literature on how previous positive experience with a brand lead to decreased risk perception. The participants were presented with one scenario out of two, using the randomization feature in *Qualtrics*, where one scenario (*positive experience*) explained that the respondent had a positive experience with an online retailer with no setbacks. The other scenario (*no experience*) explained that neither the respondent nor any of their friends/family had any experience with the brand. Everything else in the description was kept constant to isolate the two conditions tested.

Afterwards, the respondents had to answer how likely they deemed different risks related to their purchase experience. These risks were derived from Jacoby and Kaplan (1972) and Wai, Dastane, Johari & Ismail, (2019). The risks they were asked to evaluate included non-delivery risk, financial risk, privacy risk, performance risk (in a clothing specific scenario) and product risk. This pretest help ensure that the scenarios presented in the test actually differed in terms of induced risk perception. An analysis in SPSS showed a significant difference in risk perception between the *positive experience* and the *no experience* groups. The two

descriptions of the different conditions were thus kept for the main survey, as well as the questions assessing the respondents risk perception.

No experience condition:

You decide you need a few new items in your summer wardrobe, and are therefore searching for clothing brands online. You find a new brand you have not heard of nor used before. What intrigues you about this brand is that they have a promotion out with 20% discount for new customers. To your knowledge, none of your friends/family have bought from this brand before either, and you are then unable to evaluate the quality of it based on their experiences. The website is a single-brand retailer, so all the clothing items you buy are from the same manufacturer.

Positive experience condition:

You decide you need a few new items in your summer wardrobe and are therefore searching for clothing brands online. You find a brand you have recently used, which has a campaign out with a 20% discount for returning customers. From your past experience, the brand has delivered the products to you quickly, efficiently, and as expected. The products have always been of high quality, and you have previously not needed to use their return policy. The website is a single-brand retailer, so all the clothing items you buy are from the same manufacturer.

4.4 Survey procedure

The surveys objective was to see the interaction between the variable risk perception and payment method and see how brand trust mediated the risk perception and thus also choice of payment method. Afterwards, to control for personality types and preferences as personality type can affect risk perception and preferences can affect choice of payment method. For instance, if a person has a preference for BNPL, this might be the reason they choose it and not their risk perception associated with the purchase.

Once the respondents opened the survey link they were briefed on their anonymity and the confidentiality of the responses. As in the pretest, the respondents are presented with two scenarios, one with the *positive experience* and one with *no experience.* For choice of payment method and the preferred method, the alternatives were put in randomized order to minimize order effects. To analyze the results, statistical software IBM SPSS is used.

4.5 Survey measures

Risk perception

The respondents from both conditions were presented with the same questions about their perceived risks with the purchase, which were the same used in the pretest. To recap, to measure risk perception the scale was based on the more traditional study from Jacoby and Kaplan (1972) and the one more adopted to online retailing by Wai, Dastane, Johari & Ismail, (2019). From these two studies, risks derived included financial risk, performance risk, non-delivery, and convenience risk. Firstly, to measure the performance risk three items were used: *Risk that the product does not fit as expected, Risk that the product arrives faulty (e.g., torn garment)* and finally *Risk that the product does not live up to the expected quality.* To measure financial risk two items were used: *Risk of losing money on the purchase, or otherwise not getting your money's worth* and *Risk of misuse of your credit card of personal information.* Non-delivery risk was measured using one item: *Risk that the products purchased do not arrive at all.* Finally, convenience risk also using one item: *Risk that I might have to return the product.* A five-point Likert scale was employed from *Extremely unlikely to Extremely likely,* asking the respondents to evaluate how likely they deemed these events, using different statements.

Risk taking propensity

Furthermore, risk propensity is measured using the risk propensity scale by Meertens & Lion (2008). The scale contains 5 items, containing statements indicating that the respondent is a risk avoider and a risk taker. To better fit the purpose of the study, which is to analyze an online retailing setting, certain questions were excluded, more specifically those related to one's health. The alternatives were given on a five-point Likert scale from strongly agree to strongly disagree.

Brand Trust

To control for brand trust as a mediator, the brand trust scale developed by Ballester (2017). However, it needed to be adopted to an unnamed retailer where the respondent needs to assess the brand solely based on the scenario. No brand was named to exclude the possibility of this affecting the respondents attitudes. Instead of *Brand (X)* which is included in the original scale, the respondents are asked to base it upon the brand they were described in the description they were given in the beginning. Nothing else in the question was altered. The scale was employed using a five-point Likert Scale from *Not confident* to *Confident*, the respondents were asked to evaluate how confident they felt that in the case of some of the risks associated with the purchase was realized, the brand would 1) address the respondents concerns sincerely and honestly, 2) work to solve the problem, and 3) compensate them properly.

Purchase frequency

Experience with online retailing is also measured as a control variable, by how many times a year the respondent purchases products online. Higher purchase experience might lead to higher propensity to use deferred payment, as frequent shoppers are known to be more attracted to this payment method (Constantinovici, 2021).

Preferences

To control for preferences, that is, the possibility that the participants choose a payment method because of their preferences and not solely risk perception, they were asked about their typically preferred payment option. Here, the participants could choose between the same options but also write their own under "Other", to ensure that all payment methods would be covered.

Payment option

Which payment option the respondent chooses based on their condition, is measured asking them which they would prefer given the scenario described to them. The respondents could choose from debit card, credit card and BNPL as these are common options at an online checkout, with debit and credit card being the most common ones.

Payment method criteria

It is insightful to know not only which payment options customers choose, but why. This will allow for a better understanding of why some customers choose certain options, other than that there may be an interaction between risk and payment option. The scale used for this purpose is based upon literature by Schuh & Stavins (2011), Cruijsen, Hernandez & Jonker (2016) and Swiecka, Terefenko & Paprotny (2021), who all had a several payment method advantages/criteria that customers deem important when choosing payment options. On a 5-point Likert scale from strongly disagree to strongly agree, the respondents chose which extent they agreed with statements about what their chosen payment method (given the condition they were placed in) gave them. Namely, flexibility, ease, convenience, value, and security.

4.6 Data cleaning

Most of the data cleaning was done in Qualtrics, although the force response function was on, not allowing the respondent to continue with the survey if they do not answer all questions, some non-response responses were recorded where the respondents had only answered a few or no responses. These were naturally deleted from the dataset. After deleting a few non-response responses in Qualtrics (i.e., responses that were recorded which had uncomplete responses) collected through Qualtrics was exported to SPSS for further analysis. In SPSS, Dummy variables were used for the two different conditions, making it possible to compare the two in the software.

4.7 Descriptive statistics

To get an overview of the demographics and online purchasing behavior of the respondents, a descriptive analysis is performed. For the randomization, there was an equal distribution between the two conditions with n = 101 in both conditions, in total 202 participants. The distribution of gender included 70 males (34,5%), 128 females (63,0%) and 5 non-binary/third gender (2,5%). The ages in the survey spanned from 18 to 65+, it was not possible to choose an age bracket below 18 as this is often the age restriction to purchase products online. Almost half and the majority of the respondents were in the 25-34 age bracket (41,9%), fitting the most frequent users of BNPL. This overrepresentation is one of the drawbacks of convenience sampling, and it might lead to less representative results. However, as most BNPL users are around that age, it fits the purpose of this particular study. Second largest age

bracket was 18-24 (18,7% of respondents), followed by 50-65 (19,2%), 35-50 (10,3%) and lastly 65+ (9,4%). Regarding employment, most participants were either students (30%, n = 61) or working full time (47,8%, n = 97), making up 77,8% of the sample. The participants educational background mostly consisted of highly educated people, with 36,5% (n = 78) having completed a Bachelor's degree and 38,4% (n = 74) having completed a Master's degree. Together these two groups make up 74,9% of the participants. Regarding their online purchasing habits, almost half (49,8%) reported purchasing products online more than 10 times a year, meaning they are experienced online shoppers. Only 1% reported purchasing products less than once a year. In total, 76,4% of respondents reported purchasing products online *more* than 5 times a year.

Considering that those who chose to agree or strongly agree resonate with the statement and vice versa, we find the following descriptive statistics regarding risk taking propensity:

- 76,8% prefer to avoid risks. Only 6,9% disagree with this statement.
- Only 25,2% claim to take risks regularly.
- 77,8% dislikes uncertainty, while 6,9% disagree with this.
- 25,1% categorize themselves as risk takers.
- 57,7% categorize themselves as risk avoiders.

The respondents most strongly agreed with their chosen payment option giving them *security*, indicating that this is an important reasoning and variable for a customer considers when purchasing products online. Looking into the specific payment methods, BNPL was the payment method with the highest mean score in security, but lowest in value. Refer to table 1 for the mean score of all payment methods on the different reasoning for choosing them.

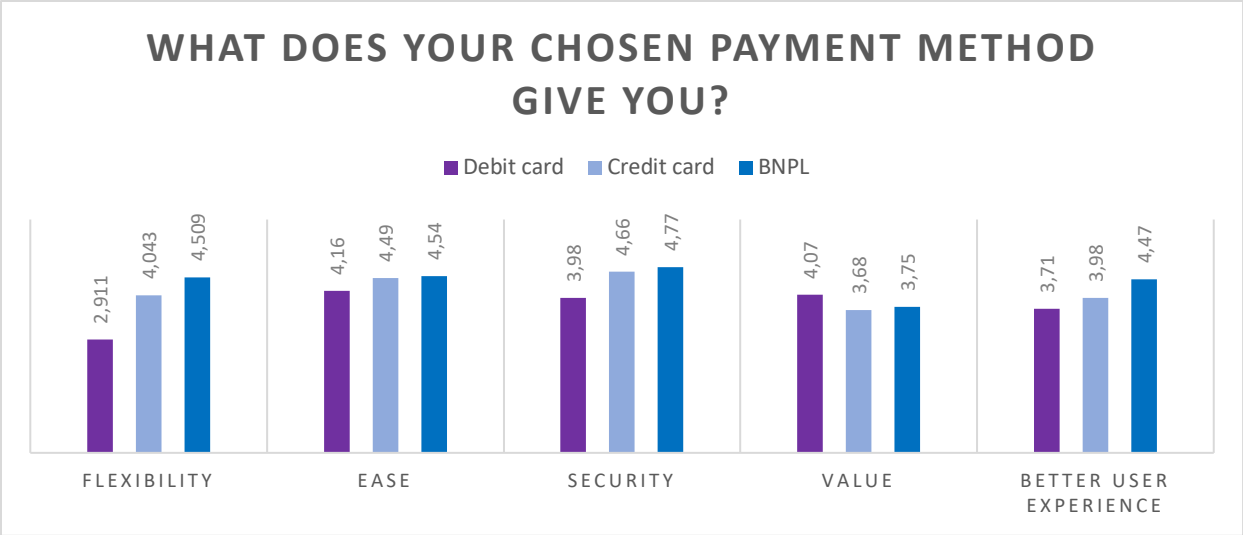


Table 1: Each payment methods mean score for the different advantages

Regarding the participants preferred payment method, 43,3% of participants (n = 88) reported BNPL usually being their preferred when purchasing products online. Credit cards made up 28,6% (n =58) and debit cards 22,7% (n=46). In the "other" bracket, making up 4,9% of responses (n = 10), the answers mostly consisted of *Vipps* (Norwegian mobile payment app) and *PayPal*. The advantages these have from a consumer perspective is that you do not need your account or card information to pay, as it is often protected with a password instead. Hence, they make easy and flexible payment methods (PayPal, 2021; Lyra, 2020). Because the study is distributed among many Norwegians and a large part of the sample should consist of these, it is no surprise that Vipps, a common payment method in Norway, emerged as a preferred method. PayPal is a payment method widely used on a global basis, so neither this came as a surprise.

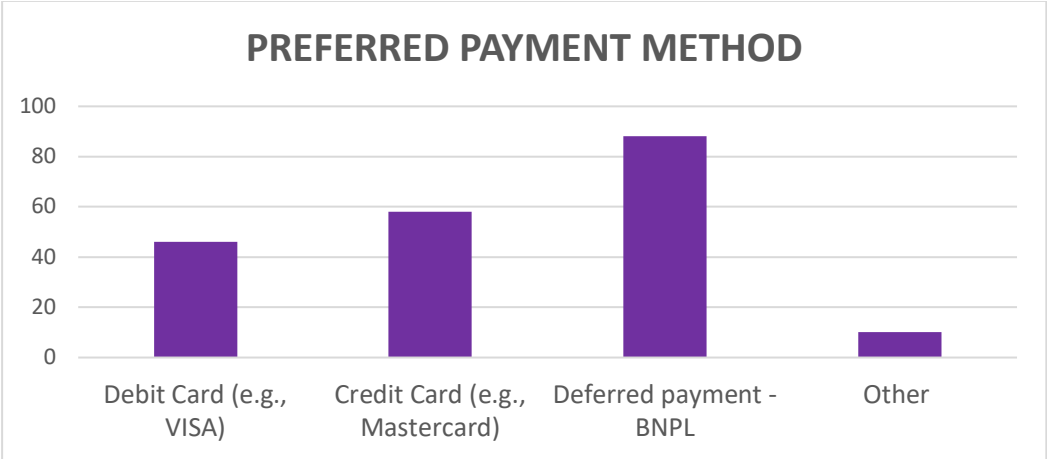


Table 2: Participants preferred method of payment.

4.8 **Data Analysis**

In the following data analysis, a reliability test is performed to measure internal consistency of all scales before continuing with the further data analysis. Secondly, independent samples t-test is performed to compare the two conditions based on the different scales. Thirdly, a mediation analysis is performed for the mediator. Lastly, a regression is performed to confirm the findings in the mediation analysis. Throughout the entirety of the data analysis, a significance level of 0.05 is used to determine statistical significance.

4.81 Reliability Analysis

A reliability analysis is conducted to ensure internal consistency with the scales used in the survey. According to Gripsrud, Olsson & Silkoset (2010) for the measurement to be reliable, the scales Cronbach's alpha should be between 0.70 and 1.

Risk Perception (7 items) = 0.917
Brand Trust (3 items) = 0.899
Risk Aversion (2 items) = 0.708
Risk Taking (2 items) = 0.760

As the alphas for risk perception (independent variable) and brand trust (mediator) is above 0.80, they are considered "very good" according to Janssens, et. al (2008). The alphas for risk propensity, both aversion and taking, are considered reliable being above 0.70. These scales can therefore be used in the further analysis of the results.

4.8.2 Independent samples t-test

For all survey measures, independent samples t-tests are performed using the two conditions as the grouping variable, to compare the differences in means for these. As an example, the risk scale is given by a mean risk perception (minimum 1 and maximum 5), where *1* would indicate lower risk perception (extremely unlikely) and when the number moves towards *5* it would indicate a higher risk perception, towards extremely likely given by the number *5*.

To compress the scales into one score, the mean is calculated for each scale and transformed into one variable. Hence, there is one mean score each for perceived risk, brand trust, risk propensity and payment method criteria. For payment method choice, the original variable ranging from 1-3 is used.

For **perceived risk,** the mean of risk perception in the unknown condition is 3.02 (SD = 0.93) and for the known retailer it is 2.32 (SD = 0,82). The results show a significant difference in risk perception between the two conditions, given by a significant value of <.001. The mean difference between the two is 0.70. These results are in line with the results of the pretest, as well as literature stating that less experience leads to higher perception of risk.

Secondly, for **brand trust,** the mean in the unknown condition is 3.17 (SD = 1.01), and 3.87 (SD = 0.86) in the known condition. The mean difference here is also 0.70, in favor of the known condition. Further, it is significant with a p-value of <.001. Hence, the participants trust the retailer more if they have a positive experience with it which is in line with what literature suggests.

Thirdly, for **payment method choice**, the mean in the unknown condition is 2.50 (SD = 0.687), and 2.14 in the known condition (SD = 0.895). These results mean that those in the *Unknown* condition are more inclined to choose payment option number three (BNPL). This difference is significant with the significance value of <.001. Hence, there is a significant difference in payment choice between those who have a positive experience with a retailer and those who do not have any experience. In the following section, a regression analysis will be conducted to see if risk perception is a significant predictor of payment method choice.

Fourthly, it is relevant to look at the different in the **payment method** criteria based on the condition the respondents are assigned to. It is hypothesized that risk perception has an effect on payment method choice, which we have seen in the previous t-test, yet it is also relevant to look into why the respondents choose different payment methods based on their assigned condition.

There is a significant difference in the two groups for the following reasonings for choice of payment method: security, and value. The other variables have a mean difference as well, but it is not significant. The means and standard deviation of the two variables are shown below:

Security:
Mean (unknown): 4,69
Mean (known): 4,45
SD (unknown): 0,612
SD (known): 0,700

Mean difference: 0,248 (two-sided p: 0,031).

Value:
Mean (unknown): 3,65
Mean (known): 3,95
SD (unknown): 1,053
SD (known): 0,948

Mean difference: -0,307 (two-sided p: 0,008).

Hence, there is a significant difference between the two conditions in terms of security of value. The implication for this is that in the unknown-condition, security is more important than value for the customer. Secondly, it implies that increased risk levels lead the customer to choose a payment option they consider giving them security. Therefore, payment choice can be used as a risk mitigation method by the customer.

4.8.3 Regression

Performing a simple linear regression with solely X (risk perception) and Y (payment method choice) gives an r square of 0.15, meaning that 15% of the variation in payment can be accounted to the different perceived risks associated with the purchase.

The significant predictors of payment method are risk of poor fit, poor quality, and product not arriving. Risk of poor fit (coefficient = 0,161), risk of the product not arriving (0,178) has

a positive effect on payment choice (i.e., higher inclination to choose BNPL). Interestingly, risk of poor quality has a negative effect, meaning in those scenarios the participants are more likely to choose another payment option. Refer to the full regression table below.

Model	B	Std. Error	t	Sig
Constant	1.961	.173	11.330	<.001
Risk: Faulty product	.161	.085	1.883	.061
Risk: Poor fit	**.161**	**.081**	**1.984**	**.049**
Risk: Poor quality	**-.269**	**.082**	**-3.303**	**.001**
Risk: Return product	-.147	.081	-1.817	.071
Risk: Product not arriving	**-.178**	**.073**	**2.457**	**.015**
Risk: Value	-.007	.084	-.078	.938
Risk: Fraud	.132	.070	1.871	0.063

Table 3: Regression table

Examining the data closer, 33% of those perceiving the highest risk of poor quality chooses payment option number 2 – credit cards, for instance a VISA Mastercard. The higher the risk of poor quality, the data shows a higher propensity to choose the credit cards option. At the same time, choice of BNPL is the highest in the lower risk perceptions of this particular risk.

4.8.4 Mediation Analysis

As it is now established that risk perception (X) and payment method (Y) is associated, it is appropriate to perform a mediation analysis to see how the mediator brand trust (M) has an effect on this cause-effect relationship (Hayes, 2017). The mediation analysis was performed using the PROCESS model by Andrew F. Hayes in SPSS, and the exact model used was number 4. In the model the independent variable (X) of risk perception and the dependent variable (Y) of payment method is included, along with the proposed mediator brand trust (M) and control variables of preferences and individual risk perception.

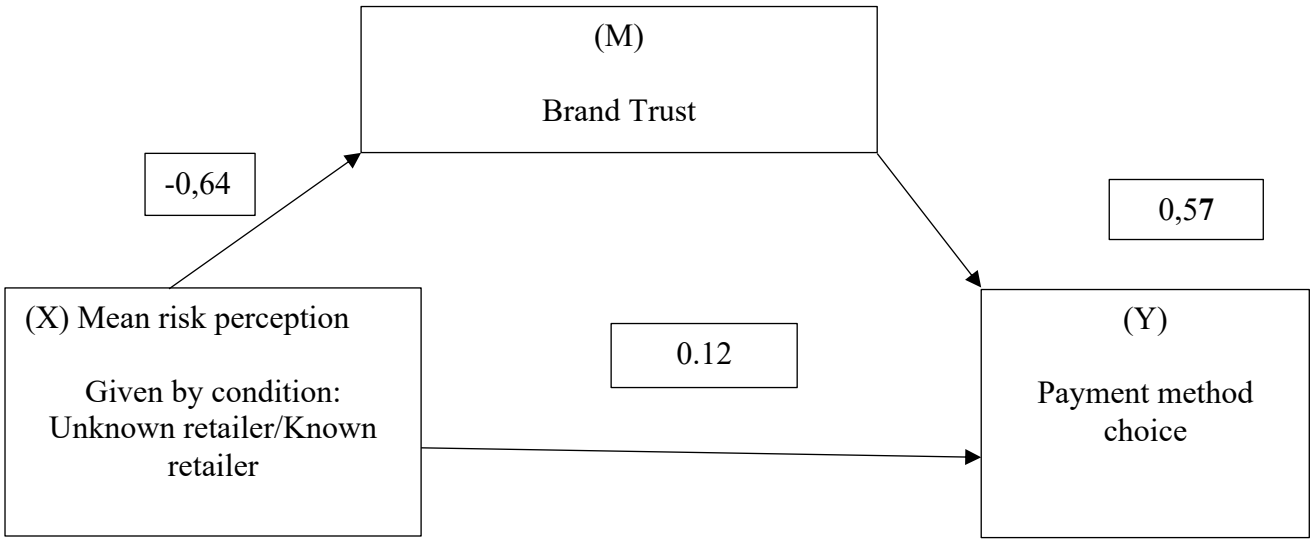
The model has a R square of 0.46, meaning that 45% of the variation in payment choice can be accounted to risk perception, brand trust, purchase frequency and preferences. The model has a p-value of 0.00 and thus statistically significant.

All variables expect risk propensity has a significant value, meaning that there is not sufficient support in the data for risk propensity to be a confounding variable in the choice of payment method. However, habits are significant with a positive coefficient of 0.28, meaning that it has an effect on choice of payment method, often leaning towards BNPL.

X -> Y, c` = 0.12 -> t-value = 2.09 -> p-value 0.04
X -> M, a1 = -0.64 -> t-value = -10.42 -> p-value 0.00
M -> Y = b1 = 0.57 -> t-value = 11.08, -> p-value 0.00

For payment method, the scale is given from 1-3, with 3 being the choice of BNPL. If risk perception increases by 1, the payment method choice is likely to increase by 0.64 – meaning a larger propensity to choose BNPL. Looking at the effect sizes of each relationship, we find that all have a p-value of less than 0,05. Thus, they are all statistically significant.

Proportion of the total of effect that risk perception has on payment method operates indirectly is 46,66%, hence this is the effect of the mediator and the covariates. The rest operates directly in the relationship between risk perception and payment method. However, the mediation effect is not significant as seen from the confidence interval in the output (bootLLCI = -0.0475, bootULCI = 0.1513). Thus, we do not find statistical support that brand trust mediates risk perception in choice of payment method, although it is indicated in the data.



Hence, risk perception leads to less brand trust, and through decreasing brand trust this will have a positive effect on payment choice method, meaning that customers are more inclined to choose payment method number 3 – deferred payment, i.e., BNPL. The direct effect size of X on Y is 0.12 and is significant with a p-value of 0.04. The total and indirect effect of X on Y (through the mediator) is 0.17.

The bootstrap interval for the direct effect of X and Y falls above 0, with bootLLCI = .0065 and bootULCI = 0.2337. The direct effect is therefore statistically significant.

Chapter 5 – Conclusion

5.1 Results and Conclusion

To conclude the study, it is relevant to look back at the two-hypothesis formed in the previous sections and determine if there was found support in the data analysis for these two.
Firstly, **hypothesis 1:**

Consumers that perceive higher risk related to the online purchase, will have a higher propensity to choose BNPL. On the contrary, consumers that perceive a lower risk will have a lower propensity to choose BNPL. Thus, a positive relationship between risk perception and BNPL choice as payment methods, is likely to occur.

The independent samples t-test found support for *hypothesis 1,* as there was a significant difference between the two conditions, and risk being a significant predictor of.
The proportion of total effect risk perception has on payment method operates directly 53,34 %.

Secondly, **hypothesis 2:**

Higher perceived risk in an online retail setting decreases the trust consumers have in the brand thus, leading to BNPL as the payment option for transactions.

Based on the mediation analysis, we do not find support for hypothesis 2, as the mediation effect was not significant. As such, there is not enough statistical evidence in the data that brand trust mediates risk perception in the choice of payment method, in the setting described in the study (online retailing for the clothing category).

In conclusion, support for hypothesis 1 was found in the analysis, but not hypothesis 2. In other words, we find sufficient support in the data that higher risk perception led to increased propensity to choose a BNPL payment solution, but not that brand trust mediates this relationship. Referring to the descriptive statistics, BNPL gives to the largest extent security for the respondents choosing it. Hence, BNPL is used more in situations where customers feel more risk, and thus use it as risk mitigation method. To the least extent, BNPL gives value, as the smallest percentage strongly agree with this.

The results and discussion section involves discussing the study's research question. As a reminder, this was:

How does risk perception affects payment choices, more specifically BNPL, associated with online purchases of clothing items?

As shown in the data analysis, there is a causal relationship between risk perception and payment choice method, where the presence of higher risk leads to a higher propensity to

choose BNPL. In lower risk situations, this propensity to choose BNPL decreases. A part of the explanation behind this is indicatively security for the customer. As there was no significant mediation effect for brand trust, it cannot be inferred that this plays a part in this choosing of payment method. Still, different levels of risk perceptions were associated with different levels of brand trust, as seen in the two conditions.

Naturally, clothing is a specific category, in which results may not be generalizable to other product categories that are lower involvement (e.g., grocery products) or higher involvement (e.g., automobiles). Still, it remains essential for insights into online retailing as it is the most popular category (Statista, 2022). Hence, the results are relevant for a vast number of online retailers in this category, as well as BNPL service providers as clothing is also the most popular category using this payment method (C+R Research, 2021).

The aim of the thesis was to gain insight into consumer choices of payment options and make a contribution to the somewhat limited research in this area. Through collection of primary quantitative data and an analysis in statistical software SPSS, this study has provided information about consumers online behavior and choices using different risk-induced scenarios. More specifically, that risk perception has an effect on which payment method is chosen. Thus, the reasoning behind these choices in a high involvement product scenario where consumers put more thought into their choices. In this study, the focus was on the payment solution known as BNPL. Increased security seems to be the reasoning behind this choice, although this should be further empirically tested.

5.2 Managerial implications

The main finding of risk perception having a direct effect on choice of payment method, has important managerial implications. Firstly, focusing on the online retailers, those who have yet to gain trust in the market, and thus inducing higher risk perception among the consumers, a BNPL payment solution could be used to mitigate said risk and get the customer to “try before they buy”. It is not established in the study whether the absence of BNPL would lead the customer to not buy the product, but as there is higher risk perceived with the purchase it is more likely that a customer will abandon the purchase if BNPL was not present. Therefore, it is reasonable to assume that the presence of BNPL leads to higher acquisition rates and sales, especially for retailers that has yet to gain a lot of repeat customers. As noted in chapter

1, risk has a negative impact on the customer purchase experience, making it less pleasant for the customer. Although it is not tested in this study whether the presence of BNPL has a positive impact on the customer purchase journey (which can be difficult in such an artificial setting), the presence of a risk reliever should make the experience smoother for the customer as there is increased perceived security. Secondly, for BNPL service providers, such as Klarna or Afterpay, gaining increased insight into why customers choose their solution is useful as a selling proposition both in the B2B and B2C market. As mentioned, security is indicatively the most important reasoning behind customers choice of BNPL in higher risk scenarios. Hence, the sense of security this payment solutions give customers can be communicated to persuade more online retailers to adapt to their solutions. Marketing campaigns towards customers should increasingly be centered around the security aspect, as well as the existing narrative of better flexibility and ease of use.

Overall, in the study, the most preferred payment method regardless of condition the respondent was exposed to was BNPL, supporting that the adoption of this solution will only continue to grow. As such, it will be crucial for online retailers to provide this payment solution for its customers. For other payment solution providers, the higher value it has compared to BNPL can be a powerful persuader for customers to choose these instead. As BNPL has been tied to overconsumption and consumer debt, such insights are valuable for marketers working to reverse this trend.

5.3 Limitations and future research

As any study, this is not short of limitations worth mention. Inherent in the study and sample method there are several limitations already mentioned. These were related to over representativeness of certain age groups, which was realized in the sample with 60,6% of respondents being below the age of 35. Secondly, there is the possibility of nonresponse bias and self-selection bias.

Firstly, the brand trust manipulation, which managed to induce risk perception but was not a significant mediator, may not be reliable because it presents a mere description of a scenario. A mere description is often not enough to mimic a natural setting, and now that an interaction between the variables have been established, for future research these should be tested in a more natural setting to increase the generalizability of the results. Also, there was no brand

present in the study, which excludes all the variables that may influence the customer. These include brand name, logo, website design, among others. These factors naturally make the study less generalizable to a real setting, although adding these to the study would possibly have added several confounding variables difficult to control for.

Furthermore, it is not tested in the study whether BNPL actually induces a higher willingness-to-purchase, only that it is a preferred payment option in cases with higher risk. However, to know if consumers truly use it as a risk mitigation method it would be required to test if they would buy from the retailer despite of the higher risk they perceive, and that they would do so using BNPL. Additionally, a condition could be added where the customer itself does not have experience with the retailer, but solely friends and family. Word of mouth, both online and in-person, has a strong effect on purchase intention and willingness to buy and should also have an effect on the results in this study (Keaveney, 1995; Chen et al., 2014). Further research should look into the purchase intention of these consumers based on the results in this study. Hence, if the presence of BNPL actually leads to the purchase.

Summary

Chapter 1 - Introduction

The chapter started by explaining how e-commerce and the wide array of payment solutions that go with it are growing and expanding. One of the most rapidly adapted payment solutions, which is also relatively new, is known as Buy Now, Pay Later (hereby referred to as its acronym BNPL). This payment solution is mostly available online, although some physical retailers have started implementing it as well. As its name states, BNPL allows the customer to buy a product immediately but delays the payment until later. The sum is paid upfront by the BNPL provider, thus involving little financial risk for the retailer (although having to pay a fee) (Fisher, Holland & West, 2021). Different BNPL service providers offer the customers different purchase options. However, most of them involve that the customer either pay in installments (For instance four installments where each is paid every second week) or delaying the payment into a given future date (Such as 14 days, 10 days, 30 days). The availability of the specific payment type varies based on geographical territory and service provider. The number of providers offering BNPL is increasing, yet the most prominent players include Klarna, Afterpay, and PayPal Credit (Grand View Research, 2021).

Many companies used deferred payments as an option to please risk-averse and convenience seeking consumers (Deufel & Kemper, 2018), as deferring payments give customers the option of trying the product before actually buying from it (in the sense that money is withdrawn from their account). As long as the amount due is paid within the specified timeframe, it is interest-free and often free of charges, in several ways being more beneficial than the traditional credit card. BNPL has experienced substantial growth in recent years, with solid consumers and retailers adoption. As an example, from 2020 to 2021, adoption of BNPL increased with 18% in the U.S. (FinTechtris, 2021). The Covid-19 pandemic has made consumers more comfortable with e-commerce, as it became an even more convenient option due to physical stores closing or consumers avoiding visiting them due to fear of getting infected. With the pandemic, online retailing has only continued to grow its momentum, with 71 % of consumers reporting that they have purchased more items online since its beginning (C+R Research, 2021). Hence, seeing the need for more insight into online retailing and, among others, how consumers make choices in this scenario which is the focus of the paper.

Such insight is relevant for many reasons, but the main one named in this thesis paper is that it is relevant for online retailers to know how adapt their payment options to the needs of their customers and the experience they want to provide them. The founder of the 4Ps of marketing, Philip Kotler, has stated that "Payments have become an important element of the selling proposition and should be considered the 5th P of marketing" (Shevlin, 2021). Previous research has emphasized that it is crucial for businesses to offer flexible payment channels to meet their customers' expectations, as 83% of customers want retailers to implement alternative electronic payment options, such as BNPL (Global Payments Inc, 2021).

There are several reasons behind consumers choice of BNPL, and this has been explored to some extent in selected empirical research already. As mentioned initially, consumers like to delay payments because the pain of paying gives negative emotions. Still, BNPL allows consumers the instant gratification of buying themselves something new. Furthermore, consumers have reported using BNPL because they cannot otherwise afford it – 59% of respondents in data collected by C+R Research (2021) say they purchased an "unnecessary" item that they otherwise could not afford. Other reasons include being more convenient and flexible, lower interest rates, and an alternative for maxed-out credit cards. For product categories, the most common items purchased using BNPL are clothing (accounting for 47% of the respondents purchases) and electronics (44%). Further insights into why consumers choose BNPL are relevant for policymakers as well, as it has been tied to consumer debt and overconsumption of products. BNPL has been criticized for encouraging consumers to take on debt they might not afford, thus being tied to increased consumer debt. In fact, over the past two years, 43% of BNPL users have made late payments (Shevlin, 2021). Data also indicate that BNPL is here to stay, as among those who have used the service, 85% plan to continue doing so in the future (TSG, 2021). The use of BNPL has received criticism as well, as it is tied to overconsumption, especially clothing, because consumers tend to order more when seeing this option at checkout (Gifford, 2020).

For demographic data on the BNPL customer, they are more likely to be a Gen Z or Millennial (Gen Y) female (Bien, 2021) early in their career. Gen Z and Gen Y have a larger tendency to employ different payment methods when purchasing online and have a higher credit card use, which BNPL has become the main competitor of (PYMNTS.com). Because consumers view online retailing as having some uncertainty, it can be deemed a safer solution to delay payment until the item is received. A BNPL report by Bain (2021) found the option

to "try before you buy" as an advantage that consumers value with the services, which can be viewed as a risk mitigation method as it delays the loss of potentially buying something you do not want to keep. Still, risk mitigation in itself has not been explored or mentioned as a direct advantage of BNPL, and in some reports, no such method (as try before you buy) is included. Thus, it is interesting to assess how perceived risk and the mitigation of such risk affect the choice of payment options online.

The research question that emerged from this discussion was:

How does the deferred payment involved with BNPL option affect consumers' risk perceptions and payment choices with online purchases of clothing items?

Chapter 2 – Literature review

The most substantial part of the thesis, the basis of the literature review was that BNPL is a concept yet to be widely explored, although it has increasingly caught the interest of researchers (Garcia Alvarez, 2021). Especially the link between consumer debt among young people and the payment solution has been explored in the literature. For other payment solutions, other areas such as benefits for credit cards has been explored in the literature (e.g., Chakravorti & To, 2007). Still, BNPL distinguishes itself from other e-payments in terms of convenience

On the basis of this, the literature review focused mostly of psychological factors. As BNPL distinguishes itself from other e-payments and is an increasingly adopted and in-demand payment solution, often being preferred by consumers to credit cards, there is a need for further research on the topic. Firstly, as there is no actual money withdrawn from the customer's credit card, it delays the perceived monetary loss (Prelec & Loewenstein, 1998; Bornemann & Homburg, 2011). In the case of temporal distance as with BNPL, the loss of money becomes more abstract and can mitigate the pain of paying associated with a purchase (Soman, 2001). This factor can partly explain why consumers overspend with BNPL, as the actual loss of money is delayed and thus seen as having less consequences. Secondly, there is often no interest charge with BNPL, as there often is with credit cards. These differences have proven to have important implications for consumer behavior, given the rapid and increasing adoption of the service.

As discussed, BNPL is mostly adopted by online retailers and mostly relevant in an online setting; thus, the online retailing environment will be the focus of the study. Consumer perceptions and behavior differ in an online setting, and thus it there is the need for a review on this specific setting (e.g, Wolny & Charoensuksai, 2014; Dokulil et. al, 2020). An important reason for this difference is that customers in online retailing cannot ascertain the quality of the product before purchase, which can lead to uncertainty and increased risk perception on the consumers' side (Akerlof, 1995; Dokulil et. al, 2020). The same can be said for high and low involvement purchases, as the amount of time, effort, and resources the purchase requires shape consumer behavior in many ways (Mittal, 1995; Bloch and Richings, 1983; Jain, 2019). Trust is shown to decrease perceived risk and is thus discussed. Because many online retailers do not have a physical presence and rely solely on e-commerce, and are not well-known brands, risk management is imperative in e-commerce and especially for the online marketer (Grabner-Krauter & Kaluscha, 2003).

Forsythe & Shi (2003) defines perceived risk in specifically online retailing as "the subjectively determined expectation of loss by an internet shopper in contemplating a particular online purchase". Several studies have shown that perceived risk is considered the most impactful negative psychological influencer of online retailing behavior (e.g., Ariffin, Mohan & Goh, 2018; Mortimer, Hasan, Andrews & Martin, 2016; Wu & Ke, 2015). Jacoby and Kaplan (1972) found five relevant components of perceived risk for consumers: financial risk, physical risk, performance risk, psychological risk, and social risk. In sum, these become the overall perceived risk. Bitner and Zeithaml (2003) assume that financial risk often occur right after the customer makes an online order. As such, with the option of paying later, this risk is mitigated or delayed until a later time because there is no actual loss from the consumers' side until they can properly assess the product (Consequently mitigating the perceived performance risk). Performance risk is related to the product not being as expected (e.g., size too small or product being faulty). With the introduction of e-commerce, researchers have extended the different categories of perceived risk into an online setting. These include non-delivery risk, convenience risk and return policy risk (Wai, Dastane, Johari & Ismail, 2019). Especially the possibility of delivery failure and financial risk were strong determinants of perceived risk and thus negative influencers of purchase intention. Risk perception also greatly depends on past experience (Siegrist, 2019), and consumers that have less experience with e-commerce will also experience it as riskier (Mainardes et. al, 2019).

Purchases differ in terms of complexity and how much thought the consumer put into it and are classified as either low or high involvement purchases (Mittal, 1995). Among other factors determining degree of perceived risk, it can vary from product category to product category. Partly due to risk perception varying for low or high involvement purchases because the amount of effort and resources put into them vary. BNPL is mostly used to purchase clothing, which is commonly considered a high-involvement product (Solomon, 1986; Jensen & Hansen, 2006). A relevant characteristic for high involvement purchases is that they are riskier (Bloch and Richings, 1983; Jain, 2019), also expressed through the perception of consumers (Pires, Stanton & Eckford, 2004). Perceived beliefs about the outcome of our behavior are predictors of behavioral intentions (Ajzen, 1991), and in the case of a potential loss, we will alter our behavior to mitigate this risk. Hence, if consumers perceive risk at the point of choosing payment solutions, they will choose one that reduces the uncertainty with the transaction.

In review of the relevant literature on risk mitigation in online retailing, it is clear that an aspect that has not been widely explored is the choice of payment solutions in online retailing as a means of reducing uncertainty. Arguably, the presence of being able to pay later removes some of the potential loss perceived by the customer. Further, customers should choose the payment method that reduces the uncertainty of the transaction. Hence, BNPL can work as a loss aversion/risk mitigation method in the case of uncertainty. In a recent study on the choice of payment method, Jang, Miao & Chen (2021) found that pay now options are avoided by consumers if they feel higher risks related to the purchase. Hence, they use it as a type of risk mitigation method. Temporal construal theory state that distant future situations are construed on a higher level than near-future situations (Liberman & Trope, 1998). Research shows that it has important implications in decision making, as it affects how people perceive a certain event (Trope & Liberman, 2010). Hence, the implications are more abstract and thus the monetary loss may feel less concrete for the customer in the case of delaying payments. Temporal distance has implications for BNPL because the time between the purchase and the actual transfer of money is longer.

The study by Jang, Miao & Chen (2021) was set in the travel industry, which is both higher involvement and often higher temporal distance to the purchase moment (compared to clothing which is the focus of our study). Hence, it is interesting to look into how this proposed effect works in lower involvement products such as clothing, and where the

realization of the purchase is more present in time (higher degree of instant gratification). As such, in the case of purchasing clothing online, as the delivery time frame is often shorter than for a travel. Jang, Miao & Chen (2021) argue that their research is the first to study how consumers perceived risks from different payment options are influenced by temporal distance (as is the case with BNPL).

Trust in the online retailer can overcome the barrier of risk (Harridge-March, 2006), and ensuring that trust is stronger than risk is imperative for e-commerce companies (Grabner-Krauter & Kaluscha, 2003). Conversely, lack of trust leads to transaction aversion, especially in online economic exchanges (Hoffman, Novak & Peralta, 1999; Cases, 2002; Ha & Stoel, 2009). Hence, in case of the consumer not trusting the online retailer, they adhere from purchasing from them. Although studies have been made in an online retailing setting, how payment method choices are made online remain quite unexplored in the literature (Deufel & Kemper, 2018). Because it is easier to abandon a website than walking away from the cashier at a physical retailer, customers are more sensitive online with respect to payments. Also, it is easier to search for alternatives. The "online purchase decision-making is a dynamic and highly flexible process" (Karimi, Papamichail, & Holland 2015). As such, the consumer decision process is intricate and needs thorough examination, especially regarding what factors cause certain behavior and how to influence these. Age and experience are also named in the literature review as factors affecting the choice of payment method online.

In summary, knowledge areas yet to be fully explored include a more in-depth analysis on how risk perception affects the choice of payment method, and how consumers try to mitigate loss perception through the purchase stage of the consumer journey, increasingly important with the wider array of choices consumers have. One of the concepts worth to be investigated is how the delay in payment may induce or make more prone the consumer to take more risk, as there is a lower potential loss perception. The research gap that the study aims to fill is the lack of full understanding of how the choice of payment methods may be affected. More specifically, how consumers delay payment as a means of risk mitigation in cases of higher perceived risk purchases.

After the literature review, it is hypothesized that instead of there being a simple linear relationship between risk perception and payment method choice, brand trust is an antecedent of risk perception. Hence, decreased brand trust has a causal relationship with risk perception

which in turn affects payment method choice. The research question that came out of the literature review is as follows:

- *How does the deferred payment involved with BNPL option affect consumers' risk perceptions and payment choices with online purchases of clothing items?*

Chapter 3 – Conceptual Framework

In the conceptual framework, it is shown that because risk perception creates an expected loss, which is especially present online, not having a monetary loss associated with the purchase can make it more abstract. There are a lot of reasons consumers choose different payment methods, where the ones mostly named in literature is related to cost (such as service or interest fees), convenience, security (related to unwarranted monetary loss or disclosure of personal information), preferences and habits. Others include place of purchase, transaction amount, customer demographics, among others (Cruijsen, Hernandez & Jonker, 2016; Swiecka, Terefenko & Paprotny, 2021).

It is also looked into which consumers are more likely to be risk averse, and experienced customers should be less risk averse. Studies have also shown women to be more risk averse than men (Byrnes, Miller, & Schafer, 1999). Previous experience with a brand can also mitigate the risk associated with a purchase, as well as the presence of reasonable return policies (Kim, 2010; Roselius, 1971). Furthermore, it is shown that customers feel less "pain" when there is a time gap between the time they consume the product and when they actually pay for it (Ariely & Kreisler, 2018). Hence, the actual monetary loss is felt less deeply. Because of this, deferring payments can be used as a mitigation method where consumers fear a monetary loss, i.e., they experience higher perceived risk of the purchase.

From this discussion, the first hypothesis is formed:

Hypothesis 1: Consumers that perceive higher risk related to the online purchase, will have a higher propensity to choose BNPL. On the contrary, consumers that perceive a lower risk will have a lower propensity to choose BNPL. Thus, a positive relationship between risk perception and BNPL choice as payment methods, is likely to occur.

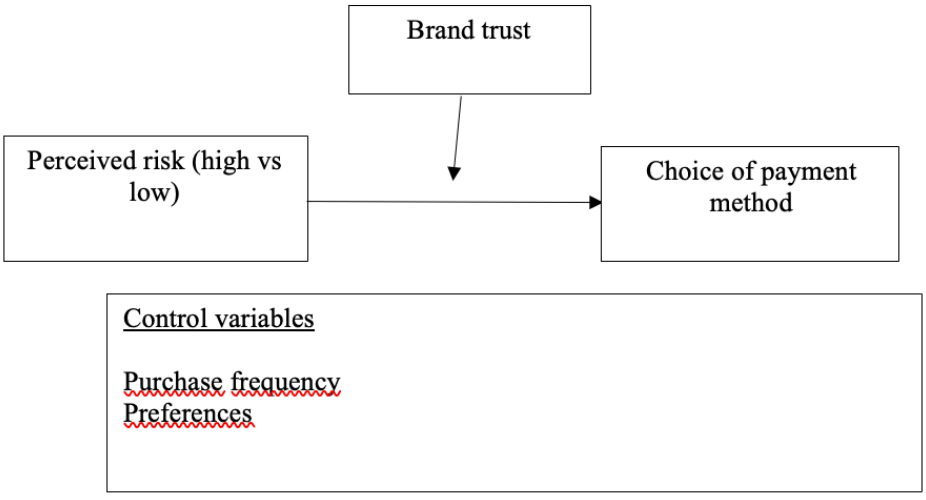
Trust as a variable is also discussed and is shown in many studies to have an inverse relationship with risk, especially in high involvement product categories. Hence, increased risk should lead to less trust, and vice versa. Also, increased trust leads to less trust. This is also found to be true for brands and in B2C relations.

From this discussion, the second hypothesis was formed, where brand trust is found to be a mediator in the relationship between risk perception and payment method choice:

Hypothesis 2: Higher perceived risk in an online retail setting decreases the trust consumers have in the brand thus, leading to BNPL as the payment option for transactions.

With the relation and link between the above variables, the conceptual framework is expected to work as described below. Perceived risk is the independent variable and choice of payment method is the dependent variable. Brand trust is the mediator. In addition, there are two control variables:

- **Purchase frequency**: Higher purchase experience might lead to higher propensity to use deferred payment, as frequent shoppers are known to be more attracted to this payment method (Constantinovici, 2021).
- **Preferences:** Arguably, the preferred payment method can be chosen regardless of the risk perception of the customer, and it is therefore important to control for. For instance, a customer may choose BNPL out of preference and not the risk associated with the purchase.



Chapter 4 – Methodology

The *research design* chosen for the study is a quantitative survey, as the aim is to see the interaction between the independent variable risk perception and the dependent variable of payment method, and the mediating effect of brand trust. In addition, a survey allows for controlling for online purchasing experience as well as preference in payment method. Limitations to this method is named (Namely that it is difficult mimicking a natural setting, and the possibility of non-response bias).

For the *data collection,* there is a pretest and a main survey where responses are both collected through *Qualtrics.* Respondents to the survey were collected through a mixture of convenience and snowball sampling, as the survey was distributed through social media, and many were encouraged to distribute it further to their networks. This sampling method is cheap and convenient, yet there is the possibility of *over-representation* of certain groups (in this case it is more likely to be Gen Z and early Millennials). The sample size ended up consisting of **202** respondents, after data cleaning. These respondents were evenly distributed in both conditions, ensuring that they had over 100 respondents each.

A mentioned briefly, a pretest was conducted prior to the main survey (with n = 47 respondents). The pretest simply tested if two different scenarios created different risk perceptions, as the scenario described had not been empirically tested although based on literature on how previous positive experience with a brand lead to decreased risk perception. The participants were presented with one scenario out of two, using the randomization feature in *Qualtrics*, where one scenario (*positive experience*) explained that the respondent had a positive experience with an online retailer with no setbacks. The other scenario (*no experience*) explained that neither the respondent nor any of their friends/family had any experience with the brand. Everything else in the description was kept constant to isolate the two conditions tested. Afterwards, the respondents assessed how likely they deemed specific risks associated to the purchase. These risks were derived from Jacoby and Kaplan (1972) and Wai, Dastane, Johari & Ismail, (2019). The risks they were asked to evaluate included non-delivery risk, financial risk, privacy risk, performance risk (in a clothing specific scenario) and product risk. This pretest help ensure that the scenarios presented in the test actually differed in terms of induced risk perception. An analysis in SPSS showed a significant

difference in risk perception between the *positive experience* and the *no experience* groups. The two descriptions of the different conditions were thus kept for the main survey, as well as the questions assessing the respondents risk perception.

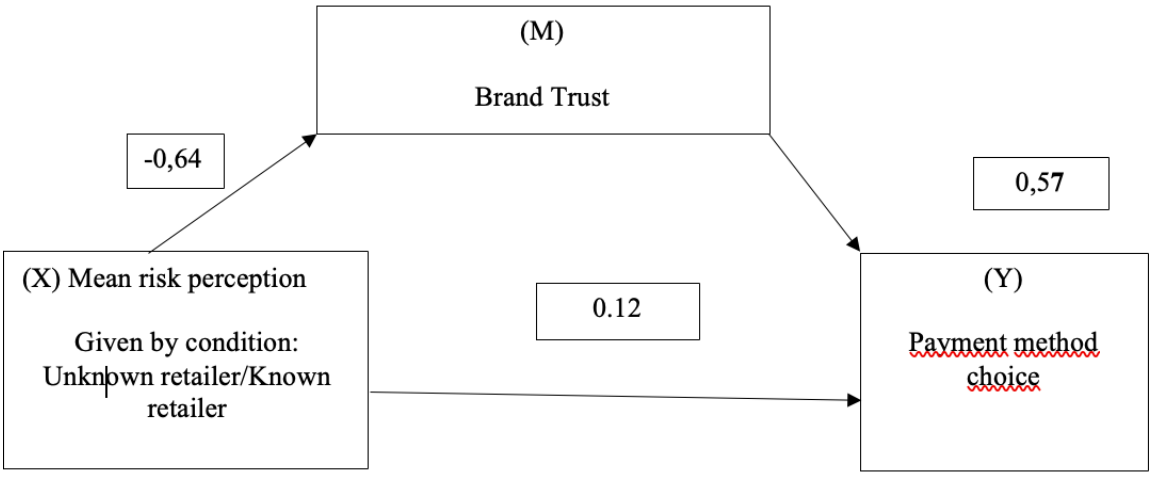
In the main study, survey measures included risk perception, risk taking propensity, brand trust, purchase frequency, preferences, which payment option that the respondents choose according to their assigned condition and what this payment method gives them (e.g., convenience, security – to assess the reason behind their choice). All were on a 5-point Likert scale, but questions warried from likelihood to strongly agree/disagree. See the appendix for the entire, final survey. The survey also measured demographics.

Descriptive statistics revealed a larger representation of females, and those in the age groups below 35 years. Still, all ages and genders were represented in the sample. Most were employed full-time, or students, and considered highly educated (minimum Bachelor's degree). Interestingly, almost half of the respondents reported purchasing products online more than 10 times a year, making this a sample of experienced online shoppers. BNPL was the most preferred payment method, with almost half of respondents naming this.

A *reliability analysis* showed decent internal consistency among all the scales used, with two of them classifying as "very good" according to Janssens, et. al (2008). These were risk perception and brand trust, both derived from scales developed by academics. An *independent samples t-test* showed a significant difference between the two conditions for perceived risk, brand trust, and payment method choice. The unknown condition experienced more risk, less brand trust, and was more inclined to choose BNPL as payment option. For the reasoning behind their choice, those in the unknown condition shown a statistically significant preference to choose option based on *security* (consistent with what it was hypothesized that would be the reasoning for choosing BNPL). However, those in the known category shown a statistically significantly preference to choose based on *value*. The implication for this is that in the unknown-condition, security is more important than value for the customer. Secondly, it implies that increased risk levels lead the customer to choose a payment option they consider giving them security. Therefore, payment choice can be used as a risk mitigation method by the customer.

A *regression analysis* showed that 15% of the variation in payment (R square = 0.15) can be accounted to the different perceived risks associated with the purchase. Risk of poor fit (coefficient = 0,161), risk of the product not arriving (0,178) has a positive effect on payment choice (i.e., higher inclination to choose BNPL). The significant predictors of payment method are risk of poor fit, poor quality, and product not arriving. Risk of poor fit (coefficient = 0,161), risk of the product not arriving (0,178) has a positive effect on payment choice (i.e., higher inclination to choose BNPL). Interestingly, risk of poor quality has a negative effect, meaning in those scenarios the participants are more likely to choose another payment option.

Lastly, a mediation analysis was performed to assess the mediation effect of brand trust, which is related to hypothesis 2. The model has a R square of 0.46, meaning that 45% of the variation in payment choice can be accounted to risk perception, brand trust, purchase frequency and preferences. Proportion of the total of effect that risk perception has on payment method operates indirectly is 46,66%, hence this is the effect of the mediator and the covariates. The rest operates directly in the relationship between risk perception and payment method. The model has a p-value of 0.00, thus; statistically significant. The conceptual framework after the mediation analysis is shown below. However, it is important to note that the mediation analysis did not find sufficient statistical support for brand trust working as a mediator.



Chapter 5 – Conclusion

Based on the data analysis, sufficient support was found in the data for hypothesis 1, but not 2. The two hypotheses are repeated below:

> ***Hypothesis 1:*** *Consumers that perceive higher risk related to the online purchase, will have a higher propensity to choose BNPL. On the contrary, consumers that perceive a lower risk will have a lower propensity to choose BNPL. Thus, a positive relationship between risk perception and BNPL choice as payment methods, is likely to occur.*

> ***Hypothesis 2:*** *Higher perceived risk in an online retail setting decreases the trust consumers have in the brand thus, leading to BNPL as the payment option for transactions.*

Referring to the descriptive statistics, BNPL gives to the largest extent security for the respondents choosing it. Hence, BNPL is used more in situations where customers feel more risk, and thus use it as risk mitigation method. To the least extent, BNPL gives value, as the smallest percentage strongly agree with this. The results and discussion section involves discussing the study's research question. As a reminder, this was:

How does risk perception affects payment choices, more specifically BNPL, associated with online purchases of clothing items?

As shown in the data analysis, there is a causal relationship between risk perception and payment choice method, where the presence of higher risk leads to a higher propensity to choose BNPL. In lower risk situations, this propensity to choose BNPL decreases. A part of the explanation behind this is indicatively security for the customer. As there was no significant mediation effect for brand trust, it cannot be inferred that this plays a part in this choosing of payment method. Still, different levels of risk perceptions were associated with different levels of brand trust, as seen in the two conditions.

The aim of the thesis was to gain insight into consumer choices of payment options and make a contribution to the somewhat limited research in this area. Through collection of primary quantitative data and an analysis in statistical software SPSS, this study has provided information about consumers online behavior and choices using different risk-induced scenarios. More specifically, that risk perception has an effect on which payment method is chosen. Thus, the reasoning behind these choices in a high involvement product scenario where consumers put more thought into their choices. In this study, the focus was on the payment solution known as BNPL. Increased security seems to be the reasoning behind this choice, although this should be further empirically tested.

Three important managerial implications are discussed:

- Online retailers who have yet to gain trust in the market, and thus inducing higher risk perception among the consumers, a BNPL payment solution could be used to mitigate said risk and get the customer to "try before they buy". It is not established in the study whether the absence of BNPL would lead the customer to not buy the product, but as there is higher risk perceived with the purchase it is more likely that a customer will abandon the purchase if BNPL was not present. Therefore, it is reasonable to assume that the presence of BNPL leads to higher acquisition rates and sales, especially for retailers that has yet to gain a lot of repeat customers.
- For BNPL service providers gaining increased insight into why customers choose their solution is useful as a selling proposition both in the B2B and B2C market. As mentioned, security is indicatively the most important reasoning behind customers choice of BNPL in higher risk scenarios. Hence, the sense of security this payment solutions give customers can be communicated to persuade more online retailers to adapt to their solutions. Marketing campaigns towards customers should increasingly be centered around the security aspect, as well as the existing narrative of better flexibility and ease of use.
- Overall, in the study, the most preferred payment method regardless of condition the respondent was exposed to was BNPL, supporting that the adoption of this solution will only continue to grow. As such, it will be crucial for online retailers to provide this payment solution for its customers.

For limitations and future research, the main limitations are connected to it not being set in a natural setting, with no actual brand present and the customer not choosing the payment option on a real (or even imitated) website. Furthermore, it is not tested in the study whether BNPL actually induces a higher willingness-to-purchase, only that it is a preferred payment option in cases with higher risk. However, to know if consumers truly use it as a risk mitigation method it would be required to test if they would buy from the retailer despite of the higher risk they perceive, and that they would do so using BNPL. Additionally, a condition could be added where the customer itself does not have experience with the retailer, but solely friends and family. Word of mouth, both online and in-person, has a strong effect on purchase intention and willingness to buy and should also have an effect on the results in this study (Keaveney, 1995; Chen et al., 2014). Further research should look into the purchase intention of these consumers based on the results in this study. Hence, if the presence of BNPL actually leads to the purchase.

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Appendix

Appendix 1: Survey

Dear respondent,

The following survey is made as part of my master thesis in Marketing at Luiss Guido Carli University. Participation in this study is voluntary, but highly appreciated, and will only take a few minutes. All responses will be anonymous and kept confidential.

In the following page you will be given a description of a scenario involving an online retailer. As the first part of the study is based upon this scenario, please read the description carefully. However, please note that there are no right or wrong answers and I am solely interested in your own personal evaluation.

Thank you in advance for your participation!

Appendix 1a: Unknown Condition

You decide you need a few new items in your summer wardrobe, and are therefore searching for clothing brands online. You find a new brand you have not heard of nor used before. What intrigues you about this brand is that they have a promotion out with 20% discount for new customers. To your knowledge, none of your friends/family have bought from this brand before either, and you are then unable to evaluate the quality of it based on their experiences. The website is a single-brand retailer, so all the clothing items you buy are from the same manufacturer.

Appendix 1b: Known condition

You decide you need a few new items in your summer wardrobe, and are therefore searching for clothing brands online. You find a brand you have recently used, which has a campaign out with a 20% discount for returning customers. From your past experience, the brand has delivered the products to you quickly, efficiently and as expected. The products have always been of high quality and you have previously not needed to use their return policy. The website is a single-brand retailer, so all the clothing items you buy are from the same manufacturer.

Appendix 1c: Survey

Based on the description above, how likely do you perceive the risk of the following scenarios?

	Extremely unlikely	Somewhat unlikely	Neither likely nor unlikely	Somewhat likely	Extremely likely
Risk that the product arrives faulty (e.g., torn garment)	○	○	○	○	○
Risk that the product does not fit as expected	○	○	○	○	○
Risk that the product does not live up to the expected quality	○	○	○	○	○
Risk that I might have to return the product	○	○	○	○	○
Risk that the products purchased do not arrive at all	○	○	○	○	○
Risk of losing money on the purchase, or otherwise not getting your moneys worth	○	○	○	○	○
Risk of misuse of your credit card of personal information	○	○	○	○	○

If one or more of the above-mentioned scenarios occurred, please indicate how confident you would feel that the brand would do the following..

	Not confident	Slightly unconfident	Neither confident nor unconfident	Slightly confident	Confident
Address my concerns sincerely and honestly	○	○	○	○	○
Work to solve the problem	○	○	○	○	○
Compensate me properly	○	○	○	○	○

Given these considerations, which of these available payment options would you prefer (given that none other are available to you)?

- ○ Debit card (e.g., VISA)
- ○ Credit card (e.g., Mastercard)
- ○ Buy Now, Pay Later (deferred/delayed payment)

What does this payment option give you?

	Strongly disagree	Somewhat disagree	Neither agree or disagree	Somewhat agree	Strongly agree
Flexibility	○	○	○	○	○
Ease and convenience	○	○	○	○	○
Security	○	○	○	○	○
Value for money (e.g., fewer fees)	○	○	○	○	○
A better user experience	○	○	○	○	○

	Strongly disagree	Somewhat disagree	Neither agree nor disagree	Somewhat agree	Strongly agree
I prefer to avoid risks.	○	○	○	○	○
I take risks regularly.	○	○	○	○	○
I really dislike not knowing what is going to happen.	○	○	○	○	○

I consider myself more of a..

	Strongly disagree	Somewhat disagree	Neither agree nor disagree	Somewhat agree	Strongly agree
Risk taker	○	○	○	○	○
Risk avoider	○	○	○	○	○

Please indicate your age group

- ○ 18-24
- ○ 25-34
- ○ 35-50
- ○ 50-65
- ○ 65+

Please indicate your gender

- ◯ Male
- ◯ Female
- ◯ Non-binary / third gender
- ◯ Prefer not to say

What level of education have you completed after high school?

- ◯ No completed education past high school
- ◯ Trade or vocational
- ◯ 3 year degree (e.g., a Bachelors)
- ◯ 4-5 year degree (e.g., a Masters)
- ◯ Professional or Doctorate

What best describes your current employment status?

- ◯ Student
- ◯ Working part-time
- ◯ Working full-time
- ◯ Self-employed
- ◯ Unemployed
- ◯ Retired

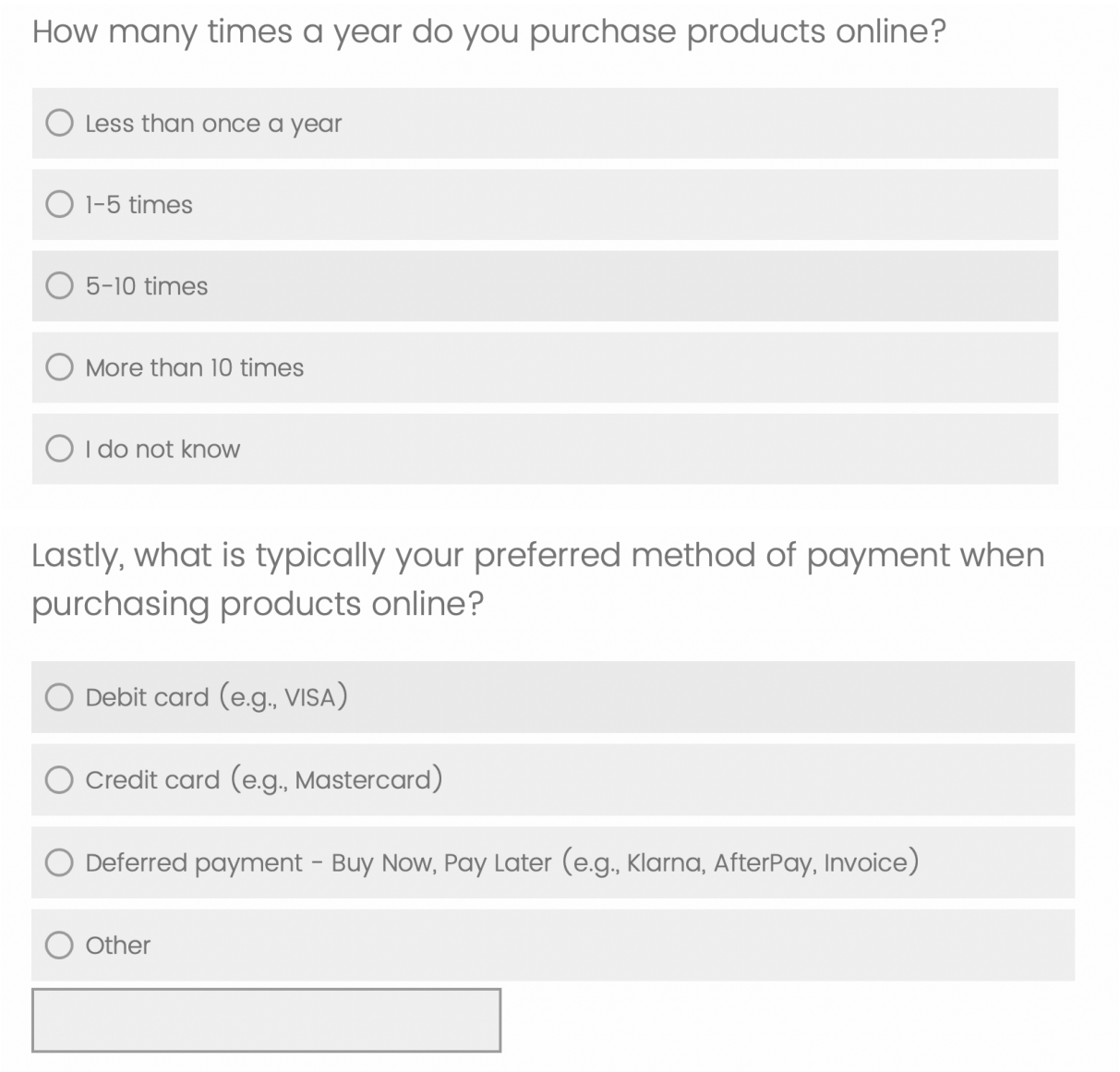

Table: Variables

Scale/Nominal etc.