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KLARNA - NAVIGATING A SCALE-UP THROUGH MARKET TURBULENCE

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A FAIR VALUATION OF KLARNA IN THE MIDST OF A DOWNTURN IN PUBLIC  
MARKETS

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## Abstract

Klarna has earned a reputation as the leading "Buy-now-pay-later" service provider. The fintech's success is heavily built on external capital, having raised \$3.7bn and achieving a post-money valuation of \$45.6bn in 2021. The case begins in June 2022 when Klarna is forced to decide whether to accept a down round to cover its high cash burn and negative profitability after market conditions worsen. The aim of this case is to explore a fair valuation of Klarna given the current market environment.

Keywords (Venture Capital, Downround, Valuation, Fintech, Growth, Profitability, Strategy, Management, Entrepreneurship, Entrepreneurial Strategy, Investments, Entrepreneurial Finance)

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# GROUP PART

## 1. Intro

It was early in the morning in June 2022. Sebastian Siemiatkowski, the CEO and Co-Founder of Klarna, was standing in line at his favorite bakery in Stockholm to get breakfast, as he does every day. Today he was particularly tired, as he had repeatedly slept poorly. There were many things circling in his head at the moment, but probably the toughest decision this year still caused him the most discomfort and is the reason why he racked his brain all night. Only last month, Siemiatkowski had to inform his staff via a recorded video message that 700 employees, 10% of the workforce, would have to leave the company (Browne, 2022). The CEO of the buy-now-pay-later (BNPL) service provider rectified the decision by naming the war in Ukraine, the change in customer sentiment, rising inflation, and volatile stock markets as the main reasons contributing to a shift in the company's future outlook. "We are strongly influenced by the outside world. When we set our goals for 2022 in autumn, it was a very different world than the one we have today," he said (Billing, 2022). Indeed, similar layoffs occurred at Robinhood, Better.com, or BitPanda, which, like most tech companies, have been affected by changing market conditions and need to become more crisis-resistant (Azevedo, 2022). This was also the case for Klarna, which has experienced a steep rise since its founding in 2005, thanks to a transformation from a profitable startup with consistent growth to an international fintech giant with an aggressive growth strategy. This growth was built on a series of funding rounds that provided Klarna with more than \$3.7bn, provided by renowned investors such as Silver Lake and Sequoia Capital. This was necessary to maintain its position as a leader in the BNPL market. Siemiatkowski, who was on his way to the office equipped with an orange juice and a sandwich, knew that after only a year since its last funding round of \$639m in June 2021, the fintech would reach the end of its runway with no additional capital forthcoming - In other words, Klarna would get into real trouble. This threw up some new hard decisions that he and

his management team had to face. There was the option of accepting \$800m in funding, amid the worst stock downturn in 50 years, which would mean slashing Klarna's valuation by 85%, from \$45.6bn to \$6.7bn, causing media backlash and dilution for the founder. On top of that, there was already a tough meeting coming up this afternoon with investors who wanted an update on the firm's strategy. With a recession looming, and the prevailing adverse market conditions driven by large declines in the value of tech stocks in his mind, Siemiatkowski had to ask himself the following questions not only to be prepared for the upcoming discussion with the investors but also to pave the way for Klarna's future strategy to go through tougher times: What are the company's steps to adapt to the market environment? What measures does Klarna need to take to achieve profitability and how would this influence the long-term strategy of the company? And what will be a fair valuation he can accept given the more cautious investor sentiment and the sharp downfall in public markets?

## **2. Background**

Sebastian Siemiatkowski and Niklas Adalberth became friends when they worked on the assembly line at Burger King. Besides having to pay their dues, they also followed the ambition of becoming entrepreneurs themselves. Together with their university friend Victor Jacobsson, they eventually founded a startup in 2005 that would become Klarna, one of the world's most successful online payment processors. Before founding Klarna, the three young postgraduates participated in the Stockholm School of Economics annual entrepreneurship award in 2005 and came up with the idea to make online payments easier and more secure for both consumers and retailers. Although their vision was not enthusiastically received and they ended up being last in the pitch competition, they held on to the pitch of "buy now, pay later" and founded the company under the brand name Kreditor Europe AB. "It made us sound serious, trustworthy and larger than we were," the founders remembered (Klarna, n.d.). Fortunately, the founders of Klarna were eventually introduced to the Swedish angel investor Jane Walerud at a

networking event after their initial rejection. The trio ultimately received €60,000 in seed financing from Walerund in return for a 10% stake in the business (see Exhibit 1). Walerund was not only convinced by their idea but also provided five software engineers to begin working on the project in exchange for a further 37% ownership stake in Klarna (Failory, 2022). In their early days, they developed a website that made it simple for customers to buy things online and receive an invoice within 30 days. “When they began, they didn’t position themselves so much as a startup or as a fintech,” recalls Skype founder Niklas Zennström, whose venture capital firm Atomico would eventually invest in Klarna. “People referred to them as the invoicing company” (O’Hear, 2020).

Being among the first ones developing this payment service, this gave Klarna a significant advantage over its rivals at the time, as e-commerce was still a relatively new idea, putting Klarna early on to the forefront of retail sales. Subsequently, Klarna, still under the name Kreditor, managed to raise capital on a larger scale for the first time in 2007 to begin its international expansion. Through a Series A funding round, the Swedish company AB Öresund invested \$2.2m. This enabled Klarna to launch its payment solution in Norway, Finland, and Denmark within the next two years. Meanwhile, the business benefited especially from the increasing e-commerce activity and gained more and more acceptance among consumers. In 2009, Kreditor was renamed Klarna and employed 120 people before entering the German and Dutch markets the following year (see Exhibit 2). The company's recent success did not go unnoticed in Silicon Valley. In May 2010, Sequoia Capital became an investor and joined the fintech's board. The San Francisco-based VC firm fueled Klarna's growth with a \$9m Series B funding round. As a result, Klarna increased its revenue by 80% to more than \$50m in 2010. The rapid growth coupled with a well-known investor on board eventually attracted interest from other growth investors. These included General Atlantic, which led a \$155m funding round in 2011 with participation from DST Global and secured seats on the board. In 2012,

Klarna launched its checkout product, introducing the "buy now, pay as you go" approach. This gave Klarna the opportunity to manage the entire checkout process instead of being "just" one of the payment options. The product immediately achieved a high level of acceptance among consumers as well as retailers. After just one year, the number of users rose to 10 million. In 2013, after only eight years since its inception, the BNPL provider achieved a \$1bn valuation and \$200m in revenue, making it an unicorn.

2014 was a difficult year for the company, as they had to deal with a large number of invoices not being paid on time as well as complaints. But despite these difficulties, Klarna decided to launch its solutions in the US, while being valued at more than \$2bn. Starting with 10 American merchants, including Overstock.com, the company conquered 18 geographic markets and by the end of the year served more than 50,000 merchants with about 1,000 employees globally. Shortly after announcing its entry into the US market, one of the co-founders, Niklas Adalberth, stepped down from his position as deputy managing director but remained in his position as director of the board. His decision meant that CEO Sebastian Siemiatkowski would remain the only one of Klarna's original founders. Former CFO and co-founder Victor Jacobsson left Klarna in 2012. In 2016, the company launched its successful "Smooth" marketing campaign to illustrate how frictionless payments can be for consumers and online merchants using the platform. The "smooth" concept included the three ways consumers can shop with Klarna: "Pay now" - pay directly at the checkout, "pay later" - pay after 14 days and "slice it" - split the payments for the purchase over time. The successful marketing efforts were accompanied by Klarna's transformation into a bank. In 2017, the company received a full Swedish banking license, which it had applied for in 2015. The license gave Klarna the ability to launch an open-banking platform that provided access to more than 5,000 European banks in 16 countries (Lunden, 2017).

After that, in 2019, Klarna raised \$460m. This round lifted the company's valuation to \$5.5bn,

making Klarna the highest-valued private fintech company in Europe and the sixth largest in the world. At the same time, Klarna announced its first year of losses. The fintech company posted a net loss of \$92.8m. This was a clear sign of a turning point in Klarna's strategy, which had become focused on growing and entering new markets by any means necessary, accumulating more and more external capital while showing steadily increasing negative cash flow. Symbolic of this development, Klarna raised a \$650m funding round at a valuation of \$10.65bn in September 2020 to tackle its increasing cash burn. It was led by global technology investment firm Silver Lake (Dillet, 2020).

At the time, investors saw Klarna as undervalued. Hans Otterling, a partner at Northzone, told the Swedish press that this was a bargain compared to fintechs like Paypal or AfterPay because Klarna was growing so fast. "I would say this is a low valuation of the company," he said (Skjelsbæk, 2020). At the time, there was already speculation about Klarna going public within a year or two. In March 2021, Klarna's valuation tripled to \$31bn. In 2020, sales increased by 40% to \$1bn. This Covid-driven growth was enough to convince several new and existing investors to put \$1bn into the company in March 2021 (Drozdiak, 2021). However, it is worth noting that despite the revenue increases in 2020, Klarna's net losses increased by 50% to around \$109m that year due to high expansion costs. Only three months later, the company received fresh capital of \$639m again while the valuation increased exorbitantly to \$45.6 bn (Azevedo, 2021).

But this boom did not last long. Initially, through the onset of the Covid pandemic, Klarna's products gained significant popularity and continued to drive its growth. Overall, many tech companies such as Netflix, Zoom, or Peloton experienced a brilliant upswing during the pandemic, fueled by stimulus programs and higher demand due to the lockdowns. However, in 2022, the market environment changed significantly, especially for the tech sector. Since the beginning of the year in 2022, stock markets have sold off sharply, inflation levels increased

sharply and consumer spending slowed. With a fear of recession, Klarna was to switch its focus from growth to short-term profitability, according to the fintech's CEO Sebastian Siemiatkowski: "We decided that we're going to change the weight of our investments and focus more on short-term profitability over long-term new, potential investments" (Pymnts, 2022). As a result, Klarna was forced to start reducing costs. As a first step Siemiatkowski announced in May 2022 that the fintech would lay off about 700 employees, or 10% of its workforce. Despite these circumstances, Siemiatkowski told employees that "Klarna continues to hold a strong position in the market" and says he's still "relentlessly optimistic about Klarna's future" (Roth, 2022).

### **3. BNPL Industry**

Despite its growing popularity and newfound adhesion, the buy-now-pay-later method has been around since the 19th century. This short-term financing method grew from the installment plan system, where merchants made their expensive products such as furniture, pianos, and farm equipment, more accessible to consumers. In the US, after the Second World War, several retailers such as Sears and Macy's provided individual store accounts and, later, retail store credit cards, where debt was written off monthly (King, 2020).

The first store card to reach a large crowd was the famous Diners Club card, created in 1950 by Frank McNamara after going out for dinner and noticing he had left his wallet at home. Considered the birth story of modern credit cards, it set up the borrowing system we are familiar with today. At the time, restaurants would bill the patrons' meals to Diners Club, which in turn would pay the restaurant, taking a small commission on the transaction, and required cardholders to pay their debt each month. Later in 1958, the previous freight transport company American Express started to provide charge cards, replacing the need of carrying large sums of money, charging customers a monthly fee for this safer service, and taking a percentage of the amount charged from merchants.

However, the digitalization of finance brought up innovation to this space. Now, BNPL is not restricted to expensive items and equipment as it gives customers the choice to defer payment of cheaper items and larger shopping carts through point of sale (POS) installment loans. Adding to the debt aversion experienced by millennials and younger generations, the increase in purchasing power and the control felt by nearly instant credit approvals, faster payment schedules, and interest-free credit alternatives made BNPL plans' popularity skyrocket (see Exhibit 3). On the retailers' side, BNPL translates into decreasing shopping cart abandonment and increase in sales volume and recurring clients (Tijssen & Garner, 2021). In sum, it provides a simple payment solution that can be easily installed by merchants and has a great usability for the customers. Since Klarna is paying the retailers directly, they do not have to worry about missing payments or fraud and have at the same time the possibility of offering payment plans (see Exhibit 4). As such, Klarna had seen its user base grow from 86 million to 147 million in 2021, as opposed to its competitors Afterpay and Affirm that, as of June 2021, had 16 million and 7 million active users respectively, with 250.000 merchants accepting Klarna as a payment option, on a market that was forecasted to grow at a 45% rate until it reaches \$3.86t in 2030. High the highest adoption rate amongst its peers (Business of Apps, 2022), Klarna was well underway to become a market leader.

But how do Klarna and its competitors make money? Revenue relies on both key actors: merchants and consumers. From the sellers' side, BNPL firms receive either a small percentage of each purchase amount or they charge a flat fee for each transaction. Despite merchants being asked to give up some of their profit, there is evidence that the lower commitment and easier checkout process for customers lead to higher conversions. Most BNPL players do have apps or some sort of network with partner merchants. To be part of such a network is highly valuable for retailers since the BNPL companies generate leads. When looking closer, these generated leads are of high quality. New potential customers which already have Klarna or other BNPL

applications installed and are keen to spend some money are redirected from these providers to the merchants. Most likely it is easier to generate revenue with such leads than with others. The monetization from the consumers' side comes from the default of payment. Nevertheless, the clear benefit for buyers is the access to credit at a low price and therefore an outstanding alternative to conventional credit cards. Also, the outstanding amount of money only must be paid when the articles arrive, and the buyer wants to keep them. This is eliminating insecurities and comes in extremely handy when shopping for clothes, for example.

But Klarna, and other big BNPL firms for that matter, hadn't been profitable since 2018. Despite valuation multiples on pure BNPL players going as high as 58 times, as opposed to 4 times for traditional lenders, these business models are very hard to monetize. The extremely competitive and saturated market, fostered by low asset intensity requisites and soft regulations, puts pressure on players to keep up with one another and capture as many users as possible. To make matters worse, fee-based revenue models translate into very low margins for firms despite their high sales volume, making them extremely sensitive to funding costs.

Then how can these valuations be explained? Even though BNPL doesn't seem like a profitable business model, it is incredibly attractive to users, turning pure-BNPL firms into customer acquisition accelerators. Companies such as PayPal and Square can sustain themselves through their other products on the fintech space but use the opportunity that POS is to increase user growth. This means that, for investors, BNPL companies are made of "exit through acquisition" material.

#### **4. Klarna's Business Model**

As described above, BNPL companies are making money through customer fees and merchant commissions. Klarna is hereby offering various options to its customers. The shoppers can usually choose to either repay Klarna in up to 30 days or spread the costs of the purchase into three equal installments in the UK and Europe, and four installments in the USA. These

possibilities are free of charge for the customer if the debt is paid back on time. Merchants, however, do have to pay a commission in form of a flat fee, which is usually around \$0,30, depending on the country, and a percentage of the purchase's value ranging from 3.3-6%.

For bigger acquisitions, such as expensive electronics or furniture, there are financing plans available for up to 36 months. This option requires the buyer to pay an interest fee of up to 18.99% as well as the merchant to pay a commission of 3.5%. Although Klarna is famous for its BNPL payment model, it is interesting to see, that 50% of their volume is pay now, which is free of charge for the customer and only the retailer must pay a commission here. (Klarna, 2021) It is also important to mention that Klarna cannot keep all commissions. Usually, with every transaction, Klarna pays 1.5-3% processing fees to credit card or payment processing companies, such as Visa, Mastercard, or Stripe (see Exhibit 5) (Sacra, 2022).

Retailers who want to use Klarna must register and add the respective option to their checkout panel in their online shop. If customers want to use the service, they do have to create an account online or in the Klarna app. Throughout the onboarding process of customers, Klarna conducts an initial credit card check to ultimately enable them to make purchases. When making a purchase through Klarna, another soft credit check, which usually does not take longer than a few seconds, is carried out to ensure that the customer is authorized for credit. This is important, because when a shopper is buying something via Klarna's BNPL services, the merchant is receiving its money right away. This means, that all credit default risks from the buyers are transferred to Klarna which might result in significantly risky situations if credit checks are conducted imprecisely.

It is important to mention, that Klarna's business model does not only work with e-commerce merchants but is also available for many brick-and-mortar stores of larger retail companies. Whenever a merchant is making revenue through the Klarna platform, a flat fee and an additional commission of the amount paid must be carried out by the seller. When the payment

went through, customers receive payment instructions from Klarna plus an invoice. Klarna customers can also use Klarna services in physical stores that are not official partners of the network with the Klarna card. This card is available in a physical or virtual version.

Another important thing to mention is the Klarna app. With the app, Klarna is providing an all-in-one solution for customers, where the whole shopping experience, from the initial idea, over getting inspired, comparing products, to the final payment is all done via the app. Also, new features are constantly introduced, such as a coupon and loyalty system, or functions that support virtual shopping. This app has the potential to turn first time users into loyal customers, which is desirable. The initial credit check does not need to be conducted anymore and usually, for existing customers there are less marketing efforts needed to make them buy items. Also, the app is a cheap and effective way to place promotions for customers. All in all, customer acquisition costs can get decreased significantly with the help of the app. Another great benefit of loyal customers is that the credit default risk is typically considerably lower than with new ones.

#### **4.1 Value Proposition**

Klarna is making the life of shoppers easier on the one hand, and on the other hand helping merchants by increasing conversion rates and average basket sizes. However, these benefits are not Klarna-specific and are described further up in the document. Since Klarna can be considered the first mover of BNPL providers, customers benefit extremely from the network effect. In the 2021 financial report, it is stated, that Klarna is partnering with more than 400k global retail partners. For customers of the company, this is extremely convenient. On top of that, Klarna achieved to have the world's largest open banking network with 15,000 connected banks, spread over 26 markets (Klarna, 2022).

#### **4.2 Revenue streams**

Klarna's core business revenue-creating activities can be divided into the following: Firstly,

Klarna charges interest fees for customers who are making larger purchases with financing options up to 36 months. Hereby, the annual percentage rate (APR) can be as high as 18,9% depending on the credit score of the customer (Klarna, 2022).

Another revenue stream is late fees: These apply when a customer fails one of their payments. The late fees differ between missed one-time payments or late months when paying in installments (see Exhibit 6). Next to the different kinds of fees, Klarna is also gaining revenue through commissions. These must be paid by the merchant and depend on the payment option the shopper is choosing. The commissions always consist of a flat fee which is usually around \$0.30, depending on the country, as well as a percentage in the range of 3%-6% of the transaction amount. The final stream of revenue is the Klarna card which works like a credit card and can be used to pay in physical stores. Main source of revenue here are late fees from nonpaying shoppers. According to Klarna's financial statement (2021), the biggest driver of revenue is retailer income. In 2020, as well as 2021, this position did account for more than 50% of sales. Consumer income generated around 45% of revenue in the respective years. Klarna stated in its 2021 financial report, that commission income did increase 42% YoY, caused by an expanding network of retail partners and consumer adaption. Interest income also grew significantly by 24% YoY. However, not at such an immense pace as revenues through commissions because there has been a higher demand for Klarna's interest-free products on the customers' side (Klarna, 2021). Until 2017 Klarna's sales were highest in its home country market Sweden. From 2018 onwards though, Germany is the market where Klarna is earning most of its revenues (Klarna, 2020). In 2021, \$80bn has been achieved in gross merchandise volume which resulted in \$1.6bn total net operating income. It is impressive to see that the year-over-year growth was 42% and 38% for the respective. Revenues kept growing at such a pace since Klarna continued to launch new products and enter new markets. Generally, when looking at the graph of total operating income since 2014, it can be observed that there is

exponential growth with a CAGR of 32% from 2014 to 2021 (see Exhibit 7) (Klarna, 2021).

### **4.3 Cost structure**

#### **4.3.1 Operating costs**

Total expenses before credit losses increased from 2014 to 2016 in a relatively stable manner, with around 30% year over year. 2016 to 2017 Klarna managed to save costs compared to revenues which resulted in only a 16% growth in operating expenses. The years from 2017 to 2020 were characterized by more than 40% growth YoY in operating costs before credit losses and from 2020 to 2021, costs skyrocketed by 73%. All in all, there is evidence that there is a clear tendency for an increase in the change of operating costs YoY (see Exhibit 8). When looking at the graph of operating expenses in absolute numbers, a slight exponential growth can be observed (see Exhibit 9). General and administrative expenses were the greatest cost factor throughout the years. 2018 the respective costs reached 80% of sales and increased steadily until 2021 when solely this position did outweigh the net operating income. Klarna is justifying these numbers with the further very ambitious market and product expansion. Therefore, average full-time equivalents (FTE) were 4789 throughout 2021 for the Klarna Group as the company scaled to provide its service all around the globe. Looking at the financials, however, one can see that spending on salaries decreased in percentage, relative to the total general and administrative expenses. Nevertheless, with in between 20% and 30% throughout the past years, this position has been a considerable cost factor for Klarna (Klarna, 2021).

Another significant element of expenses in the past have been marketing effort. The company did spend a big amount of money on the “Smooth” campaign in 2016 (see Exhibit 10). In that year, these clips were all over the internet and created an international buzz around the brand. Since then, a rather aggressive growth strategy was aimed, and consequently, marketing spending had to be increased year after year. Two other examples are the 2019 campaign with

well-known music artists Snoop Dogg and the 2021 campaign with A\$AP Rocky (see Exhibit 11) (Klarna, 2022).

Moreover, there is spending on the development of products. Especially as a tech company, it is important to develop and reinvent products constantly further. One example is the launch of the Klarna app in 2017. From planning over development to rollout, such processes are costly and take time. Another substantial component of expenses is the technology behind Klarna. To support products like apps, browser add-ons, and the whole payment structure in general, the company needs to maintain an expensive IT infrastructure.

#### 4.3.2 Credit losses

When breaking down Klarna's business model and the risk associated with it, one considerable part of it is providing credit. Therefore, it is crucial to keep an eye on credit losses. When analyzing this position, it is conspicuous that credit losses showed very volatile annual change rates over the years (see Exhibit 12). The total numbers, however, did show tendencies of exponential growth in credit losses. Total sales exhibited the same behavior. Increasing sales caused increasing credit losses. When looking closely, however, one can see that credit losses grew at a more significant rate than sales. Between 2015 and 2021, operating revenues grew with a compounded annual growth rate of 32%, whereas credit losses showed an increase of 55% compounded annual growth rate (see Exhibit 13 and Exhibit 14).

However, it is more interesting to compare the growth of GMV with the increase in credit losses. Between 2018 and 2021, the figures increased by 40% and an incredible 81% CAGR respectively. Credit losses grew steadily in relation to sales from 13% in 2015 to 34% in 2021. When comparing credit losses as a percentage to GMV, the same tendency is observable with 0.3% in 2018 and 0.7% in 2021 (Klarna, 2021).

Although Klarna's credit losses of 0.7% of GMV in 2021 might seem high, but when putting things into perspective by analyzing competitors, this number does not seem that bad anymore.

Credit losses of Affirm, Afterpay and Zip are 1.65%, 1.06% and 1.22% of GMV respectively (see Exhibit 15).

## **5. Klarna's growth strategies**

### **5.1 M&A**

The transformation from a small Swedish startup to the leading BNPL provider, which now offers a comprehensive range of digital payment, banking, and shopping services, required some time. Corporate acquisitions have been an important strategic tool for the technology company's tremendous growth. Exhibit 16 and Exhibit 17 provide an overview of selected M&A deals and the new segments Klarna has entered as a result.

In 2011, Klarna made its first transaction with the acquisition of Analyzd, an Israeli risk and fraud management company (Butcher, 2011). Klarna entered the open banking space for the first time when it acquired SOFORT, a leading payment service provider for €150m in 2014. This enabled Klarna's customers to pay instantly in one step without installments using the "Pay Now" feature (Klarna, n.d.). At the same time, the transaction paved the way for the strong growth the fintech experienced with its open banking business, which has been transferred into a separate business unit called Kosma since March 2022 (Williams, 2022). Among other things, the acquisition of the startup SOFORT enabled Klarna to serve 14 European countries and work with more than 43,000 merchants (Penn, 2013). Today, Klarna has more than 450,000 merchant partners, covering 150 million active users and two million transactions per day. In 2016, Klarna acquired the technological assets and employees of Cookies Labs, a German-based financial technology company that offers person-to-person money transfers (Samavati, 2016). In 2017, Klarna acquired German payments company BillPay, gaining access to over 5,000 merchant partners to strengthen Klarna's payments presence in Germany and across Europe (Klarna, 2017). In 2018, Klarna acquired ShopCo, a German developer of browser extensions that can turn websites into connected online shops, by buying only the intellectual

property and eight ShopCo employees (Ecommerce News, 2018). In 2018, Klarna bought Close Brothers Retail Finance from UK merchant banking group Close Brothers Group with the aim of significantly strengthening its position in the UK retail finance market (Klarna, 2018). In 2020, Klarna acquired a total of six companies, sending a clear signal to further prioritize its inorganic growth. These include US-based retail marketing company Spring Marketplace, Italian BNPL startup Moneymour, UK online shopping portal Nuji, post-purchase experience startup Woilà, including its intellectual property and team, and Swedish startup search Engine Marketing, which operated two services, Semtail and Shoptail, that enable sellers to advertise more effectively on Google. With seven acquisitions in 2021, Klarna even managed to break its acquisition record from 2020. In the first quarter of 2021 Klarna acquired San Francisco-based Toplooks.ai, which provides AI-driven content creation tools that offer retailers personalization features and virtually unlimited shoppable content. To further enhance the e-commerce business for its retailers, Klarna acquired UK-based Hero in July 2021, a virtual social shopping platform that provides live-streaming solutions for online retailers and store associates to assist and convert online shoppers. In the same month, startup APPRL Fashion joined the FinTech giant. Their SaaS platform allows content creators and retailers to easily collaborate to create engaging and informative shoppable content. Alongside retailers, Klarna is also striving to continuously improve the consumer experience and attract new customers. For a sum of €110m, Klarna acquired Stocard, a leading mobile wallet provider, and its customer base of more than 3.5 million users. Klarna also added the online travel planner Inspirock, which, according to Siemiatkowski, " makes the entire journey from inspiration to planning to prepare a trip easier, less stressful, and more fun for customers, while Klarna's merchant partners can better reach and engage with their audience by offering personalized content. This is a natural extension of the benefits Klarna brings to payments and shopping" (Klarna, 2021). Since the acquisition of the startup Piggy, consumers are able to use

a browser extension to get discount offers displayed while browsing a website and make purchases with Klarna's payment options in any online shop, even if the merchant is not yet a Klarna partner (Schlenk, 2021). In addition, Klarna bought the Swedish price comparison platform PriceRunner for around \$1bn, with the aim of developing the Klarna app as the main point of contact for consumers. Overall, the recent acquisitions can be interpreted as part of Klarna's strategy to evolve beyond its origins as a buy-now-pay-later (BNPL) company into a one-stop shop for the entire customer shopping experience and to become a so-called super app. Chief Product Officer David Fock let on in this context that this would put Klarna in a position to take on the big tech companies: "Klarna will not be a marketplace, but a viable and competitive alternative for retail partners against Amazon, Google, and Facebook," he said (Competition Policy International, 2022). Industry experts confirm that Klarna's growth strategy, with the help of a wider product range for the benefit of retailers and consumers, is necessary to offer customers a comprehensive and unique shopping and banking experience and thus establish itself as an established player in the market (Johansson, 2021).

## **5.2 Geographical expansion and product development**

Together with corporate M&A activities, the expansion of services and operations into new geographical markets has also been of tremendous importance to the growth strategy of Klarna (see Exhibit 18). Obviously, Klarna started to provide its services initially in Sweden. However, the company started to reach new markets rapidly. Between 2006 and 2008, Klarna launched in Finland, Norway, and Denmark. These markets were still managed from the headquarter in Stockholm, Sweden. Already in 2010 though, Germany and the Netherlands were integrated. The firm decided to not only provide its services in the respective areas but also be present there for operational activities and therefore opened offices in Nuremberg, Germany, and Amsterdam, Netherlands. In 2011, Klarna entered another market through the acquisition of Israeli-based risk management company Analyzd which turned into an office of the Klarna

Group in Tel Aviv. However, until today, it is not possible to use Klarna's services in Israel. The next market entered was Austria in 2012. At the same time, the new product Klarna Checkout was launched. A payment solution that enabled management of the whole checkout process instead of being only one of the payment options available. This service was not introduced to all markets at the same time and had to be rolled out step by step. Consequently, in 2013 the Klarna Checkout reached Norway and Finland. In the same year, Klarna achieved to have more than 10 million customers within the seven active markets so far.

Klarna continued to grow at an immense rate, expanded in 2014 to the UK, and opened an office in London. One year later, in 2015, the corporation made its first attempts to enter the American market by opening offices in Columbus, Ohio, and New York City. According to the Klarna website, opening the offices in the USA was meant to test the market first instead of launching products right away with full commitment.

The Klarna app finally launched in 2017. Customers can now get the whole shopping experience from getting inspired all the way to making the payment in one app. In 2018, the pay in 4 installments product was launched in the USA whereas, in the UK, the product is called "pay in 3", with only three installments to be paid. Both markets started to gain traction that year. Another important product launch in 2018 was the Klarna card in Sweden. The great effort of product launches and massive growth in two such big markets could also be observed in the income statement. SGAs increased by almost 50% from 2017 to 2018.

After successfully launching the Klarna card in Sweden, Germany was the next country where this product was introduced in 2019. Also, within the US market the product portfolio was expanded with the launch of the Klarna app. 2020 marked another milestone in terms of growth to new geographic markets. Klarna launched its services in Australia, Belgium, Spain, and Italy. Moreover, Klarna did reach 11 million customers in the USA plus 2 million monthly active users of the app. In the following year, US customers were almost doubled to 20 million

and Klarna introduced real bank accounts for its German customers and launched the Klarna browser extension. 2021 saw once again immense growth in terms of geographic expansion. Shoppers in New Zealand, France, Poland, Ireland, Portugal, and Switzerland were able now to benefit from Klarna's services.

Nowadays, Klarna is active in over 20 markets across 3 continents. There are Klarna offices in 28 different cities including Zurich, Berlin, Paris, Toronto, and Shanghai. The last two cities might be indicators for future expansions.

In terms of product development, Klarna has launched the Klarna Checkout, which entails the different individual payment options the firm is providing, the Klarna app, the physical card for in-store payments, and even real bank accounts for certain markets.

Nowadays, around 35% of all e-commerce stores using Klarna are from Germany, which are well over 40.000. The United States and UK both have somewhat between 17.000 and 18.000 active stores which do rely on the services of Klarna. Both countries account for approximately 15% of stores that are using Klarna, whereby the United States has a slight edge here. The country, ranking on place four in terms of stores using Klarna is Sweden with 9% followed by Austria with circa 5% (see Exhibit 19) (Store Leads, 2022).

Especially when looking back on Klarna's various product launches since Sebastian Siemiatkowski and his friend founded the company in 2005, it becomes clear that Klarna is not only a BNPL company anymore. The firm is offering a holistic product, including payment card functions, bank accounts, shopping features such as loyalty programs, delivery tracking, and discounts (Klarna, 2022).

## **6. Klarna's efficiency strategies**

Over the course of its years of operations, Klarna has seen consistent growth, driven by consumers moving away from credit card payments towards BNPL solutions, large external capital injections to fund Klarna's aggressive expansion strategy, and, more recently, the Covid

pandemic, which has accelerated merchant adoption and repeat consumer usage. These favorable market conditions have enabled Klarna to compete in the market without demonstrably implementing efficiency measures and cost savings to sustainably improve the company's profitability situation, in addition to growing into a leading BNPL provider. However, it shows that the fintech may well be forced to change its course as soon as external factors develop in the opposite direction. Klarna's profitability declined in 2021 and 2022, thus pushing the company to shift its focus from expansion to profits. The profits, which Klarna reports as net result, amounted to minus \$826m when compared to the average SEK/USD exchange rate for the entire year 2021 (Best, 2022). This trend became more pronounced in the fourth quarter of 2021 and the first quarter of 2022 when economic uncertainty and the war in Ukraine led to a shift in consumer sentiment. Additionally, net losses in the first quarter of 2022 nearly tripled compared to 2021 to minus \$275.35m. In addition, due to more cautious investor sentiment and volatile stock markets, Klarna as a result had to take initial steps to make its organizational structure more efficient. "We've had a few years now where growth has been really heavily prioritized by investors," Siemiatkowski said. "Now, understandably, they want to see profitability" (The Financial Revolutionist, 2022). To reduce employee expenses, Siemiatkowski announced in May 2022 the decision to lay off about 10% of its global workforce to focus again on the core business and short-term profitability.

## **7. Competition among BNPL players**

Klarna is facing increasing competition from "buy now, pay later" providers, which mainly target the US market to benefit from the consumer shift from credit cards to BNPL services. One of them is Affirm. Founded in 2012 by one of the co-founders of Paypal, Affirm initially operated its BNPL lending service only in the US before entering in Canada by acquiring BNPL competitor PayBright in December 2020. Affirm offers "buy now, pay later" installment loan products for almost any transaction size and for terms from 6-48 months. The fintech contracts

directly with merchants who offer the Affirm platform as a payment option. The merchants pay Affirm fees based on a percentage of the total order value, which vary depending on the interest rate offered. Merchant fees are typically 3-5%. Apart from their BNPL solution, Affirm offers various products ranging from installment pay, virtual cards, split pay, consumer marketplace app and savings accounts. After only 8 years of operation, Affirm was listed on the NASDAQ stock exchange in January 2021. In 2021, Affirm reported \$15.5bn worth of completed transactions. The company's activities had garnered \$1.35m in revenues in 2022 growing at a compound annual growth rate of 81% from 2019 to 2022. In addition, Affirm has raised more than \$1.5bn in funding. Overall, Affirm has access to more than 234,000 partner merchants and 14 million active users, coming mostly from the US.

Splitit, another direct competitor of Klarna which was founded in 2012 and went public in 2009 is based in New York. The company's approach to the BNPL space is unique as it allows consumers to leverage their existing credit. By using their own credit or debit cards with the installment program, customers see installments on their bills, effectively balancing the cash flows. The ability to split payments into smaller chunks without incurring additional interest, applications, or fees, while building credit, makes Splitit an attractive option for consumers as well as a safe option for merchants. Core operating markets include the US, Canada, and Australia. While many BNPL services focus on business-to-consumer (B2C) transactions, Splitit targets a business-to-business (B2B) context and tailors its functions to the needs of suppliers and companies. With Splitit, customers can split the bills in 3-24 installments, while merchants are charged a fee of around 1.5% per transaction. In 2021, Splitit reported a \$395m GMV, with revenues reaching nearly \$11m growing more than 150% from 2019-2021. In addition, the company recorded more than 400,000 active shoppers who transacted with over 1,500 merchants at an average order value of \$1,000.

Afterpay is a BNPL company based in Australia. It serves international markets including the

US, UK, Canada and New Zealand. In 2017, Afterpay merged with Touchgroup, an Australian fintech before it went public at a \$500m IPO in Australia. After the company's success in 2018, Afterpay acquired 90% of the shares of Clearpay, a competitor in the UK. Within two weeks, the platform gained over 200,000 users and strengthened Afterpay's presence in the UK. Afterpay was acquired by the US fintech Block for \$29bn in August 2021. Like Klarna, Afterpay does not impose a specific credit score that is required for a loan. However, unlike Klarna, Afterpay does not check the creditworthiness of its customers, which implies a more favorable procedure. In addition, Afterpay does not report credit delinquency to the authorities, so the use of the platform should not affect a customer's credit history. Afterpay received funding worth around \$375m and over \$833m in revenue and carried out nearly \$20bn in transactions, mainly from BNPL and cash services. As of 2021, Afterpay reportedly has 16.2 million users and 98,200 merchant partners across 40 countries worldwide.

PayPal is a well-known fintech giant from the US and was founded in 1998. The company has raised a relatively small amount of \$216m before it had its IPO in 2002. Although more popular as an international digital wallet, PayPal has also introduced its own BNPL, known as PayPal's 'pay in 4' in 2020 and 'pay monthly' in 2022. As the name implies, PayPal BNPL works by allowing customers to make purchases at the point of sale through credit, which is then paid in four installments, or in the case of "pay monthly", it can be split into 6 to 24 installments. The term depends on the customer's preferences and can range from 6 weeks to 2 years. PayPal does not charge additional fees for late payments to customers, nor does it charge additional fees on top of the existing fees of around 3% for its existing merchant network. Although PayPal does not disclose earnings and other figures in each business segment it operates, it was reported that around 70% of PayPal's customers also used the platform's BNPL installment feature in 2021. During the same period, PayPal BNPL generated over \$3.6bn worth of transaction volume. The platform's "buy now, pay later" feature is only available in the US,

UK, Germany, France, Italy, Spain, and Australia. As of 2021, PayPal has 35 million global partners and already 250,000 merchants using the BNPL feature on their website.

Zip can also be considered one of the leading companies in the BNPL space. Founded in 2013 and headquartered in Australia, the company offers payment options for retail giants such as Apple, Amazon, and Walmart. With categories covering everything from education and pets to shoes and travel, Zip is available on a variety of platforms as well as in physical retail shops, offering customers interest-free payment options. After three years of operations, the company was listed on the Australian Securities Exchange and raised more than \$5m in 2016. In 2018, the company launched its marketplace app on the Apple Store and Google Play Store, where Zip recorded more than one million downloads on each platform. As of early 2022, Zip is one of BNPL's top 5 apps in terms of downloads and ratings, along with Klarna, Afterpay and Affirm. In 2020, Zip acquired QuadPay, a US-based fintech company operating in the same industry. This increased the combined value of the two companies to \$1bn and helped Zip enter the US market. Zip not only offers zero interest rates but is also not as strict about credit checks. People of legal age who have an approved debit or credit card can get their loans approved quickly on the platform. Zip splits the customer's bill into four installments, which are paid within six weeks. Depending on the customer's preference, repayments can be made weekly or monthly. The Australian fintech charges merchants a fee of about 2-4% per transaction. As of June 2022, Zip has an estimated worth of \$1.93bn. In addition, their revenue has peaked at more than AU\$397m, while the reported volume of transactions was worth about AU\$5.8bn. Zip recorded 7.3 million users in 2021, with markets in Australia, the US, Canada, the Czech Republic, Mexico, India, the Philippines, New Zealand, Poland, Saudi Arabia, UAE, South Africa, and the UK.

The first half of 2021 had been particularly favorable for BNPL valuations as market capitalizations reach a historical high with Afterpay achieving a market cap of \$35.13bn in

February, with operational KPIs of \$924.7m in revenue, 16.2m users, and 98.2k merchants worldwide. As of November 2021, Affirm broke the record with a \$45.61bn market cap and, by the end of the year, finished ahead of the market leader with a market capitalization of \$28.26bn within their first trading year. With a revenue of \$870m but only 7.1m active users and 29k merchants, this achievement was short-lived as stock value plummeted and Afterpay was the clear number one by April 2022 with a \$14.77bn valuation. While Afterpay and Affirm fought for the top, ZipPay's public valuation stayed in the top 3 all along, ending 2021 on a \$2.55m market cap. By that time, ZipPay had 7.3m users and was making over \$390m in revenue. Overall, both users and merchants clearly preferred Afterpay out of these three.

Klarna, on the other hand, maintaining its private valuation of \$45.6bn, was catering to 147m active users and had plans with 400k merchants, four times more than Afterpay, and had made \$1.42bn in revenue the past year. As such, Klarna was favored by users and merchants over its public counterpart and industry giant Afterpay. While both would set up four installments of 25% of the total purchasing price, starting at shipping, Afterpay's late fees were tighter than Klarna's \$7, as they charged at the minimum between \$68 or least \$10 and up to 25% of the loan's value. Additionally, Klarna would let you set up single-use cards to finance your purchases even if a retailer didn't have an agreement with them and you could opt for longer repayment terms that were subject to interest.

To determine the health of an e-commerce business it is important to look at parameters such as the gross merchandise value (GMV) as it accounts for the total value of merchandise sold and fees charged over a period. As such, it is also a key metric for BNPL firms as they facilitate e-commerce, without ever owning any merchandise, and since it portrays the total monetary value of sales. With a GMV of \$80bn in comparison with Afterpay's \$21bn, Klarna is the one that manages most purchases made through this method. Exhibit 15 provides an overview of the competitive landscape around BNPL.

## **8. Macro environment impacting the VC market**

Whilst not quite as exposed to macroeconomic trends as other institutions such as banks, the contraction of economies makes VC funds susceptible to market risk, therefore impacting the funding market and its players.

Traditional VCs manage funds raised from their Limited Partners (LPs), that can range from wealthy private investors to banks, insurance companies or pension funds, and invest in startups that they consider to be opportunities with potential for high growth and favorable exits. These types of investments are also considered high risk and have a long-time horizon. Nevertheless, VC funding is held as an accelerator for innovation, especially with the rise of new emerging industries based in high-tech. Kortum and Lerner (2000) measured that during periods of high VC activity there was a significant rise in patent pursue and that it was responsible for about 10% of US industrial innovations.

When the first symptoms of financial crisis start to hit the most exposed institutions such as banks and insurance companies, VC funds get caught up on the down turns. Raising investment funds gets more and more difficult as the traditional LPs shy away from such risky activities. Additionally, with stock markets following economies' growth, exits through Initial Public Offerings (IPOs) become unattractive for investors and no longer pose as viable and profitable options. When comparing the charts of the Nasdaq and S&P500 indexes it becomes evident, that especially stock prices of tech companies decreased strongly, in comparison to more traditional stocks (see Exhibit 20) (Euromonitor International, 2022). While BNPL companies received strongly increasing valuations from spring 2020 onwards, the situation changed promptly in late 2021 as the stock prices of respective companies started to tumble (see Exhibit 21). Strong decreases in the stock markets can usually be interpreted as a sign of fear among investors. Often, when the public markets experience negative growth previously, the private markets follow with slight delay.

Also, recessions led to the decrease in consumer spending which heavily impacts the ventures in the portfolios and the VCs' ability to generate profit. However, historically there has never been an absolute halt in VC funding during these times. What is seen is an increase in due diligence from VCs and a bigger proportion in financing of early stage and seed rounds as these are the moments to invest in great opportunities at a discount, since banks shy away from this early of a venture which usually don't have hard assets to secure their loans on. Later-stage companies, on the other hand, receive about 20% less funds during crisis than they would the period before according to Block and Sandner (2009).

As venture capitalists tighten their investment protocols and company valuations begin to decline, the market is likely to see an increase in down round financings. This occurs when a company raises additional funds at a lower valuation than in previous rounds. Down rounds usually have adverse consequences for previous investors, founders, and employees, such as dilution and impairment of their shares. But when companies need equity to keep operating in the face of an economic downturn, poor performance or increased competition, accepting a down round may be their only chance of survival.

Klarna has long been tipped as one of Europe's brightest IPO candidates, but recently it has been caught in a storm in capital markets sparked by rampant inflation, rising interest rates, and the Russo-Ukrainian war.

As such and as of now, with a war in Ukraine causing looming energy prices which are fueling inflation, investors are rather careful and appreciate money-saving measures to become profitable, as well as consumers who are trying to save up to compensate for the increase in prices of basic goods, such as food, electricity, and gasoline. For companies such as Klarna, this ultimately means less volume in merchandise, since the firm's business model profits mainly from shoppers spending money on electronics, apparel, or sports equipment.

Also, inflation is forcing central banks to increase their benchmark interest rates. Until May

2022, the US saw already five raises, a trend that is very likely to continue (Euromonitor International, 2022). Rising interest rates are poison for unprofitable companies since future earnings are worth less when higher interest must be paid on the debt in future years. It also means, that higher interests will decrease Klarna's margins.

On top of the negative sentiment among investors, the current economic situation, and the resulting actions from central banks, the still fairly new BNPL sector might experience huge regulatory developments in the near future (Euromonitor International, 2022). Depending on legislation it could mean that certain groups of consumers will not get access to credit so easily anymore and eventually shrink the total addressable market for BNPL products. Also, more requirements, such as additional credit checks will increase costs for lenders. It will be hard to pass on the respective to consumers without losing them.

One year after raising a \$639m round that valued the company at \$45.6bn, Klarna had the possibility to raise another massive round to manage its rapid growth and cash burn with the caveat that this would most certainly be a down-round. However, the company was burning cash at a considerable rate. Approximately 1bn SKE which equals circa \$120m each month. With that rate, Klarna would run out of funds in approximately six months (Klarna, 2022).

But what would a cut in valuation mean for Klarna, its investors, and its employees? First, a down-round would require Klarna to give out more shares which would heavily impact anyone without any kind of anti-dilution privileges. Typically, it is rather the investors holding such privileges, whereas the employees' stock options and founders' shares decrease in worth. This could lead to displeasure among employees and compromise future motivation and performance. Furthermore, with signaling being one of the most important factors in this ecosystem, it would generate negative feelings on the public and investors, as well as on employees.

Nevertheless, what the historical data has shown, is that down rounds do not necessarily doom

the companies for failure, as data from 2008 to 2014 shows that only 13% of US venture-backed companies that took down rounds during this period were unable to raise new rounds or exit immediately after, either through a buyout or a private equity acquisition (Mathur, 2022).

## **9. The road ahead**

Siemiatkowski has arrived at his desk meanwhile, taking the last bite of his sandwich and sipping on his orange juice, reflecting on the tough situation Klarna is facing: On the one hand, he and all Klarnauts can be extremely proud of what they achieved during the past 17 years. On the other hand, there are serious challenges ahead that are threatening Klarna's future success.

The current economic environment with rising interest rates and inflation is causing a market environment where investors are acting rather tentatively. Consequently, it will not be as easy as in 2021 to attract new VC investors in such a scope while still writing red numbers.

“Despite these extremely adverse conditions for funding”, thought Siemiatkowski to himself, “we cannot wait much longer for the next infusion of money to keep Klarna alive.” Time was running against Siemiatkowski. He was thinking about the past round of funding in Q1, 2021 when Klarna achieved a post-money valuation of \$45.6bn and became the highest-valued privately owned company in Europe. When approaching a new financing round in such an environment, it is certain that it must be agreed on a down round at a valuation lower than in the previous round.

The founder thought back about the beginnings of Klarna and how BNPL is well established in their home market in Sweden for more than a decade now. In other markets, such as the USA, there is probably still a lot of potential and since a considerable amount of consumers are not familiar with the benefits of BNPL in comparison to credit cards yet, this market appears to have significant potential. Demand for such services is probably still high, but with

increasing competition, it will be hard for all players to become profitable on the one hand, while on the other hand showing some considerable growth. Especially now, it would be important for Klarna to continue its aggressive growth strategy to outperform its competitors. His thoughts were wandering around different scenarios, the road ahead of Klarna and the whole BNPL industry. Has the BNPL industry already seen its saturation point? Is it possible that the party is already coming to an end?

## **INDIVIDUAL PART – GIUSEPPE VINCIGUERRA**

### **Case Synopsis**

In 2005 Sebastian Siemiatkowski, Niklas Adalberth, and Victor Jacobsson close friends and fellow students founded Klarna, a global payments and shopping service provider. The Swedish fintech has earned a reputation as the leading "buy now, pay later" (BNPL) service provider by offering credit to their clients throughout the checkout process. Klarna's success is heavily built on external capital raised from investors such as Sequoia Capital and SoftBank. After raising more than \$3bn and reaching a valuation of \$45.6bn in June 2021 the market environment changed completely. A set of circumstances such as high inflation, rising interest rates, mounting fears of a recession, and the aftereffects of the Covid pandemic caused a significant downdraft of tech stock prices with peers dropping 80-90% compared to peak valuations. When the case picks up in the end of June 2022, Siemiatkowski must decide what to do next. After laying off 10% of Klarna's workforce the company is still burning an extensive amount of cash which eventually lead to pre-tax losses that have tripled to \$250m in the first quarter of 2022 compared to last year. As Klarna is running out of cash the company is forced to raise an additional financing round amid the current market environment that complies with the change in investor sentiment. Time is running out as the CEO faces a tense meeting with his investors, where he has to provide an update on Klarna's strategic direction and be prepared to understand a fair valuation of Klarna given the turmoil in public markets.

### **Learning Objectives**

This case offers students a profound insight into a topic that is rarely discussed by neither entrepreneurs nor venture capitalists – a significant drop in valuation or in other words: a down-round, where the valuation of a company loses a substantial value compared to the previous funding round. Students are encouraged to critically think about possible reasons for such decreasing valuations of privately owned technology companies. Moreover, students can put

themselves in the shoes of venture capitalists and founders and examine which valuation methods are most suitable for a company like Klarna and if the firm might be potentially under or overvalued.

## **Target audience**

This case study and its related assignment questions are intended for undergraduate and postgraduate as well as MBA students who are pursuing a business-related study program and are focusing on entrepreneurial finance and venture capital.

## **Assignment Questions**

1. What methodology can be used to evaluate Klarna's enterprise value?
2. What will be a fair valuation given the current market conditions?

## **Teaching plan**

The case is taught in one day in any course related to "Entrepreneurial Finance and Venture Capital". Students are supposed to prepare this case study by reading the case and work on the assignment questions beforehand. Additionally to the information provided, students are invited to do own research on the internet, as this case aims at a more practical approach. The following questions are intended to stimulate discussion about valuation methodologies for scale-up companies and the prevailing market conditions that affect the valuation of private technology companies.

## **Analysis**

The analysis will first explore different valuation techniques that can be applied to determine the final methodology in order to eventually derive a fair valuation of Klarna's enterprise value reflecting the prevailing market conditions and investors' sentiment. Finally, a critical evaluation will recap the findings and provide a basis for further class discussion in which students will be asked to discuss their findings with the real down round that occurred at the

time this case took place. Exhibit 22 provides key information on the down round that has been publicly disclosed.

## **Valuation methods**

In general, there are three valuation approaches that can be applied to a venture capital backed tech-company like Klarna. The first, discounted cash flow (DCF) valuation, is used to relate the value of an asset to the present value of that asset's expected future cash flows. The second, relative valuation is based on multiples that estimate the value of a company by looking at the pricing of comparable publicly listed companies relative to a common variable such as earnings or sales. The third method, contingent claim valuation, uses option pricing models to determine the value of assets that have option features. Some of these assets could be financial assets such as warrants, and some of these options are not traded and could be based on real assets like projects or patents. The latter are often referred to as real options. Depending on which approach is used, the results can be very different (Damodaran, 2012). For this analysis option pricing models will be disregarded. While the contingent claim valuation method has interesting features, it is not feasible without detailed company information that allows us to identify the option. Adding to the valuation techniques mentioned above, in the specific case of young and fast growing companies that draw back on large amounts of external capital, those investors often value private companies using the so-called venture capital method. This involves forecasting the private company's earnings for a future year in which the company is expected to go public. These earnings are used in combination with an earnings multiple estimated from listed companies in the same industry to determine the value of the company at the time of the IPO, known as the exit or terminal value. This value is discounted back to the present at what venture capitalists call a target rate of return, which measures what venture capitalists believe is a justifiable return, given the risk that they are exposed to. This target rate of return is usually set at a much higher level than the conventional cost of equity for the firm

(Carver, 2011).

## **Selection of relevant valuation method**

First of all, it is necessary to apply the right valuation methodology that fits best the company's characteristics. Klarna is a fast growing, late-stage technology company that generates losses and negative cashflows due to its expansion investment needs to position itself as a market leader in the BNPL space. These characteristics might be typical for venture capital funded fintech companies, but complicate the application of traditional valuation approaches such as the DCF method. Firstly, as Klarna reported net operating losses in the first half of 2022 as well as for the last three years from 2019 to 2021, profit growth rates cannot be estimated and used in DCF valuation models. The problem is that it's no longer possible to estimate an expected growth rate to profits and apply it to current profits to forecast future profits. When current profits are negative, applying a growth rate will just make it more negative instead. An alternative approach to estimate earnings growth is to use information provided by the company in its annual reports or other filings on when the company expects to turn profitable. Due to its private nature, Klarna is only disclosing a minimum amount of information from where it is not possible to derive an earnings forecast over the next years. However, industry related data such as peer financials or market reports may be helpful to make appropriate estimates. Secondly, with negative income and cashflows, the tax calculation becomes more complex. The standard approach to tax estimation is to apply the marginal tax rate to the pre-tax operating profit to determine the after-tax operating profit. This calculation is made under the assumption that profits in the current period generate tax liabilities. While this is generally true, companies that make losses may carry those losses forward and offset them against profits in future periods. Therefore, valuing Klarna requires to keep in mind the net operating losses and remember to use them to shield future periods' income from taxes. Thirdly, the going concern assumption may not hold. The final problem with valuing companies with negative profits

under a DCF model is the very realistic chance that these companies will go bankrupt if profits remain negative. Therefore, the infinite life assumption underlying the terminal value estimate does not hold anymore in these cases. Adding to that, the majority of the value resulting from a DCF valuation will generally be in the terminal value and its magnitude of the terminal value is not only determined by its target margin but also by its growth assumptions. From 2018 to 2021 Klarna's sales grew at 36% on a compound annual growth rate. This not only underlines the high growth it currently achieves but also showcases how difficult it is to estimate the point of time when the DCF model can determine a steady growth rate that can be integrated into the terminal value.

Overall, it is not impossible to value Klarna using a traditional DCF model. However, what a DCF valuation approach can't capture is the current public market values, as it focusses to capture the intrinsic valuation it generates through its expected cashflows instead. Venture capital backed tech-companies such as Klarna are heavily tied to public markets and hence relative valuations. A relative valuation based on multiples is much more likely to reflect the current market sentiment, as it attempts to measure relative rather than intrinsic value. Therefore, in the underlying market at the time of this case, where the prices of all technology stocks are falling, the relative valuation is likely to result in lower values than the DCF method. To reflect the turmoil in the markets that caused technology stocks such as Meta (-50%), Netflix (-70%) or Affirm (-80%) losing a significant portion of their share price in the period from Q4 2021 to Q2 2022 (see Exhibit 23), valuing Klarna using multiples is the best approach to determine a fair valuation that prices in these market conditions. This is also in line with the venture capital method, which applies a relative valuation as mentioned earlier to make an investment decision.

### **Selection of multiples**

As a next steps it is important to decide on the right multiples, which can be used to compare

Klarna to public peers and to get a sense of the underlying valuation for the company. To compare companies, it is vital that all valuation multiples are scaled to a common measure, and conventional scaling measures include earnings, book value and sales. For Klarna, it makes most sense to look at sales multiples, as both earnings and book value multiples would create problems. First, unlike earnings and book value multiples, which would become negative for companies with negative earnings such as Klarna and therefore not meaningful, sales multiples are available even for troubled or young companies. Second, sales are relatively difficult to manipulate, unlike profit and book value, which are heavily influenced by accounting decisions about depreciation, inventories, research and development, acquisition accounting and extraordinary charges, among others. Third, sales multiples are not as volatile as earnings multiples and are therefore less affected by yearly fluctuations in company performance (Damodaran, 2012). There are two basic revenue multiples in use, which we could look at. The first one is the multiple of the market value of equity to the revenues of a firm also known as the price-to-sales ratio. The second, and more appropriate ratio for Klarna is the multiple of the value of the operating assets (enterprise value) to revenues or simply EV-to-sales ratio. For this analysis we exclude equity multiples, as we want to value the business and not only the equity of the firm. The price-to-sales ratio divides an equity value by revenues and would result in lower values for more highly levered firms, and consequently lead to misleading conclusions when price-to-sales ratios are compared across firms with different degrees of equity and debt proportions in their capital structure (Damodaran, 2009). As a last step to determine all factors of the multiples used, it is important to use updated information. For firms with negative earnings and high growth in revenues, the numbers tend to change significantly from period to period. Consequently, it makes more sense to look at the most recent information available. Applying Klarna's revenues from the last 12 months (LTM) will provide a much better estimate of value than using earnings from the last financial year. Additionally, to more recent data, we

will also add forward looking revenue multiples to the relative valuation analysis to incorporate future growth potentials of the companies being taken into consideration.

## **Positioning of Klarna**

The following steps will determine the valuation and positioning of Klarna among its peer companies in a structured manner. As a first step, this analysis will identify and select a universe of comparable companies for Klarna. Then, these peer companies will be benchmarked against Klarna based on financial statistics. The multiples calculated will then serve as the basis for extrapolating a fair valuation range for Klarna reflecting current market conditions.

### **Select the universe of comparable companies**

Firstly, students need to study Klarna and identify its key characteristics in order to identify commonalities with other companies and select comparable companies. Therefore, it is necessary that students study the case study by focusing on the business model, financial and operational performance including revenue and geographic segmentation of Klarna and its direct competitors in the BNPL space. Exhibit 15 provides a more detailed comparison between the BNPL providers. Based on this information we found Affirm, Splitit, Afterpay<sup>1</sup>, Paypal (Credit) and Zip, that share similar characteristics in terms of business model, operational and financial performance. They can be considered as direct competitors as they operate in the BNPL space and primarily target the US market, which Klarna identified as its major growth market and where it intensified its market penetration. Comparing GMV in 2021 with Affirm (\$22.4bn) and Afterpay (\$19.7bn), Klarna generates a GMV of \$80bn that is nearly four times as big as the two closest pure BNPL peers. Similar to that, Klarna builds on an active yearly user base of 146 million consumers in 2021, whereas Affirm has 14 million and Afterpay has

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<sup>1</sup> Afterpay has been acquired by the US-listed company Bloc Inc. (NYSE: SQ), formerly known as Square, in Q1 2022 for \$29bn **Invalid source specified.**

16.2 million consumers on their platform. GMV translates into average order values of \$110 (Klarna), \$600 (Affirm) and \$117 (Afterpay) by putting GMV and total number of transactions per year in relation to each other. However, PayPal outperforms all BNPL providers in terms of adoption speed. Nearly two years after launching its BNPL product in Q4 2020, PayPal has passed both Afterpay and Affirm in the number of new customers, according to company information. According to several sources, PayPal already reached an user base of 22 million consumers that pay for purchases in interest-free installments (Pymnts, 2022). This early momentum reflects PayPal's considerable scale potential. 1.6 million or 54% of all merchant websites accept PayPal (30% of these websites are from the US), compared to 89,000 websites or 3% that offer Klarna at checkout (SimilarTech, n.d.). Furthermore, PayPal offers BNPL at no additional costs for its merchant network which facilitates the integration process for their existing merchants. Out of 35 million merchants partners, around 280,000 already used PayPal's BNPL solutions. Hence, in addition to Affirm and Afterpay (Bloc Inc.), PayPal has to be considered one of the strongest competitor for Klarna that relies on a huge network and scaling potential, especially in the US to quickly catch up on the BNPL giants.

Affirm, Afterpay and PayPal are positioned as a consumer-facing technology, where they coordinate with merchants to deliver BNPL services, which consumers are able to access as a payment method. Due to these similarities, they are considered decisive when applying valuation multiples to Klarna's enterprise value.

However, evaluating Klarna within the current market environment requires not only to look on direct competition but to reflect on risks and growth potentials associated to its business operations and market situation, as they determine the future outlook and positioning of Klarna within the BNPL sector and the financial industry as a whole. As a relative valuation can widely vary depending on these factors, this analysis will incorporate further clusters of companies that impact Klarna's business and give a more accurate picture of a fair valuation range.

Klarna has been granted full banking licenses in its operating countries, which gives the fintech company the right to offer banking products and services to its customers, such as issuing payment cards, operating saving accounts and turning into an all-in-one digital wallet. On the other hand, it implies that this bears similar risks associated to financial institutions. They mainly include credit default risks and regulation changes that can impact Klarna's business operations. Credit default risk refers to the risk of default on debt. In Klarna's case this arises when it realizes losses due to not having its receivables repaid, due to the counterpart's inability or unwillingness to fulfill its obligations. Klarna is exposed to credit risk primarily from customer lending, exposure to merchants, governments, municipalities and credit institutions as well as risk against third party payment service providers who accept payments on behalf of Klarna (Klarna, 2021). Regulatory changes affecting financial institutions and BNPL offerings may pose another significant risk to Klarna and the consumer-facing BNPL industry as a whole. Even though addressing this risk might create complexities as regulations can vary between all operating countries due to different policy makers and legislations, there are already examples reflecting on actions taken to tighten regulation for the BNPL industry. In the UK, one of Klarna's main markets, the Financial Conduct Authority (FCA) marked that "the current economic climate of a cost-of-living crisis, rising inflation and interest rates and talk of wider recessionary pressures, has the potential to create an environment that makes BNPL more attractive to consumers" (Financial Conduct Authority, 2021). As a result, in September 2020, the FCA commissioned a review of the unsecured lending market, which concluded that there is an urgent need to regulate all BNPL products to protect consumers. In June 2022 the UK government set up a plan to strengthen regulation of unsecured short-term interest-free credits, including a more in-depth credit check process to guarantee that loans are affordable for consumers as well as stricter advertising guidelines (HM Treasury, 2022). This is only a glimpse of what regulation can entail for consumer credit lenders but underlines potential

threads affecting BNPL providers such as Klarna. All in all, both credit default risks and regulatory changes show that Klarna has risk exposures similar to consumer focused financial service companies. Therefore, including consumer specialty finance companies, that offer similar banking products for consumers and face similar risks, provides a base for a more robust valuation range. A third cluster, which allows to incorporate further upside on Klarna's future development, comprises global payment technology companies such as Visa, Mastercard or Fiserv. These two-sided networks benefit significantly from their strong network of consumers and merchants, which reinforces widespread acceptance, based on both groups' benefits accessing the network and its participants. This enables payment technology giants to create interactions between consumers and merchants and try to get the two or multiple sides on board by appropriately charging each side (Sidak, 2016). In addition, there is a strong lock-in effect as customers, merchants and other payment service providers rely on the payment infrastructure that has been built, which in turn allows companies like Visa to use the network to easily integrate new offerings along the payment value chain, reinforcing their dominance, adoption and innovation process. Given Klarna's yearly customer base of nearly 150 million users, its rapidly growing merchant network of more than 450k partners, the expansion of its existing open banking platform and the establishment of a go-to-shopping app with 23 million users, Klarna offers a highly favorable environment to become a similar two-sided network.

**Locate necessary financial information, spread trading multiples, benchmark comparable companies and determine enterprise value**

Exhibit 24 outlines an overview for locating the necessary financial information to calculate key financial statistics and multiples for the selected comparable companies. Once the information, for each of the comparable companies has been located, it is entered into a table to display the financial data and to calculate the relevant trading multiples (see Exhibit 25). While the entire universe provides an useful perspective, we established three clusters

consisting of pure BNPL, consumer finance and payment technology comps as a basis for creating different valuation scenarios for Klarna's implied enterprise value. These scenarios consist of a conservative, pessimistic and optimistic case that capture future risk and growth drivers (as examined before in the teaching note) affecting Klarna, which will be further discussed in a critical assessment. Additionally for each peer group the medians, highs (75th percentile) and lows (25th percentile) are calculated to establish a preliminary reference point for determining Klarna's valuation range. More specifically the medians of the EV/Sales multiples were used to extrapolate a defensible range of multiples, while the high and low multiples provide further guidance for adjustments within each peer group.

For the conservative scenario in June 2021 where we compare Klarna to its direct peers from the BNPL space, Klarna trades in the range of 3.1x (low) to 6.1x (high) LTM (06.2021) Sales. Here, the Median of 4.8x serves as a multiple to produce an enterprise value of \$7.7 bn. In a more pessimistic case, where we assume that BNPL providers resemble consumer finance companies, Klarna's enterprise value would be around \$3.5bn with a median of 2.1x, which serves as multiple. By contrast, in an optimistic scenario where Klarna potentially becomes a two-sided network similar to payment technology companies, the fintech trades in the range of 5.0x to 14.7x LTM (06.2021) sales. Here, the EV/sales multiple of 14.7x (75th percentile) is used as a multiple to incorporate a significant uplift in enterprise value to \$16.1bn. Exhibit 26 provides an overview of all valuation scenarios.

### **Critical assessment**

To provide a critical review and thus stimulate possible discussions that can be addressed in class, we take a critical look at the valuation methodology used and assess implications that arise from the valuation scenarios. Finally, we weigh the extent to which the analysis determines a fair enterprise value, taking into account the actual valuation that emerged in reality from a down round.

Using an EV/sales multiple, the relative valuation methodology makes it possible to systematically determine Klarna's enterprise value without performing an intrinsic valuation and without taking the company's profits into account. But in the case of Klarna, a major disadvantage of focusing on EV/sales multiples is that Klarna can be assigned a high value because the company achieves high sales growth. However, this approach does not take into account the significant losses. Ultimately, a company must generate profits and cashflows to have real value. It is paramount to always keep this principle in mind before evaluating a company.

We have also found out that relative valuation is a useful method to value a fast-growing fintech like Klarna and derive a fair market-oriented valuation. The fact that multiples reflect market sentiment also means that using relative valuation to estimate Klarna's enterprise value can result in low values when the market undervalues comparable companies or high values when it overvalues these companies. This can be illustrated very well in our case, comparing the valuations identified here with the actual valuations that emerged from the June 2021 (peak valuation) and July 2022 (down round) financing rounds (see Exhibit 27). In June 2021, Klarna raised \$639m at a post-money valuation of \$45.6bn (EV of \$44.5bn). In July 2022, the company raised \$800m during a down round and was valued at only \$6.7bn (EV of \$5.8bn) (Klarna, 2022). Exhibit 28 shows the calculation that leads from the post-money valuation to the EV. If we first look at the optimistic case for the peak valuation, which produces an EV of \$30.8bn based on an EV/Sales (LTM, 06.2021) multiple of 21x (75th percentile), the valuation is still significantly below the real EV of \$44.5bn, under which Klarna actually raised a financing round. This shows a premium of 45% and suggests a potential overvaluation, possibly due to the value of high tech stocks and overly optimistic investor sentiment contributing to the peak valuation at that time (see Exhibit 23). Also if we compare our more conservative case during the down round to reality, we find a similar picture. More cautious

investor sentiment in a worse market environment caused valuations to fall. The multiple of 4.8x applied here determines an EV of \$7.7bn, whereas the real EV is below at \$5.8bn and is an indicator of undervaluation. It has to be noted that this result is merely an observation that emerges from the analysis conducted here and therefore is not a definitive result from which a clear right or wrong conclusion can be drawn. However, it does illustrate another point of criticism that is associated to it. While there is room for bias in any type of valuation, the lack of transparency in the underlying assumptions of relative valuations makes them particularly vulnerable to manipulation, as each analysis has the ability to change the multiple on which the valuation is based, and the selection of peer companies essentially ensures that a wide range of values can be justified.

In order to determine a market-oriented value of Klarna that prices in the present market conditions, it is also important to identify potential opportunities and risks that will move Klarna, and thus the BNPL market, in the future and already provide a fair valuation today. Valuations are forward-looking. Therefore, it is valuable to set up possible scenarios to give a comprehensive picture of Klarna's valuation and to show possible implications resulting from a more optimistic and more pessimistic valuation scenario.

In the optimistic case, looking at valuations as of July 2022, Klarna reaches a valuation of \$24bn, which is tied to the expectation that the company can develop a platform with network effects similar to payment technology companies such as Visa, Mastercard or Finserv. By increasing its consumer base, Klarna could transform itself from an unsecured consumer lender to a tech giant that collects and processes transactional data and serves as a lead generator for retailers. This would increase attractiveness to merchants and would drive conversion to the platform creating a flywheel effect, that might enable increasing user engagement and cross-selling opportunities to withstand intense competitive pressure. Additionally, by entering open banking, Klarna has already proven its ambition to build a two-sided network connecting

consumers with merchants.<sup>2</sup> Increased adoption of open banking initiatives by merchants would allow Klarna to bypass payment infrastructure service providers such as Visa and save costs by eliminating processing fees. Another point that contributes to Klarna building a two-sided network in an optimistic case that exploits further value creation potential, lies in its expansion of the "all-in-one" app. The application enables Klarna to introduce additional services that are closely integrated with the customer experience to become the go-to consumer e-commerce portal. For example, Klarna's mobile app can offer one time credit cards to use BNPL features on any e-commerce website. So, instead of being only a pure BNPL player, Klarna shows the potential to become a combination of direct-to-consumer shopping app, merchant marketing and consumer finance provider. Overall, the indicated value creation potentials and the higher publicly traded payment technology service providers (Visa, Mastercard) compared to pure BNPL companies, lead to an EV/Sales multiple of 14.7x, reflecting a very optimistic scenario.

This contrasts with the pessimistic scenario, which represents the lower end of the valuation range at \$3.5bn. In the pessimistic scenario, we assume that in addition to an increasingly crowded market and intense competition, Klarna shares risks of a financial services company. This means that credit default risks and regulatory changes may affect future growth. In terms of regulation, Klarna is regulated as a bank in its main markets but the BNPL market and related products are hardly regulated so far. Regulators in the UK are already reviewing BNPL and have decided to create a regulatory framework for BNPL products. This is an indication that there is a risk that formal regulation for this sector would have a significant impact on the adoption, product structure and profitability of BNPL. This could, for example, lead to a deteriorating reputation for BNPL products, thus affecting market growth. As Klarna offers

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<sup>2</sup> In 2019, Klarna launched its Open Banking platform. By 2022, this platform already integrates with more than 15,000 European banks through a single Access to Account API in line with the Payment Services Directive (PSD2) (Klarna, 2022).

short-term, unsecured consumer loans to customers that are not verified with standard credit checks, the company, like other consumer finance providers, is exposed to credit default risk. Klarna has reported higher credit default rates in the first half of 2022, which mainly correlates with the launch in the US market and has likely contributed to increased losses. However, since Klarna does not segment and disclose the repayment behavior of its customers, it is hard to make more precise statements about the credit default risk. Nevertheless, it can be stated that this aspect is of enormous importance for the assessment of industry-specific risks and should therefore also be considered as part of a class discussion. So in summary instead of being assessed like a BNPL or payment technology company, in the pessimistic case, Klarna would be priced like a consumer finance firm at 2.1x EV/Sales. Depending on whether investors see Klarna as a two-sided network or a financial company, its enterprise value can range from \$2.8bn to \$24bn. Nonetheless, it must be noted that these scenarios are only included as a supplement to the conservative main scenario in order to cover a broader assessment framework.

If we compare the actual EV with which investors valued Klarna when the down round was announced on July 11, 2022, we use the conservative scenario. This gives us the opportunity to focus exclusively on the BNPL market and the associated listed players and to derive a market-oriented value that probably embodies a higher practical relevance than more speculative and ambiguous scenarios such as the optimistic as well as the pessimistic case.

A multiple range of 3.1x to 6.1x EV/sales was determined, resulting in a possible EV ranging from \$5.05 to \$9.95bn (with a median of \$7.7bn). Therefore, a fair EV would only be achieved if both the management team of Klarna and the lead investors of the financing round agree on a price within this range. In reality, a down round led by Sequoia Capital took place at a post-money valuation of \$6.7bn. Assuming an enterprise value of \$5.8bn as computed in Exhibit 28, this would correspond to a multiple of 3.6x EV/sales in our model. In the conservative

scenario, this EV falls below the median of \$7.7bn at the lower end of the valuation range. This means that based on all assumptions made in this analysis, a comparison of Klarna's actual EV shows that the EV range, which we computed comes close to the value the investors assigned to Klarna given the prevailing market environment.

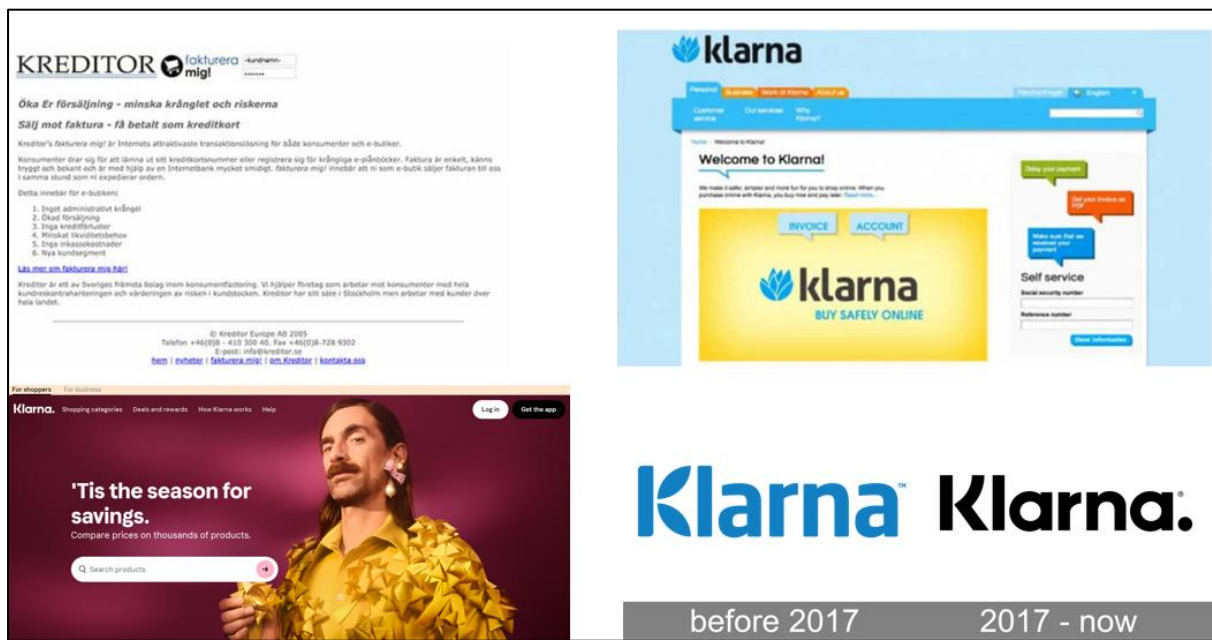
# Appendix

Exhibit 1: Overview of selected venture capital backed financing rounds

Date	Stage	Amount	Pre-Valuation	Lead investor	Investors	Use
10/April/2005	Angel	\$0,06M	\$0,54M	Walerud Ventures		Project development
7/December/2007	Series A	\$2,22M		AB Öresund		Expand to Norway, Finland and Denmark
6/May/2010	Series B	\$9M		AB Öresund and Sequoia Capital		Foster growth - increased its revenue by 80% to more than \$50 million in 2010
10/December/2011	Series C	\$ 115,24M		General Atlantic	DST Gobal and Sequoia Capital	Increase product portfolio
14/March/2014	Series D	\$ 90M		Tengelmann Ventures, General Atlantic and Panorama Point Partners	Lakestar, Atomico, IVP, SXM Global, Sequoia Capital, SSE Business Lab and Hartford Financial Services Group	
18/August/2015	Series E	\$ 80M	\$2,17B	Northzone Ventures and Wellcome Trust		
01/March/2019	Series F	\$106M	\$2,98B	Bestseller, Brightfolk and Permira	Sequoia Capital, Decisive Capital Management, Niklas Adalberth and Victor Jacobsson	Enter new markets and improve banking proposition
06/August/2019	Series G	\$460M	\$5,04B	Dragoneer Investment Group	Commonwealth Bank of Australia, IPGL, IVP, Chrysalis Investments, Inbox Capital, Louise Dahlborn Samet, Peter Sjunnesson, Mattias Ljungman, BlackRock, GP Bullhound, Förstia AP-fonden, Decisive Capital Management and HMI Capital	Increase growth in the US
10/June/2021	Series H	\$639M	\$45.6B	SoftBank Investments	Knuru Capital, ADIT Ventures, Elevation Capital, InterAlpen Partners, Khalili Brothers, Align Ventures, Inertia Ventures, Alpha Wave Global, Alder Companies, Honeycomb Asset Management, Mundi Ventures, Spring St. Group, Surton Capital, WestCap Group, Harvest Growth Capital, MSA Capital, Maximize Capital, Novos Capital, Heliad Equity Partners, West Coast Equity Partners, Redo Ventures, Solida Capital, Hestia Holdings, University Growth Fund, StraightPath Venture Partners, Arctic Ventures, K20 Fund, Super Capital VC, Mastry, Blue Opal Capital, FinSight Ventures, Backstage invest, Digital Horizon, Vista Equity Partners, Alstin Capital, Reimann Investors, NP Capital, Chaos Ventures, Flat Capital, The ECI Group, DFI Ventures, Newman Capital and Ericseuz Capital	Support international expansion and further capture global retail growth
Possible round in July 2022	Series I	\$800M	\$6,7B	Bestseller, Silver Lake and Sequoia Capital	Commonwealth Bank, Ferrer, Mubadala Investments Company, MSA Novo, D2 Ventures, Altun Capital, Two Culture Capital, Lume Capital and Canada Pension Plan Investment Board	

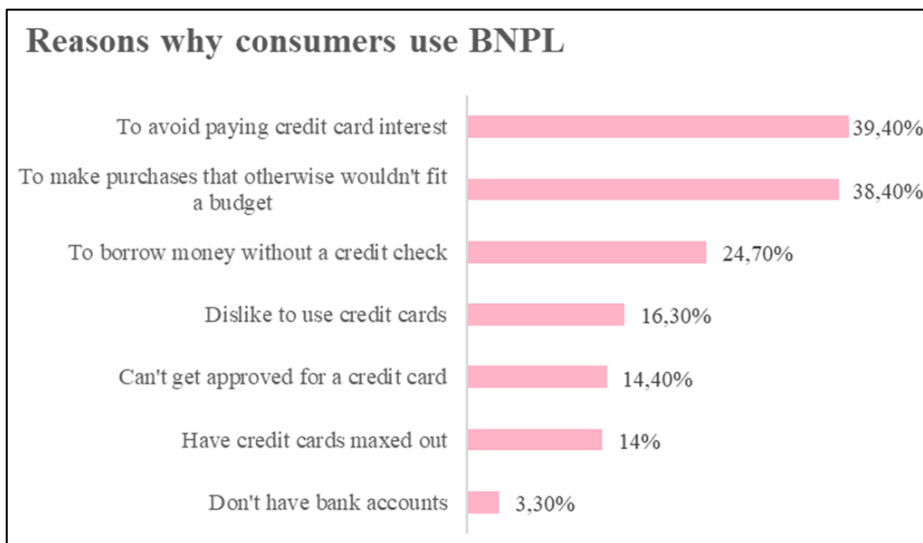
Source: Own illustration from information aggregated on Pitchbook

## Exhibit 2: The evolution of Klarna's logo and website



Source: Company information

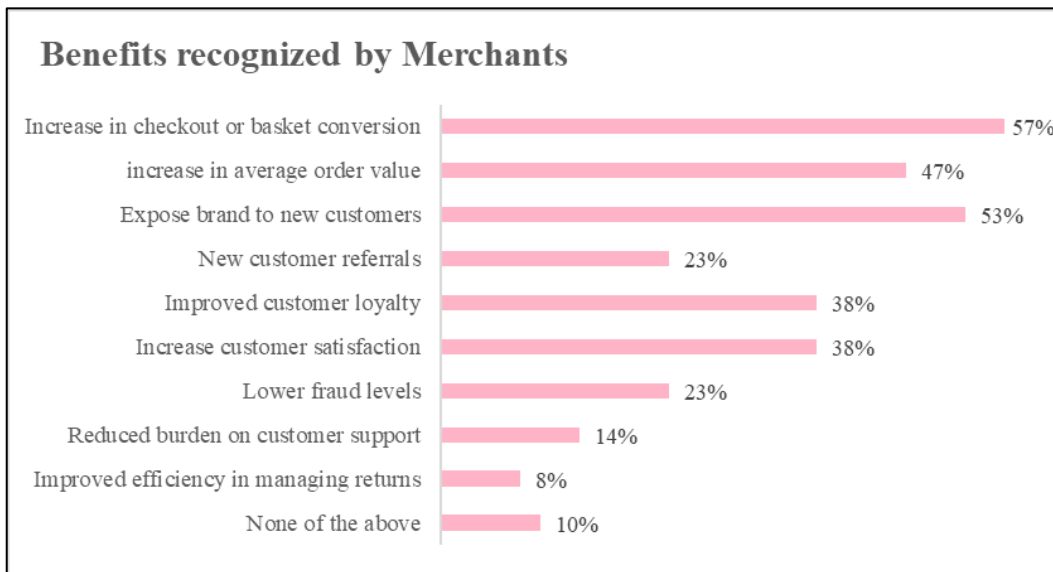
## Exhibit 3: Reasons why consumers use BNPL



Notes – US consumers only; Respondents were able to select multiple responses.

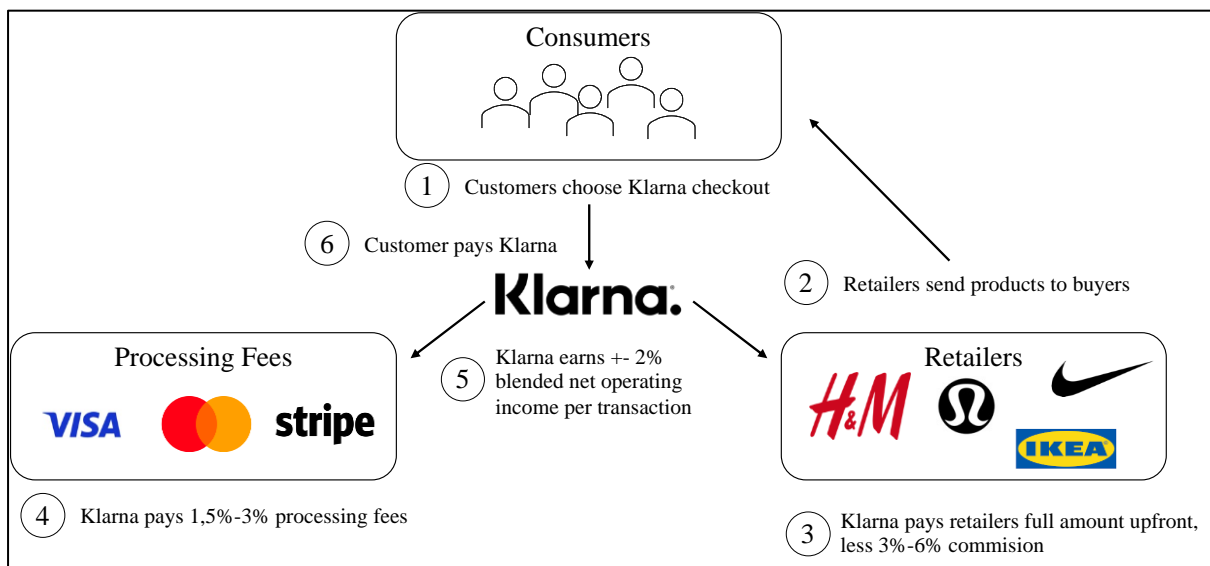
Source: Adaptation from (Insider Intelligence, 2022)

Exhibit 4: Benefits recognized by Merchants



Source: Adaptation from (Bain&Company, 2019)

Exhibit 5: Klarna's business model illustrated



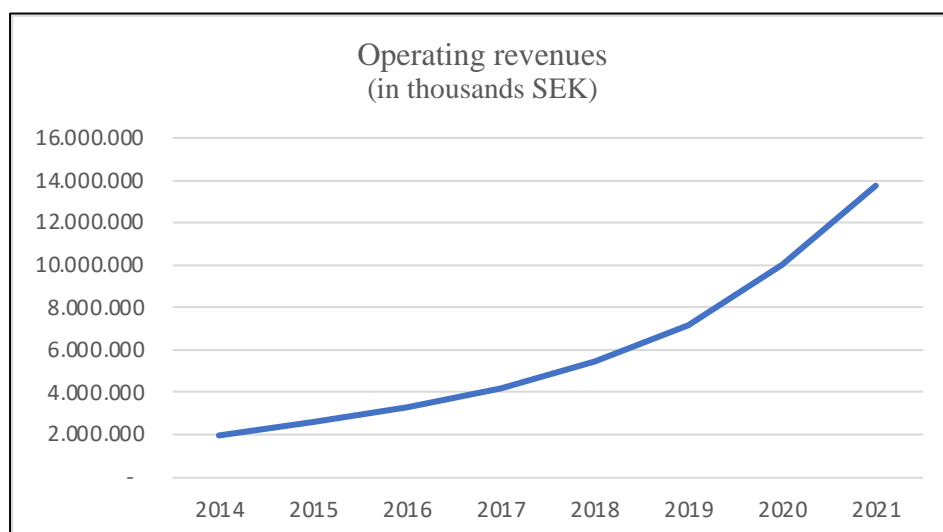
Source: (Goel, 2021)

Exhibit 6: Klarna's late fee cost structure

<b>Total order value</b>	<b>Fee per late repayment</b>	<b>Maximum late fee per order</b>
Up to \$24,99	\$0	\$0
\$25 - \$59,99	\$2	\$6
\$60 - \$99,99	\$4	\$12
\$100 - \$199,99	\$6	\$18
\$200 +	\$8	\$24

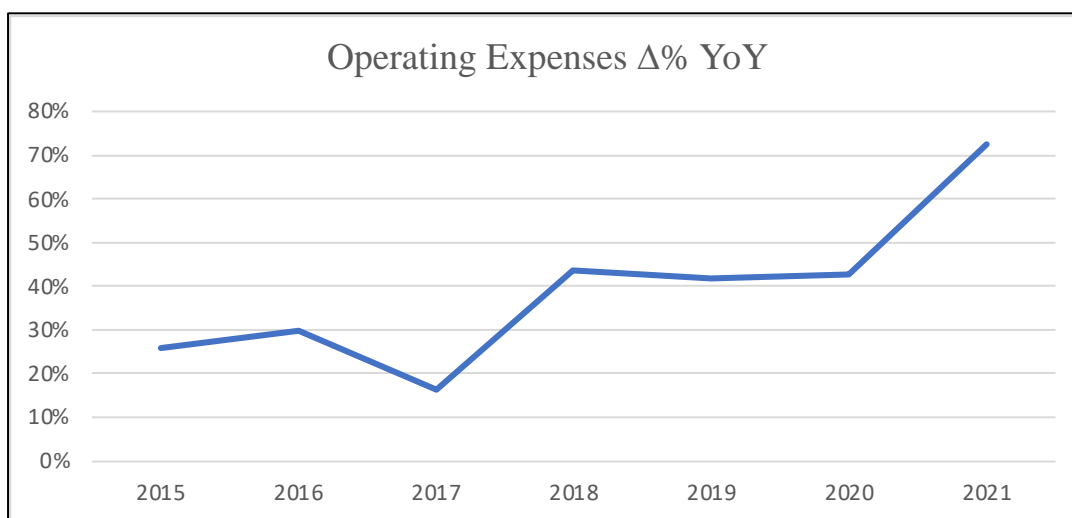
Source: Company information

Exhibit 7: Operating revenues



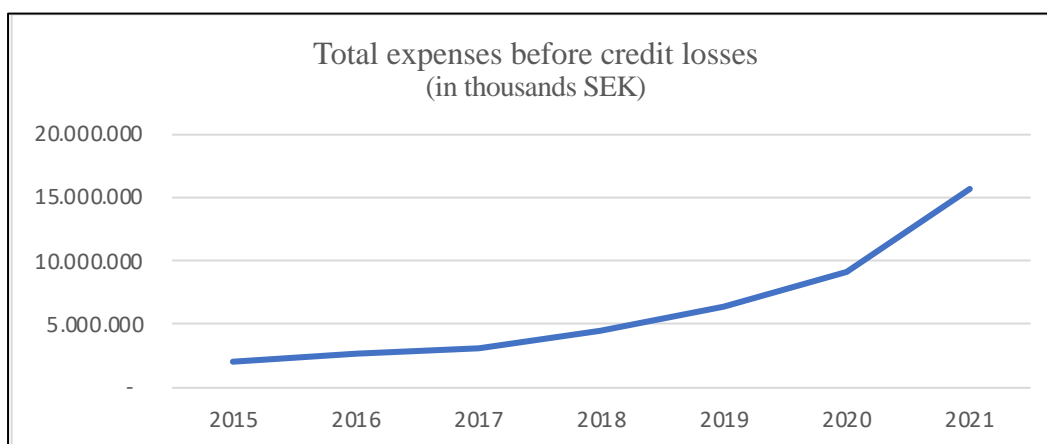
Source: Company information

Exhibit 8: Operating expenses  $\Delta\%$  YoY



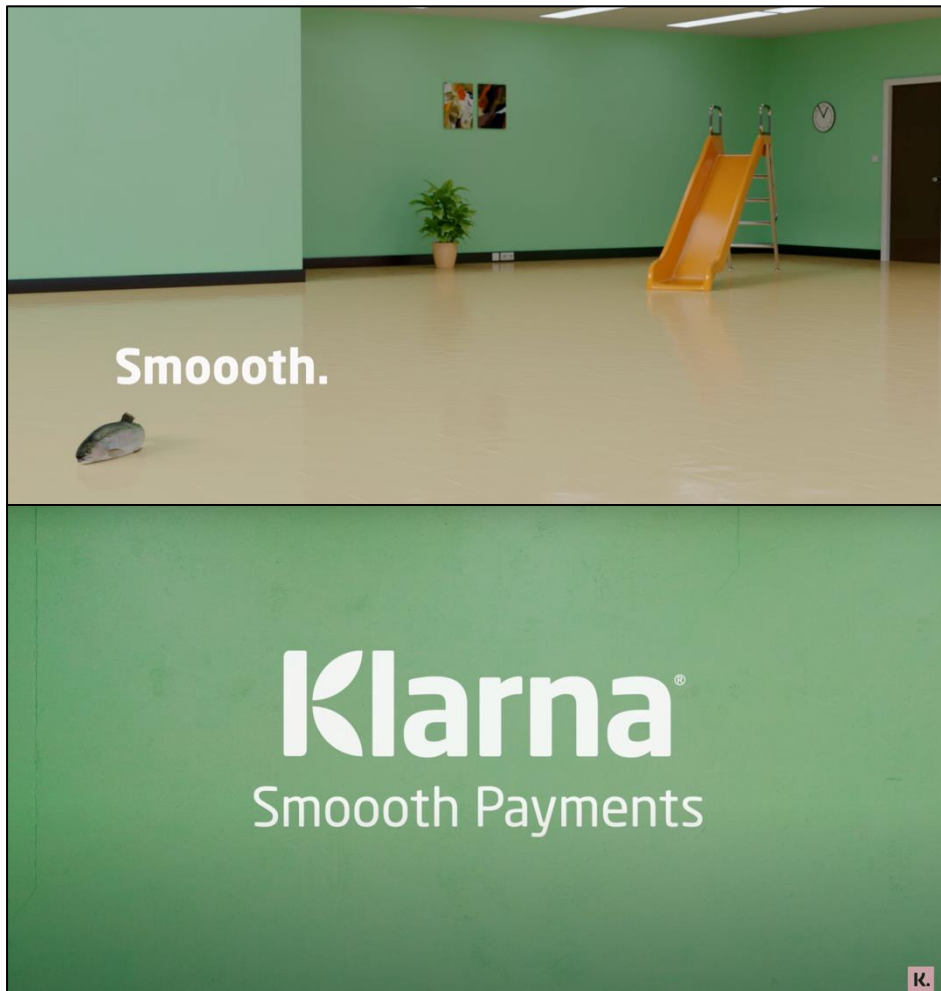
Source: Company information

Exhibit 9: Total expenses before credit losses



Source: Company information

Exhibit 10: Pictures of the Klarna Smooth campaign



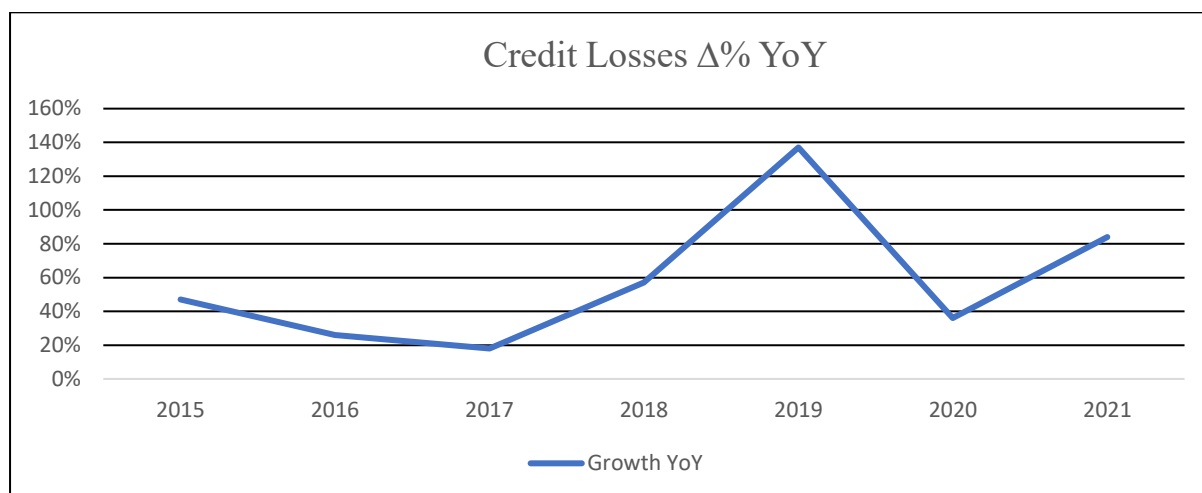
Source: (Youtube, 2016)

Exhibit 11: Picture of the Klarna campaign with Snoop Dogg



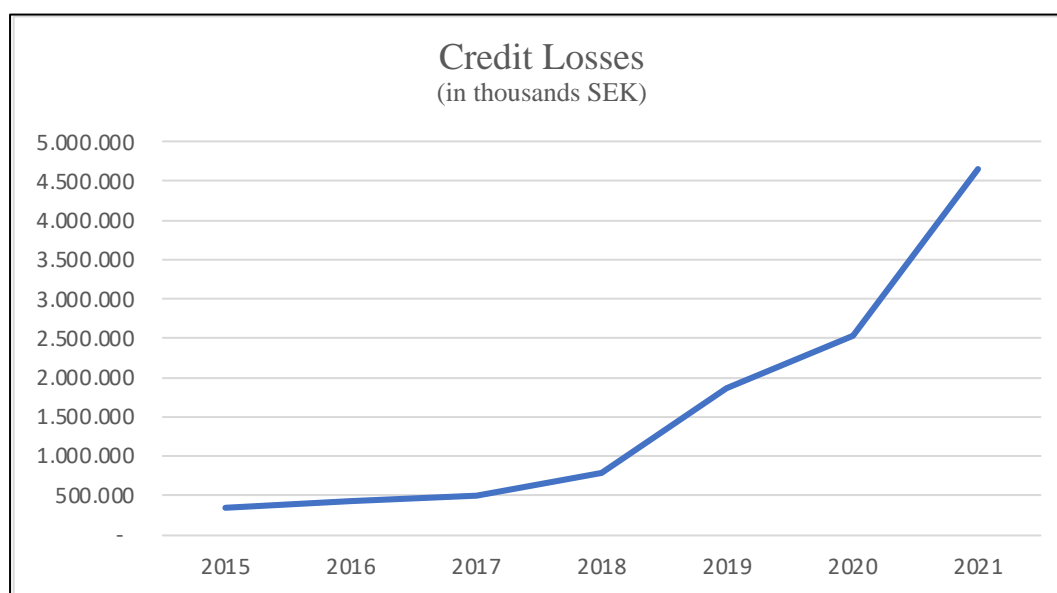
Source: (Klarna, 2022)

Exhibit 12: Graph Credit Losses  $\Delta\%$  YoY



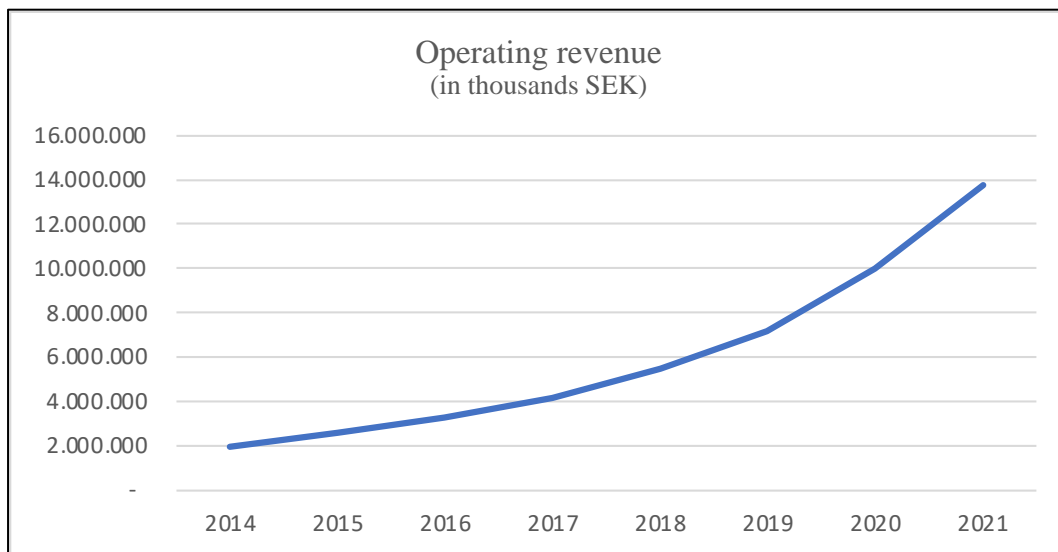
Source: Company information

Exhibit 13: Credit losses



Source: Company information

Exhibit 14: Operating revenue



Source: Company information

Exhibit 15: Overview of direct BNPL competitors of Klarna

	Klarna	Affirm	Splitit	Afterpay (Bloc Inc.)	Zip Co. Ltd.
<b>Company</b>					
<b>Founded</b>	2005	2012	2012	2014	2013
<b>Total Funding (until 30.06.2022)</b>	\$3.7bn	\$1.5bn	\$275m	\$449m (Afterpay), \$601m (Bloc Inc.)	\$894m
<b>Enterprise Value (as of 29.06.2022)<sup>2</sup></b>	Private	\$8.9bn	\$0.107bn	(Acquired by Bloc Inc. for \$29 bn on 01.08.2021)	\$1.93bn
<b>Main countries of operation</b>	Nordics, US, Germany, UK	US, Canada	US, Australia, Canada	Australia, US, UK	Australia, US, Canada, Czech Republic, Mexico, India, Philippines, New Zealand, Poland, Saudi Arabia, UAE, South Africa, UK
<b>Product Offering</b>	BNPL (split the cost of purchase into interest-free repayments with late fees charged), 'Pay in 30 days' (pay up to 30 days with late fees charged), 'personal financing' (Consumers can choose the term of loan and pay interest accordingly)	Installment Pay, Virtual Card, Splitpay, Consumer Marketplace, Savings account	Core installments via issuer by taking excess credit capacity and holding it	Installment pay (Pay for purchases in 4 installments with interest and late fees charged)	'Pay in 4' (pay for purchases, interest and late fee-free, over four separate payments), 'Pay monthly' (pay in 6, 12, or 24 payments)
<b>Distribution Channels</b>	Omni-channel (App, merchant website, in-store)	Omni-channel	Merchant website and in-store	Omni-channel	Omni-channel
<b>BNPL range of payback duration</b>	6-36 months	6-48 months	3-24 months	14- 56 days	6 weeks
<b>Take rates from merchants</b>	~3-6%	~3-5% (no late fees charged)	~1.5-3%	~4-6%	~2-4%
<b>Gross merchandise volume (GMV)</b>	SEK689bn (\$80bn) (FY 2021)	\$22.4 bn (FY 2021), \$15.5bn (LTM, 06.2022)	\$395m (FY 2021)	\$19.7bn (Afterpay, FY 2021)	\$8.7bn (FY 2021)
<b>GMV (H1 2022)</b>	SEK396bn (+21% YoY) (\$41bn)	\$8.3bn (73% YoY)	\$195bn (+ 19% YoY)	No breakdown available as Afterpay acquisition by Bloc Inc. was completed in Q1 2022	\$4.4bn (+ 91% YoY)
<b>Revenue<sup>3</sup></b>	SEK14.9bn (\$1.77bn) (LTM, 06.2022)	\$1.35bn (LTM, 06.2022)	\$108m (LTM, 06.2022)	\$16.29bn (Bloc Inc. Total revenue), \$833m (FY 2021, Afterpay revenue)	\$451.34m (LTM, 06.2022)
<b>Revenue CAGR (2019-2021)</b>	39%	81%	152%	94%	96%
<b>Merchants</b>	450k	234k	1.5k	98.2k (Afterpay, FY 2021)	81k
<b>Annual active users</b>	150m (30m in US) (LTM, 06.2022), 146m (FY 2021)	14m (mostly US) (FY 2021)	400k (FY 2021)	35m globally, 280k (using BNPL)	9.9m (06.2022)
<b>Credit default risk (credit loss as % of GMV and provision for credit loss as % of GMV)</b>	0.67% (2021)	1.65% (LTM, 06.2022)	No - sits with issuer via hold on credit line	16.2m (Afterpay, FY 2021)	400m (~22m using BNPL in FY 2022)
<b>Average order value (GMV per total number of transactions per year)</b>	\$110 (assuming 2m transactions per day, FY 2021)	\$600 (FY 2021)	\$1000 (FY 2021)	\$117 (FY 2021, Afterpay only)	\$220 (assuming 20m transactions per year)

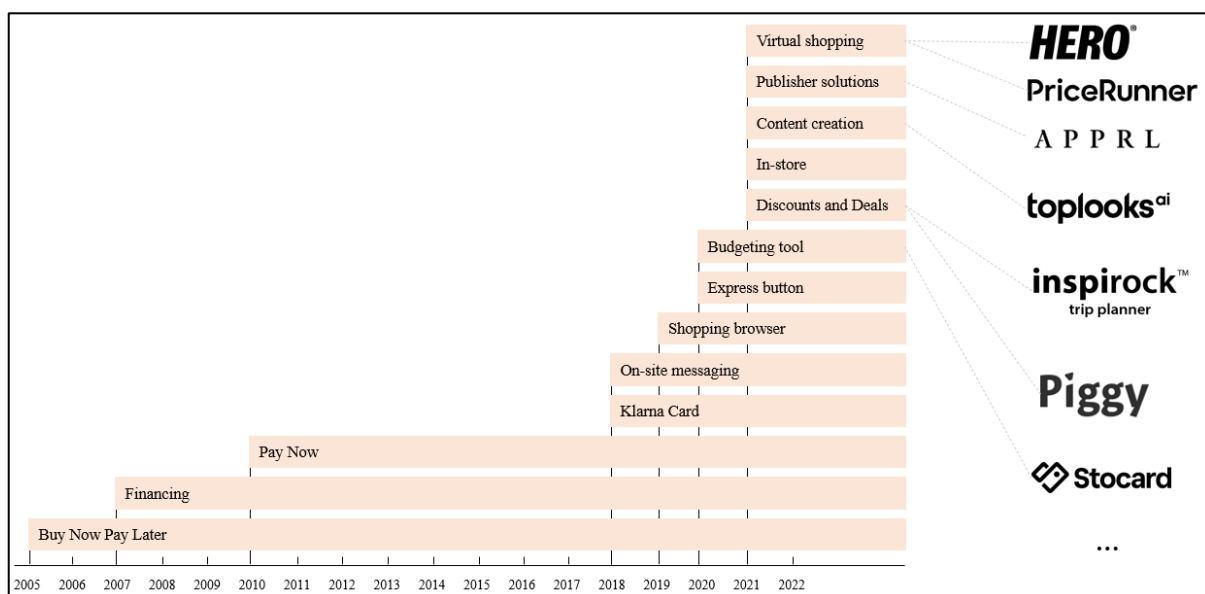
Source: 1) Ycharts 2) Company filings, press releases, 3) Bloomberg

Exhibit 16: Overview of selected and publicly disclosed transactions by Klarna

Company	Transaction Date	Origin	Description	Deal Value (\$m)
Analyzd	2011	Israel	Risk and fraud management	-
SOFORT	2014	Germany	Online payment provider, open banking	150
Cookies Labs	2016	Germany	P2P money transfer	-
BillPay	2017	Germany	Online payment provider	70
ShopCo	2018	Germany	E-commerce shopping cart provider	-
Close Brothers Retail Finance	2018	UK	Retail finance	-
Spring Marketplace	2020	US	Marketing	-
Moneymour	2020	Italy	Online payment provider	-
Nuji	2020	UK	Online shopping portal	-
Woiła	2020	Sweden	Shopping experience	-
Semtail	2020	Sweden	Search engine marketing	-
Shoptail	2020	Sweden	Search engine marketing	-
Toplooks.ai	2021	US	AI-driven content creation tools	-
Hero	2021	UK	Virtual social shopping	-
APPRL Fashion	2021	Sweden	Shopping experience	-
Stocard	2021	Germany	Mobile wallet provider	110
Inspirock	2021	US	Online travel planner	-
Piggy	2021	US	Shopping experience, Automatic couponing	-
PriceRunner	2022	Sweden	Price comparison platform	1,000

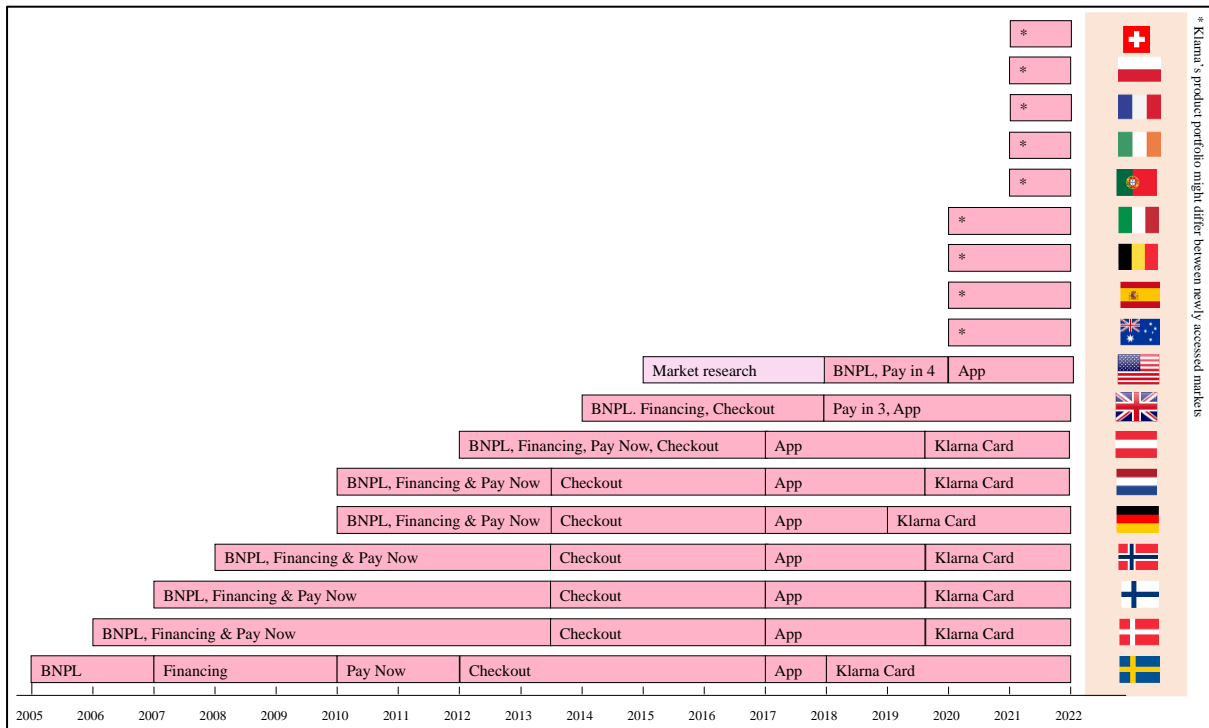
Source: Own illustration based on various press releases

Exhibit 17: Timeline of acquisitions and associated new segments



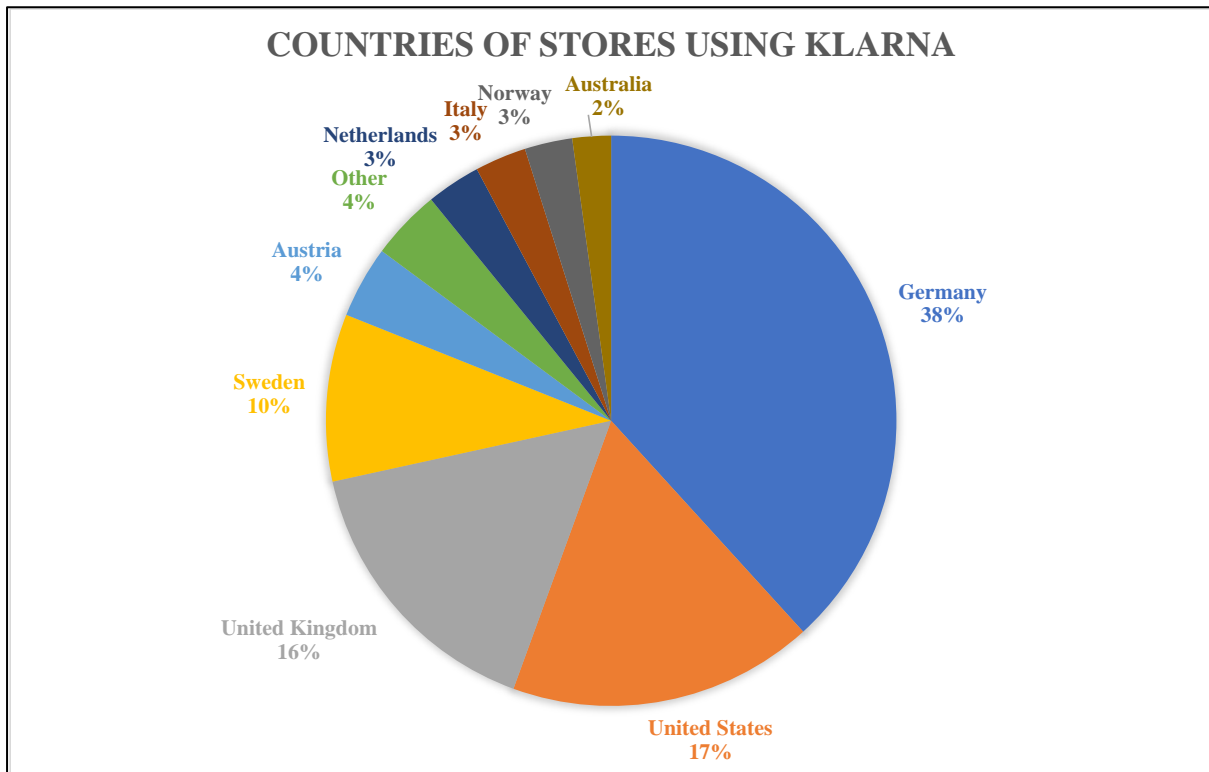
Source: Company information

Exhibit 18: How Klarna developed towards an internationally recognized fintech



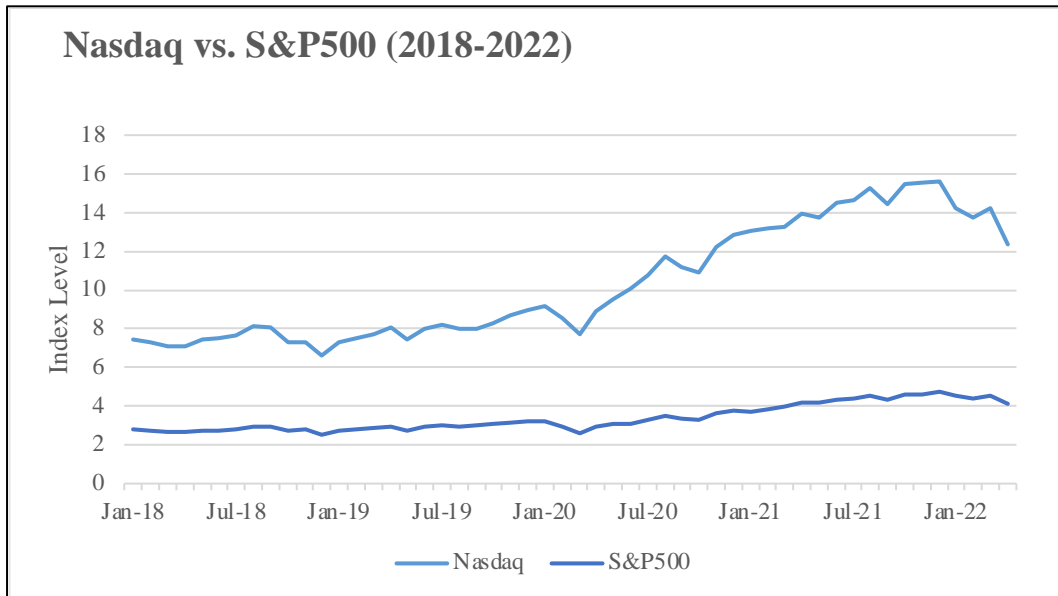
Source: Company information

Exhibit 19: Countries of stores using Klarna



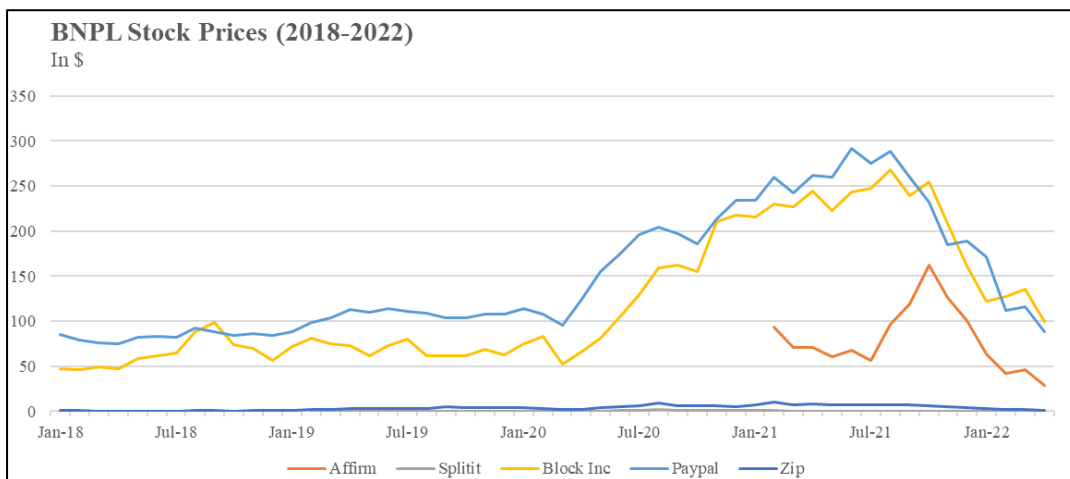
Source: (Store Leads, 2022)

Exhibit 20: Nasdaq vs. S&P500 (2018-2022)



Source: (Yahoo Finance, n.d.)

Exhibit 21: BNPL Stock Prices (2018-2022)



Source: (Yahoo Finance, n.d.)

Exhibit 22: Key information of Klarna's down round in July 2022



Source: (Thomson Reuters, 2022)

Exhibit 23: Stock price development of Meta, Netflix and Affirm between Q4 2021 and Q2 2022



Source: (Yahoo Finance, n.d.)

Exhibit 24: Summary of financial data and primary sources

<b>Information Item</b>	<b>Source</b>
Sales	Income statement from annual report of given company (10-K, 10-Q, 8-K, Press Release)
Sales Forecast	Bloomberg (terminal) or Finance Yahoo (website)
Market capitalization	YCHARTS for historical statistics (website)
Enterprise value	
Exchange rates	OFX for historical exchange rates (website)

Source: Own illustration

Exhibit 25: Valuation table including Klarna's public peers

Ticker	Name	Market cap (USDm) <sup>(1)</sup>		EV (USDm) <sup>(1)</sup>		Sales			EV-to-Sales Multiple				
		30.06.2021	30.06.2022	30.06.2021	30.06.2022	LTM, 30.06.2021	LTM, 30.06.2022	2022E <sup>(3)</sup>	2023E <sup>(3)</sup>	LTM, 30.06.2021	LTM, 30.06.2022	2022E	2023E
<b>BNPL direct peers</b>													
AFRM	Affirm	18,140.00	5,189.80	18,570.00	6,417.90	1,123.00	1,349.30	1,713.30	2,259.90	16,54x	4.76x	3.75x	2.84x
PYPL	Paypal	343,910.00	807,400.00	339,770.00	82,070.00	23,846.00	26,389.00	27,856.00	31,565.80	14,25x	3.11x	2.95x	2.60x
SO	Soce Inc. (Afterpay)	113,330.00	34,821.40	110,100.00	34,920.80	15,930.79	16,288.40	17,505.60	19,962.40	6.91x	2.14x	1.99x	1.75x
SPT	Spigit	183.20	47.11	195.35	78.25	10.79	11.00	13.20	15.84	18.10x	7.11x	5.93x	4.94x
Zip <sup>(4)</sup>	Zip	3,502.00	234.59	1,926.00	297.22.30	397.52	451.34	507.82	561.69	4.85x	6.59x	5.85x	5.29x
25th %						6.91x				6.91x	3.11x	2.95x	2.60x
Median						14.25x				14.25x	4.76x	3.75x	2.84x
75th %						15.96x				15.96x	6.13x	5.33x	4.41x
<b>Consumer Finance</b>													
SYF	Synchrony Financial	27,920.00	13,470.00	20,640.00	13,180.00	11,496.00	11,311.00	11,591.00	12,900.20	1.80x	1.17x	1.14x	1.02x
AXP	American Express	131,940.00	105,730.00	115,610.00	119,440.00	43,147.00	50,757.00	52,898.30	58,798.30	2.68x	2.35x	2.26x	2.03x
DFS	Discover Financial Services	35,640.00	26,030.00	37,690.00	33,920.00	13,317.00	12,541.00	13,292.30	14,474.30	2.83x	2.70x	2.55x	2.34x
COF	Capital One Financial Corp	69,600.00	42,650.00	55,760.00	61,990.00	29,205.00	32,353.00	34,221.50	36,719.00	1.91x	1.92x	1.81x	1.69x
25th %						1.88x				1.88x	1.73x	1.64x	1.52x
Median						2.29x				2.29x	2.13x	2.03x	1.86x
75th %						2.72x				2.72x	2.44x	2.33x	2.11x
<b>Payment technology (two sided network)</b>													
V	Visa	502,250.00	418,580.00	508,020.00	429,060.00	24,095.00	29,310.00	32,023.00	35,978.60	21.08x	14.64x	13.40x	11.93x
MA	Mastercard	305,080.00	305,380.00	367,970.00	313,600.00	16,685.00	20,828.00	22,197.50	25,300.90	22.05x	15.06x	14.13x	12.39x
FIS	Fidelity National Information Services	87,550.00	57,490.00	105,860.00	75,350.00	13,211.00	14,487.00	14,499.70	15,096.40	8.01x	5.20x	5.20x	4.99x
FBX	First	71,850.00	58,580.00	92,090.00	78,600.00	14,622.00	17,563.00	16,720.00	18,045.70	6.20x	4.54x	4.70x	4.37x
25th %						7.58x				7.58x	5.04x	5.07x	4.84x
Median						14.55x				14.55x	9.92x	9.30x	8.46x
75th %						21.33x				21.33x	14.74x	13.58x	12.04x

Footnotes

(1) Source: YCharts

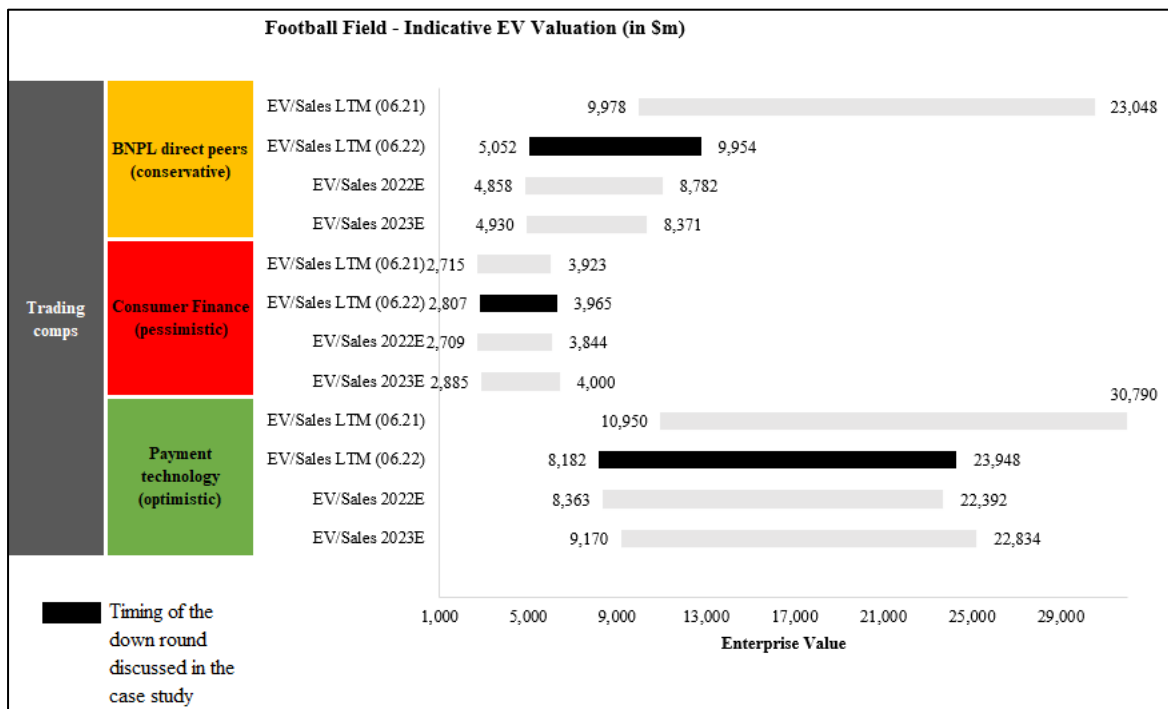
(2) Bloomberg estimates as of 20.11.2022

(3) To arrive from AUD at USD values, the average exchange rates for the last twelve months have been used. For 06.2021 LTM, 2022E and 203E: 1 USD = 1.37709 AUD; For 06.2021 LTM, 2022E and 203E: 1 USD = 1.26419 CAD; For 06.2021 LTM, 2022E and 203E: 1 USD = 1.28805 CAD

(4) To arrive from CAD at USD values, the average exchange rates for the last twelve months have been used. For 06.2021 LTM, 2022E and 203E: 1 USD = 1.26419 CAD; For 06.2021 LTM, 2022E and 203E: 1 USD = 1.28805 CAD

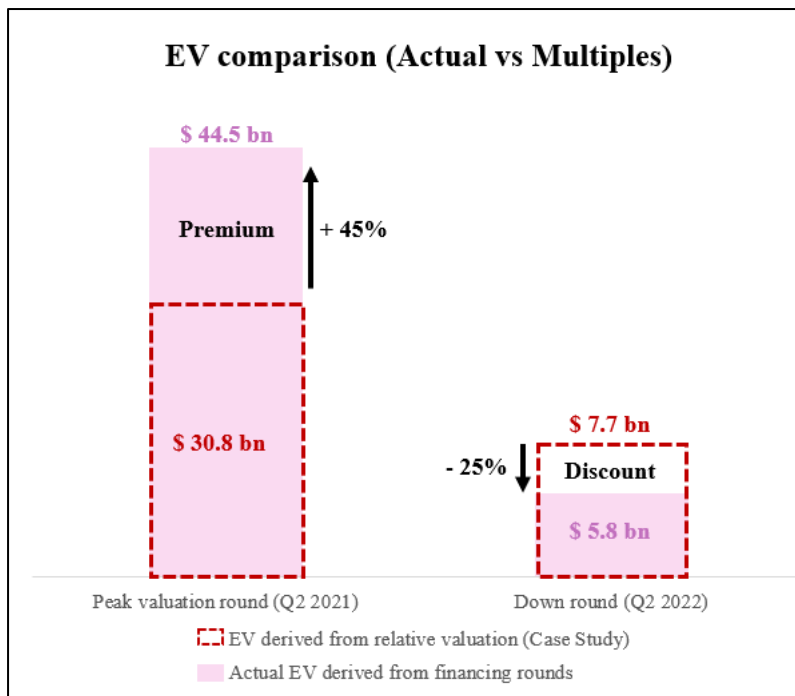
Source: Own illustration

Exhibit 26: Football Field – EV valuation including various scenarios



Source: Own illustration

Exhibit 27: Enterprise value comparison of actual values and EV/Sales values



Source: Own illustration

Exhibit 28: Calculation of enterprise values based on disclosed post money valuations

\$bn Financing round	Post Money Valuation	-	Amount raised	=	Equity Value = Pre Money Valuation	+	Net debt	=	Enterprise value
June 2021	45.6		0.64		44.96		- 0.45		<b>44.51</b>
July 2022	6.7		0.80		5.90		- 0.11		<b>5.79</b>

Source: Own illustration

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