Innovative Financial Services Through Fintech Start-Up

Abstract

India has a large untapped market for financial service technology startups – 40 percent of the population is currently not connected to banks and 87 percent of payments are made in cash. Over the past couple of years, the term FinTech has evolved from being a buzzword among technological savvy businesses to an organized sector characterized by hyper growth. Fintech refers to the scope of financial services that can be available on digital platforms. This new disruption in the banking and financial services sector has had a wide-ranging impact. FinTech is basically the amalgamation of finance and technology. According to the report of The National Association of Software and Services Companies (NASSCOM), India has a presence of around 400 companies in the fintech space, with an investment of about $420 million in 2015. The NASSCOM report also estimated the fintech software and services market to grow 1.7 times by 2020, making it worth $8 billion.[1] FinTech is not a replacement for traditional banking services; rather it is a result of the inevitable evolution of the banking space. Banking services are now being provided with the added convenience of technology.

Mohammad Arif
Assistant Professor,
Deptt.of Commerce,
Government Post Graduate College
Deoband, Saharanpur,
U. P.

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Introduction

A key element of the economic growth is innovative and inclusive financial services. The digital and technological revolution transformed business operations across all industries. Financial and banking sector is no exception for it. This is partly by harnessing new technologies, primarily the information and communication technology, more specifically the mobile technology.[2]

In particular, access to and use of a bank account, offering a minimum of basic transactions has become a key to increase economic growth rate of any nation. Banks have witnessed of significant changes in their outlook and have emerged as financial supermarkets offering a range of complex financial products and services, duly customized to the needs of their customers. On the product front, the innovations have led to emergence of complex offerings like swaps, derivatives and securitization, while on the other hand, the delivery channel is no more limited to brick and mortar branches, but has spread to modern, technology-driven channels like ATMs, mobile, internet and the social media. Technology has been used by financial institutions for more than half a century and it started playing a more critical role in the financial sector

India has a large untapped market for financial service technology startups – 40 percent of the population is currently not connected to banks and 87 percent of payments are made in cash. With mobile usage expected to increase to 64 percent in 2018 from 53 percent currently, and internet penetration steadily climbing, the growth potential for fintech in India cannot be overstated.[3]

Over the past couple of years, the term FinTech has evolved from being a buzzword among tech-savvy business executives to an organized sector characterized by hyper growth. FinTech is an industry comprising companies that use technology to offer financial services. These companies operate in insurance, asset management and payment etc.[4] It refers to the scope of financial services that can be available on digital platforms. Digital technology, and its avatar in the financial segment, is completely reinventing the way business has traditionally been done.

FinTech is basically the amalgamation of finance and technology. It refers to a new generation of companies that leverage cutting edge technology to offer financial solutions that are significantly more efficient and effective than those provided by traditional financial institutions. This new disruption in the banking and financial services sector has had a wide-ranging impact. The Indian government and regulatory institutions have in effect promoted an entrepreneurial rather than obstructive climate for fintech in India. However, policies and governance will need to match the speed of innovation in this sector to ensure secure and transparent growth.

India's financial technology (fintech) sector may be young but is growing rapidly, fueled by a large market base, an innovation-driven startup landscape, and friendly government policiesand regulations. The Indian fintech landscape is segmented as follows – 34% in payment processing, followed by 32% in banking and 12% in the trading, public and private markets.[5]

The latest surprise demonetization move has given a massive fillip to the FinTech sector.

FinTech is not a replacement for traditional banking services; rather it is a result of the inevitable evolution of the banking space. Banking services are now being provided with the added convenience of technology. Several startups populate this emerging and dynamic sector, while both traditional banking institutions and non-banking financial companies (NBFCs) are playing catch up.

Aim of te Study

Aim of this paper *is* to study the existing scenario of FinTech and how fintech startup ecosystem transforms the financial services. The paper elaborates impact of fintech on banking and financial services in India.

Fintech Startup Ecosystem in India

For instance, while traditional banks (around 100) and NBFCs (around 1100) in India use technology to simply calculate credit scores, fintech ventures use machine learning algorithms and alternative data points such as social media footprints, call records, shopping histories, and payments to utility service providers to increase efficiency and provide greater access to credit. Fintech has changed the traditional style of working and make them more transparent and easy to access.

Financial technology may still be in its early stages, but 2016 was nonetheless a whirlwind year for the FinTech world. And it's about to get even better. According to the annual FinTech Report, cumulative investment globally will exceed $150 billion in 2017.[6]

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NASSCOM predicts that India's fintech software market alone could touch US$ 2.4 billion by 2020, doubling on the current rate of growth. Fintech firms are breaking new ground in the formal finance sector through innovative and dynamic use of technology in the lending process.[8] India now ranks third among global startup ecosystems, and is expected to have more than 10,500 startups by 2020, providing employment to almost 2.1 lakh people. The startup wave and the huge investment (in excess of $5 billion in 2015) supports FinTech because this sector needs entrepreneurs who are open to innovation, are willing to experiment and are not tied to traditional ways of getting things done. Fintech investment continues to grow. After landing at $19 billion in total in 2015, global fintech funding had already reached $15 billion by mid-August 2016. The areas of fintech attracting media and investor attention are changing. Insurtech, robo-advisors, and digital-only banks are only a few of the segments making waves. B2B fintechs are also playing an increasingly prominent role in the ecosystem. It's not all good news for fintechs. Major hurdles, including customer acquisition and profitability, remain. As a result, many are becoming more willing to enter partnerships and adjust their business models. On the other hand, incumbents are enacting strategies to ensure they remain relevant. Many financial firms have woken up to the threat posed by fintechs and are implementing innovation strategies to stave off disruption. The relationship between incumbents and fintechs continues to evolve. Fintechs are no longer viewed exclusively as a threat, nor can they be ignored.

Fintech service firms are currently redefining the way companies and consumers conduct transactions on a daily basis. This is why global investments into fintech ventures have been increasing at record speed – tripling to US$ 12.2 billion in 2014 from US$ 4.05 billion in 2013, and reaching US$ 19.1 billion in 2015. In India, the scale has been much smaller but at similar growth rates – investment in India's fintech industry grew 282 percent between 2013 and 2014, and reached US$ 450 million in 2015.[9]

Government's Initiatives

Government policies in India are evolving quickly, providing a favorable backdrop for FinTech. By encouraging digitization, by promoting uniform and widespread identification (Aadhaar Card) and through bank account schemes, the government has taken several initiatives to boost the FinTech ecosystem. In short, FinTech ecosystem has a role to play in digital economy.

One of the major constraints faced by the people in getting linked to the formal financial system was the strict Know Your Customer (KYC) norms prescribed for opening bank accounts. To facilitate easy opening of accounts, especially for small customers, the KYC guidelines have been simplified to the extent that these accounts can be opened by way of a self-certification in the presence of bank officials. Further, RBI has allowed 'Aadhaar' the unique identification number allotted by UIDAI, GOI to be used as one of the eligible document for meeting the KYC requirement for opening a bank account.

The government is keen on a transition to a cashless economy because it could be cheaper to run, help reduce the underbanked population, and reduce financial crime as electronic payments are easier to track. Currently, Indian's financial inclusion penetration is extremely low, with as many as 145 million households not having access to banking services. However, the RBI's target is for the penetration to reach 90% by 2021. In September 2013, Banks are allowed to provide e-KYC services based on Aadhaar facility, thus paving the way for account opening of all epeople. It is reported that more than 817.8 million Aadhaar numbers have been issued by April 2015 and the number is still increasing[11].

FinTech can play a crucial role in financial inclusion. The push for financial inclusion from the Government helps FinTech lenders, as digital lending platforms can target customer segments that were previously underserved.[12]

A boost to the fintech sector could help another government policy succeed. The Indian government has been promoting digital finance for some time. Earlier this year, the Reserve Bank of India (RBI) launched United Payments Interface (UPI), a tool that allows users to access multiple bank accounts and merchant payments within a single mobile app.[13] The RBI recently set up a multi-disciplinary committee to study the fintech business in India. The goal is to understand the risks involved and emergence of new models, and assess how the banking system could then adapt and respond to them. The RBI has so far promoted the Unified Payments Interface and the Bharat Bill Payments System, as well as digital payments, P2P lending, and the use of automated algorithms to offer financial advice. Growth of the fintech industry, and increased use of fintech products, will only further drive the move toward a cashless economy. Initiatives by the RBI and parallel government efforts have focused on fostering financial inclusion. This has meant encouraging competition and innovation in India's nascent fintech sector on a more or less even playing field.

Fintech Startup and Its Services

There are a lot of key service offerings through fintech startup, some important of them are

Crypto-Currency

India being a more conservative market where cash transactions still dominate, usage of digital financial currency such as 'bitcoin' has not seen much traction when compared to international markets. There are, however, a few bitcoin exchange startups present in India – Unocoin, Coinsecure, and Zebpay.

Digital Lending

These companies provide flexible options for financing to SMEs and consumers. Example of such companies are Capital Float, Lendingkart, Indifi, NeoGrowth, etc[14]

Equity Funding Services

Such internet-mediated platforms are gaining popularity across the world as access to venture capital is often difficult to secure. This includes crowdfunding platforms that enable the funding of a project or business venture by raising funds from a large number of people. Examples include: Ketto, Wishberry, and Start51.

Insurance

FinTech has helped the insurance sector transform from being document-heavy to becoming paperless. Coverfox and Policybazaar are the example of such companies.[14]

Miscellaneous Software Services

Companies are offering a range of cloud computing and technology solutions, which improve access to financial products and in turn increase efficiency in day to day business operations. Examples include Catalyst Labs, AirtimeUp, ftcash, Profitbooks, StoreKey, and HummingBill.

Payment Services

These companies allow individuals and businesses to accept payments without even swiping a card. Payments are made online and the payer just needs a smartphone, without the requirement of a merchant account. PayTM, Freecharge, Oxygen Wallet and MobiKwik are among the top players in this space.

Peer-to-Peer (P2P) Lending Services

Companies use alternative credit models and data sources to provide consumers and businesses with faster and easier access to capital. P2P lending allows online services to directly match lenders with borrowers who may be individuals or businesses. Examples are Lendbox, Faircent, i2iFunding, Shiksha Financial, GyanDhan, and MarketFinance.

Personal Finance

Fintech companies are also growing around the need to provide customized financial information and services to individuals, that is, how to save, manage, and invest one's personal finances based on one's specific needs. Examples are FundsIndia.com, Scripbox, PolicyBazaar, and BankBazaar.

Point-of-Sale

Companies provide card swipe machines that enable customers to make cashless payments process easy. Mswipe, PineLabs, ICICI Merchant Services, etc are some of the larger POS machine providers in this space. [15]

Remittance Services

A few startup ventures are trying to address the gaps in remittance transactions as the current process is expensive. Inward and outward remittances can be complex, time-consuming and expensive. FinTech companies have made these transactions simple and affordable. Oxigen and Payworld are among the notable remittance platforms. These startups aim to disrupt the current monopoly held by firms like Western Union and MoneyGram. Examples are Instarem, FX, and Remitly.

Savings & Wealth Management

These companies help individuals save money as well as make and manage their own investments. Software helps to quickly compare different options so that they can make decisions. Scripbox and Funds India are to name a few.

Challenges and Opportunities for Fintech Expansion

While digital finance firms have benefited from the government's pro-startup policies, formal institutions possess an established infrastructure and legacy that is not easily replaceable. Fintech startups need to instill greater confidence among Indian customers, already known for being conservative in their financial preferences. Figuring out how to market to their needs and influence financial behavior are some of the biggest challenges, as is setting up a strong and responsive regulatory infrastructure to keep apace with the speed of technological innovation.

On the other hand, traditional banking and financial institutions can leverage their existing customer base and adopt digital products that nurture strong financial relationships while improving service efficiency and broadening access to meet changing needs. The disruptive potential of fintech firms can provoke the much needed modernization of the traditional sector, reducing costs in the process and increasing the size of the banking population.

Responding to these opportunities and challenges, banks like HDFC and Axis have launched mobile phone applications to ease digital transactions; Federal Bank announced a partnership with Startup Village to develop innovative banking products; U.K. giant Barclays is set to operationalize its fifth global fintech innovation center that will be located in India; and Goldman Sachs Principal Strategic Investments Group (GSPSI) is looking to invest in Bengaluru's fintech startup scene. Thus, the growth prospects in technological innovation may not necessarily produce a mutually exclusive relationship between traditional institutions and fintech firms in India.

Conclusion

Partnerships between FinTech companies and traditional banks clearly suggest that two entities needn't necessarily compete, but can co-opt. FinTech has bright growth prospects. One of the factors that could propel the growth further would be partnerships between this dynamic sector and the experienced traditional banking sector. Collaborations between the two can bring together the best of both worlds and offer unique products to a larger number of people in India. The FinTech sector has young businesses that need help in reaching their true potential. Incubators and accelerators can mentor these businesses and assist them in competing against the big players in an extremely challenging, cost-conscious Indian market.[16]

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