Fintechs: New Rival to Banks

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Abstract:
There has been 63% increase in venture capital investment in 2014 but funding for FinTech companies rises to 201% globally in same period (Accenture, 2015). FinTech refers to those enterprises which use information technology to deliver financial services to its customers. It is the aggregate of information technology and financial services. Inefficiencies in the existing financial system demanded a better and technologically advanced financial system which could cater to the needs of underserved customers of traditional banks. The rapid introduction and reach of new technology, particularly internet and mobile communications paved a way to the new innovative startups to fill this gap between traditional banks and their customers. These firms use information technology to provide their services. These fintechs focus on serving the unbanked and under banked. Since technology lower business costs, financial services can be given to the customers in more economic and effective way.

Keywords: *Fintechs, Financial system*

1. Objectives

The objectives of this article are to discuss about Fintechs, what comprises the Fintechs and the factors which lead to rise of Fintech corporations. The article discusses the effect of Fintechs on the existing banking system and explains how it creates disruption in the financial market. It compares the cost of the services of Fintech and Banks and examines which one is more cost effective. It considers the regulatory implications of its growth on the financial services market and the economy.

2. Introduction

There has been considerable increase in the number of innovative startups in India. According to an estimate, in 2014, population with active internet in India was 232 million of which 50-60% use mobile internet. With the rising popularity of internet, access to customers through internet has become easy. This lead to rise of startups offering their products and services through internet. One of them being FINTECH CORPORATIONS.

“Financial Services Technology Consortium” was started by Citigroup in early 1990s to expedite technological cooperation efforts. The origin of term "Fintech" can be related to this. However, investment in this sector by venture capitalist, demand for its services by consumers and regulatory considerations of regulators have increased manifold since 2014. FinTech refers to the use of information technology to deliver financial services to the customers. It is summing up of information technology and financial services.

According to census data, 41% of the population of India is deprived of banking services. Fintech is trying to capitalize on this gap left by the banks and are driving disruption within the financial services industry. These technologies not only enhances the efficiency of financial sector but also provides wider access to the banking and financial services to the customers.

Giants such as Apple and Google have also introduced their mobile payment apps- Apple Pay and Google Pay. Google is working with Verizon, AT&T and T-Mobile to get its Google Wallet payments app pre-installed on Android phones sold by these carriers.

3. Forms of Fintech

E-Payments

It involves real time transfer of money from one bank account to another in a safe manner through the internet. Payment of utility bills, booking of tickets etc. can be done in safe and secure manner through these platforms. Citrus, payumoney, freecharge are some payment platforms operating in India.

Wallets

It is an application that enables individuals to store their credit or debit cards and banking information on their mobiles, and use to make retail purchases, transfer money or other online payments such as mobile recharge, DTH recharge, bills payment. Paytm, mobikwik, oxigen are some wallet platforms operating in India.

Crowd funding

It means raising funds from large number of people in small amounts through online platform. Letsventure, wishberry, catapooolt are some crowfunding platforms operating in India.

4. Algorithm-Based Credit Underwriting

It involves computer analyzing the risk associated with a particular loan. It is more consistent, objective and cheap.

4.1 M-Insurance

Online insurance firms have also emerged. These firms in addition to insurance also provide better technological interfaces, telemedicine and real transparency in their services and provide innovative elements like free telemedicine, free generic drugs and online price comparisons. Policybazaar, coverfox, insuringindia are some insurance platforms operating in India.

4.2 Real Time Analysis through IOT Devices for Insurance

Internet of things (iot) -a slew of wearable devices can now be used for life and health insurance. US insurance companies are using sensors to determine the driving style of an individual for auto insurance.

4.3 Share Trading

There are online share trading firms which provide assistant in trading in stocks helps in choosing the the best deal. These charge lower brokerage rate from customers. Thus, customers get better services than the banks. Zerodha, finvasia, rksv are some share trading platforms operating in India.

4.4 Social Scoring

It involves assessing the credit risk of an individual using social media. It can work as complementary to their standard background checks.

4.5 Digital Currencies: Bit Coins and Block Chain

Money which is stored in a digital or electronic register is called Digital Currency. It may or may not be exchanged for fiat currency. Cryptocurrency is a programmable Digital Currency that relies on cryptography for chaining together digital signatures (maintaining a electronic ledger) of token transfers. Bit coin is a form of decentralized digital money created by an algorithm and the block chain is the database technology that maintains all records. Thus, it prevents counterfeiting.

4.6 P2P Lending

P2P sites are those platforms that connect individual borrowers to lenders. Faircent, i-lend, lendbox are some P2P lending platforms operating in India.

4.7 AI Based Financial Planning

Artificial intelligence is used in the financial planning of customers. It devises portfolios which suits best to the risk preference of customers. It studies the present and future trends in stock and bond prices and chooses the best investment opportunity.

4.8 Causes of Rise of Fintechs

Banks have always been biased against rural areas as serving rural and poor areas are costly affair. They find it unattractive to invest on infrastructure and staff employees in rural areas as same investment can be more fruitful in urban areas. Average Branch penetration in India is only one branch per 10,000 people.

Global crisis bought with it new regulatory reforms. Capital to asset ratio for banks has been increased to bring market stability and enhance their risk-absorbing capacity. This diverted money from SMEs. Now, SMEs or private individuals have to move to P2P lending platforms to cater their need for money.

Financial sector in India has been unable to serve the customers for their financial services need. It is yet under-penetrated and the service level has been low. Government is encouraging entrepreneurship to achieve social objectives of providing employment to youngsters and reducing wealth and income inequality. And technology can be a helpful hand in it. Growth of digital population has stimulated the growth of Fintechs. Number of customers with Internet has multiplied over the last few years. Increasing density of mobile internet has driven the growth of E-commerce. Smartphone has reached approximately half of the banked population. Start-ups now have become part of the culture. Entrepreneurs have started risk taking and are bolder to face the consequences. There will be immense growth in finance in less regulated developing countries such as India. Fintechs are based on the principle of LASIC principles whose five factors are: Low margin, Asset light, Scalable, Innovative, and Compliance easy. All these factors favor Fintechs and are in line with it.

5. Advantages

Fintechs do not require huge investment in infrastructure and in large employee base. Therefore, they can offer their products and services at a lower cost and with the help of information technology can provide better quality financial services. They can offer better deals to the parties dealing on their platform. Their working hours are not limited to eight hours a day i.e. from 9am to 5pm. They sell their services even after usual banking hours. They can use data or information from social media to assess the creditability of individuals and business firms. Business of Fintech firms are less geographically concentrated, they use diversification as a risk reducing technique. Most Fintech firms match borrowers and lenders directly in term of maturities thus reducing their liquidity risk.

According to World Bank, India has received remittances from its migrant workforce of around US $72 billion in 2014, being highest in the world. This is expected to grow 2.5% up in 2015 from 0.6%in 2014. But the cost of sending remains high to 7.7% globally. This high cost is due to the FX spread i.e. the difference between interbank currency conversion rate and rate quoted to the customer by bank, which is more than five billion US dollars. Startups are looking at this gap. Instarem which remitted money from Australia has transferred A$2 million (US$1.43 million) in September 2015. It charges flat fee of 1% of amount transfered which is significantlly lower than 2 to 3 percent charged by bank. (techinisia)

60% Indian population are unbanked and 90% of small business do not have access to financial institutions as against 80% of Indian population have mobile phones. The Indian government is promoting financial inclusion as well as cashless transactions. Fintech firms can be a medium to financial inclusion. (Village capital). Some examples of Fintechs are as follow-

Airtime Up- Through this platform, village retailers can provide mobile top-ups and other services in a cost effective manner to village farmers.
Catalyst Labs- It provides a secure platform to bulk buyers and farm producers to congregate.
VC Circle- It is business information website which provides online business news, data, events and training for private equity and venture capital fund managers, entrepreneurs and investment bankers.
Fine Train- It provides access to institutional finance to small businesses and other information about local business environment.
Ftcash- It provides a platform to micro merchants to offer great deals to their customers.
Gyandhan- It enables education financing to deserving students and provides access to detailed information on scholarships.
Humming Bill- It is a platform to sell subscription products and services
Kyash- It is a secure method to collect payment throughout India
Market Finance- It provides a platform to enable small and medium sized business get loans by connecting them to multiple banks.
Profit books- It is online accounting and payroll management software for non-accountants for small business.
Shiksha Finance- It facilitates education loan to students and loan to educational institutions for infrastructure.
Vote for cash- It is a P2P online market place where loans are provided based social score without collateral or guarantor.

6. Threat to Brick and Mortar Banks

Increasing number of Fintechs is itself evidence against brick and mortar banks that they are going to create a disturbance in the market of financial services. Fintechs are going to cut customers from these banks. Banks will be forced to reduce their profit margins. Furthermore, there are no specific regulations governing these businesses. They don't have any such legal boundations. They are taken as any other e-retail business offering their service through internet. This gives them immense power to fight against banks.

Fintechs provide financial services to customer through use of information technology. With the regular upgradation of technology, these businesses are in better position to serve the customers than the banks. They provide their services in more effective and efficient manner than its competitor. They use data from customers' presence on internet- shopping pattern of customers, online footprints, and academic record. These businesses have lower cost of borrowing which in turn they transfer to its customers in the form of lower costs.

However, existing banks are old players of this market and have better understanding of different situations of the market. They can relatively easily handle adverse situations. In addition, these are financially strong business units with huge fund at their disposal to cater their needs as the time demands and they can use their financial power to create a barrier for these Fintechs. Existing banks enjoy the trust of the customers as they are serving them from a long time. While Fintech have to gain customers confidence and break up their loyalty towards existing banks. Though the cost of switching from existing banks to Fintech is low, but it can have some influence on customer's decision. Customers are going to judge the services of Fintechs against those of banks to decide whether to sift to Fintechs or not. Furthermore, internet platforms are prone to hacks and because of this reason a large number of customers are not quite confident about it. Fintechs have to win over the confidence of customers regarding the security of their sensitive data.

Mobile money has created a ground for offering their products for Fintechs. Even it is the reason for establishment of many Fintechs as their whole business model is based on it such as health and life insurance premium paid by prepaid airtime, opening online saving accounts for non-banked customers, offering small business and personal loans, and trading in securities through mobile phone.

7. Conclusion

There is a large population in India who are unbanked and others who are underserved by existing banking system. This is an exciting business opportunity for FinTech to serve these customers. Fintechs use information technologies to lower their operating cost which can be passed on the customers in the form of lower operating costs for merchandise businesses and lower transaction costs for consumers. They can offer short term credit to consumers who cannot furnish the documents asked by banks but are willing to pay back the loan by using other information such as social media to assess their creditability; provide a platform where lender and taker can meet directly; offering microinsurance and online insurance by risk profiling using similar data.

Fintechs can collude and collaborate with telecommunication services providers to offer cost effective and better services to its customers. Fintechs will increase the financial inclusion of those deprived of banking system and decrease inequality of opportunity.

Since Fintechs are involved with money transactions, a proper legislation is needed for its regulation and effective working. Regulation should be in a manner that it does not prove to be a hindrance in its long term development. Regulators have to take into consideration the potential risk involved in Fintechs i.e. maintaining market stability and customer protection.

Digital disruption created by Fintech will force banks to evolve into better customer friendly organization. Now banks will have a new technically sound competitor, they will have to upgrade themselves technically to provide better and effective services to the customers. They can even follow or copy business model of Fintechs and offer their services using information technologies. Most banks have started offering their services through specially designed apps. But Indian customers need guarantee regarding the safety of transactions and their personal and sensitive data. Fintechs and banks both have to build the confidence of customers in online financial transactions. Fintechs will bring competition in the market and competition brings efficiency yielding benefit to customers and the economy. It is not the Digital India campaign of the government which force the banks to offer services through digital system but the disruption created by these Fintechs.

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