International Research Journal of Business and Social Science

Volume: 10 Issue: 1
January-March, 2024
ISSN:2411-3646

KMF Publishers

http://irjbss.net/

INTERNATIONAL RESEARCH JOURNAL OF BUSINESS AND SOCIAL SCIENCE
Volume: 10, Issue: 1, 2024

DOI: https://doi.org/10.5281/zenodo.10896530

Article

KMF Publishers
http://irjbss.net/
OPEN ACCESS

Fintechs and Sustainable Development – Indian Scenario

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ABSTRACT

Fintechs have emerged as catalysts for innovations in the financial sector with the use of technology to improve efficiency in providing diverse financial services. The fintch revolution has disrupted financial systems by opening up new opportunities. Fintechs are enablers for sustainable finance as well by incorporating technological innovations such as artificial intelligence, blockchain technology, big data, etc. among others. As there is growing recognition to promote sustainable development all across the globe, fin techs are significantly contributing towards sustainable finance by ensuring green finance, reducing cost, promoting efficiency, valuing nature's assets, and providing sustainable finance. Fintech in India is the third largest in the world after China and USA. The growth in fintech innovation contributes towards the green development of the economy. In this perspective, the present paper focuses on the role and relevance of fintechs in promoting sustainable finance. with special reference to India in the light of challenges and prospects.

ARTICLE HISTORY
Received 7 January 2024
Revised 21 February 2024
Accepted 26 March 2024

KEYWORDS
Fintechs, Sustainable Finance, Innovation

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INTRODUCTION

Digital transformation is reshaping the financial services industry. Financial technology supports growth and poverty mitigation by strengthening financial development, inclusion, and efficiency and by providing the financial services that are required for the digital economy to flourish. The growth of fintech implies the designing and provisioning of financial services by using new technological innovations, is one of the most significant developments in the financial sector in the past decade (GOI, 2019). The digitization of financial services provides opportunities to build more inclusive and efficient financial services and promote economic development. Fintech is transforming the financial sector landscape rapidly. The Indian fintech landscape is one of the most exciting digital financial ecosystems today. With more than 2,100 fintech companies and startups, India's fintech industry valuation is estimated to go beyond $150-160 billion by 2025(Economic Times, 2022). India is transitioning into a dynamic ecosystem offering fintech start-ups a platform to potentially grow into billion-dollar unicorns. From tapping new segments to exploring foreign markets, fintech start-ups in India are pursuing multiple aspirations (KPMG, 2016).

The major catalysts for FinTech adoption in India are the digital-savvy population with high internet penetration, the ability to target and service niche customer segments with tailored products, and a supportive regulatory landscape. The digital infrastructure has created new opportunities for many of these growing FinTech startups. The COVID-19 pandemic has led to an inevitable surge in leveraging digital technologies. Consumers have not only dipped their toes into the online world but have also taken the plunge to integrate digital into their lifestyles. The adoption extends beyond the consumer space as well. Micro, small, and medium-sized enterprises are increasing the use of FinTech services. These businesses constitute a distinct customer segment, with needs that differ from those of consumers and large corporations.

India's digital economy is expected to witness exponential growth to $800 billion by 2030 on the back of digital public infrastructure, the development of UPI, and the COVID-19 pandemic. RBI's recent 'Payments Vision 2025' will boost the digital payments drive, which targets to increase the number of payments by more than 3x by 202534 and target to increase the number of registered users for mobile-based transactions at a CAGR of 50% by 2025. The recent budget announcements are encouraging steps toward using technology to tackle financial inclusion. While more details on the regulatory approach are awaited, the ecosystem is poised to build a new face of banking in India. The future of digital banking is thus promising. As the Indian FinTech and digital FS adoption mature, the increased collaboration between banks and FinTech would lead to massive growth in the banking industry. It would enable banks to become more agile in their functioning and respond to shifting customer needs by embedding partner solutions into their programs while lowering their capital investment requirements and software development risk. FinTech would also benefit from this arrangement through a larger client base and improved market credibility (EY, 2022 Feyan et. al., 2023).

Fintechs – Global Scenario

Fintech refers to the advances in technology that have the potential to transform the provision of financial services spurring the development of new business models, applications, processes, and products (IMF and World Bank, 2019). Digital technology is reshaping financial services significantly owing to the internet and mobile technology. Enhanced connectivity has eliminated barriers and reduced costs for information transfer and remote interactions.

The World Bank Global Findex data show that global financial account ownership grew from 51 percent of the adult population in 2011 to 76 percent in 2021. Access to basic financial services results in better growth of small businesses and improves the lives of the poor. Technology reduces transaction costs by overcoming geographical access barriers; and increasing the speed, security, and transparency of transactions. Therefore, countries should embrace fintech opportunities and execute policies that enable and encourage safe financial innovation and adoption. Major FinTech trends that emerged globally are embedded finance, PayTech, e-commerce growth, Insurtech, and Wealthtech. From payments to investments and lending, embedded solutions are penetrating every aspect of financial services. Digital payments have become a critical enabler of e-commerce sales, supporting the expansion of businesses small and large to new customer segments and new global markets. An organic and collaborative ecosystem drives digital adoption, supported by key government initiatives. Quick adoption of emerging technologies is an enabler for the growth of tailored product offerings and FinTech initiatives.

Globally, an estimated 770 billion digital payments were made in 2020 (Capgemini Research Institute, 2021). Mobile money transactions alone numbered 41 billion, representing a total transaction value of US$767 billion across 300 million active mobile money accounts (GSMA, 2020). Sub-Saharan Africa accounted for the bulk of mobile money transactions in 2020—27.4 billion transactions, amounting to US$490 billion across 159 million active mobile money accounts (GSMA, 2021b). The volume of digital payments is growing at around 11 percent a year globally and at much higher rates in emerging markets and developing economies (EMDEs) (Capgemini 2020). Providing credit through digital channels and using data-driven underwriting and risk management have been important fintech applications. The flow of digital credit was estimated at almost US$800 billion globally in 2020, with Big Tec lending platforms representing 70 percent of this lending volume (Cornelli et al., 2020; Cornelli et al., 2021).

Digital lenders use enhanced reach and data analytics to increase access to finance to individuals and small and medium enterprises (SMEs) that had been previously excluded for lack of proximity to a branch or lack of credit history. Embedded finance providers ranging from e-commerce and logistics platforms to consumer goods distribution networks can leverage transactional data on orders, inventory, sales, or receivables to provide working capital. The interplay of technology, market forces, and policy will also influence the inclusiveness of market outcomes. Mobile connectivity is very high for low- and middle-income countries. but an estimated 600 million individuals in these countries lack internet access, and broadband affordability is a barrier for many more (World Bank, 2021).

Further, digital business models can drive down costs so that even small markets offer sufficient scale for a provider to be viable; however, such providers may have difficulty competing with cross-border entrants that can offer services remotely and leverage larger markets to achieve scale and scope economies.

Indian Scenario

Indian FinTech ecosystem has emerged as a formidable global force and continues to grow as one of the largest FinTech markets globally. One of the best digital payments ecosystems in terms of value and volume, phenomenal growth in the consumer and SME digital credit access, and towering participation of the retail investors in the stock market are testimonials that Indian FinTech companies are on the right trajectory.

The major catalysts for FinTech adoption in India are the digital-savvy population with high internet penetration, the ability to target and service niche customer segments with tailored products, a supportive regulatory landscape, and the growth of MSMEs. The digital infrastructure has created new opportunities for many of these growing FinTech startups. The COVID-19 pandemic has led to an inevitable surge in leveraging digital technologies. Consumers have not only dipped their toes into the online world but have also taken the plunge to integrate digital into their lifestyles. The adoption extends beyond the consumer space as well. Micro, small, and medium-sized enterprises are increasing the use of FinTech services. These businesses constitute a distinct customer segment, with needs that differ from those of consumers and large corporations. India's digital economy is expected to witness exponential by 2030 on the back of digital public infrastructure.

The dynamic and accelerated development of a payments ecosystem, facilitated by increased adoption of technology and innovation, supports not only the growth in digital payments but also the availability of safe, secure, innovative, and efficient payment systems. Adoption of digital payments was growing before the onset of the pandemic, but the steps taken by RBI along with additional thrust provided by the pandemic have accelerated the shift, leading to a dramatic increase in contactless and online payments.

Further, Digital payments FinTech has been the highest funded and pioneer of the FinTech revolution in India. As per RBI, overall Indian digital payment by volume stands at 72 billion as of FY21-22, with an overall transaction value of INR 1,744 trillion ($24 trillion). Riding on the back of growing acceptance of existing digital modes and novel payment offerings such as UPI, BBPS, and Buy-Now-Pay-Later schemes, the value of digital payment transactions in India is set to increase by more than 3 times by 2025.RBI's 'Payments Vision 2025' aims to curb the volume of cheque-based payments to less than 0.25% of the total retail payments49. It will also target increasing the number of registered users for mobile-based transactions at a compounded annual growth rate of 50% by 2025. Additionally, with UPI and RuPay's internationalization, India will be an undisputed global leader in payments. Linking credit cards to UPI is another game changer. Consumers are increasingly expecting an invisible payment experience, and payment players must adopt technology to provide it. To meet these expectations, payment service providers are leveraging zero-touch payments. In its vision for 2025, RBI also intends to create a new system for processing payments via the Internet and mobile banking services. Currently, the companies route these services through payment gateways and other aggregators. Payment apps use one or a combination of new technologies enabling secure yet faster and convenient payment systems. While RBI's guidelines around security systems ensure companies meet or exceed the common standards, the new-age tech adoption ensures a competitive edge in the market. In the wake of increasing cyber risks, there is a need for the regulatory push for multifactor authentication, consumer data protection, infrastructure resilience, scalability of systems, and dispute resolution mechanisms in the next few years. It is important to highlight that while agile FinTech players find it easy to partner with third-party tech vendors to integrate new technology, payment apps launched by banks would need to keep their technology stack open for such integrations.

However, fintech-related risks are similar in nature to those of traditional financial activities, but their shape and materiality can differ significantly. Mitigating risks to core policy objectives—such as financial stability, integrity, and safety—is a precondition for reaping the benefits of fintech adoption. All forms of financial services provision ultimately may give rise to, among other things, liquidity, credit, market, and operational risks at the micro-prudential level and risks from system-level externalities at the macroprudential level. The digital transformation causes these risks to present themselves in different ways and could also trigger risk migration outside of the regulatory perimeter. As such, several interrelated and heightened challenges stand out in several areas—challenges that will continue to evolve as the industry develops. Owing to economies of scale, network effects, reputation, and capital, large providers such as Big Tech companies could achieve dominant positions quickly, thereby raising entry barriers and reducing overall competition or contestability. Market dominance by a limited number of providers could reduce consumer welfare. However, in a market where competition is limited, the entry of large providers could have important welfare gains and enhance competition in the short to medium term. Financial services have been offered by new entrants that largely operate outside of the regulatory perimeter, although their activities and risks are similar in nature to those offered by regulated entities. Similarly, decentralized systems, such as crypto-assets and peer-to-peer or decentralized finance platforms, may prove more difficult to regulate and supervise if a central governing body is absent. Given the supranational nature of some fintech solutions, cross-border arbitrage opportunities complicate matters further and call for more international coordination.

CONCLUSION

In light of the fast-evolving landscape and rapid spread of innovations from market to market, adopting an enabling approach to support responsible fintech innovation and adoption is critical. Authorities must be proactive, pragmatic, clear, and collaborative with public and private stakeholders to promote trust, innovation, and investment, particularly since fintech issues cut across financial prudential supervisors, market conduct and competition authorities, and consumer protection agencies. In addition to strengthening policy frameworks, public authorities might need to consider structural alternatives like central bank digital currencies.

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