FINANCIAL INCLUSION: THE ROLE OF FINTECH AND DIGITAL FINANCIAL SERVICES

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Abstract

The cashless transaction system is achieving its growth day by day, as soon as the market becomes globalized and the development of the banking sector more and more the people moves from cash to a cashless system. The cashless system is not just a necessity but also a need of today’s order. Over the past few years, efforts to drive financial inclusion in India have delivered mixed results. Access to bank accounts has increased dramatically, driven by a strong policy and regulatory push. However, the usage of these accounts and the uptake of formal financial services beyond savings accounts have remained exceptionally difficult. The recent initiatives by the Government around demonetization and the move to cashless transactions will further drive innovation and new entrants into the Industry. The amendments to the banking act clearly demonstrate the Government, RBI and Banking institutions intent to ensure stable growth of the economy by ensuring a healthy BFSI. Building Trust within the industry will be paramount to India’s further growth. Newer technologies pose different challenges to the banks and regulators, with security being a key concern. With cyber-frauds on the rise, the regulators and the bankers would have to come together to ensure control mechanisms are in place. A strong push from the Government of India has given the non-banking population easy access to financial products. Payment organizations have demonstrated the advantages of mobile-led solutions and the traditional banking organizations are now trying to make inroads into rural India by launching innovative mobile-based banking solutions. With support from the government, large technology companies are using new ways of reaching out to the rural masses and educate them about the various financial products, thus ensuring that their hard-earned income is rightly invested.

Keywords: Financial Transactions, Digital Apps, Rural Population.

INTRODUCTION

FinTech is an umbrella term coined in the recent past to denote technological innovation having a bearing on financial services. FinTech is a broad term that requires definition and currently regulators are working on bringing out a common definition.
With the progress of the Indian economy, especially when the focus is on the achievement of sustainable development, there must be an attempt to include the maximum number of participants from all the sections of the society. The lack of awareness and financial literacy among the rural population of the country is hindering the growth of the economy; a majority of the population does not have access to formal credit. This is a serious issue for the economic progress of the country. In order to overcome such barriers, the banking sector emerged with some technological innovations such as automated teller machines (ATM), credit and debit cards, internet banking, etc. Though the introduction of such banking technologies brought a change in the urban society, a majority of the rural population is still unaware of these changes and is excluded from formal banking.

FinTech is a new term and has been gaining popularity since early 2015. This term is usually confused for being a strictly technological and tech-savvy term. When in reality this term is the merger of financial services provided by various clients with the developments and advancements in the technological arena.

The basic point is that FinTech developed more as a necessity out of the developments in the areas of financing services and the rapid growth of the technology that due to the need of such services. The merger of technology with financial service here means that various applications and platforms are being built and developed to provide you with an ease of using financial services including applying for business loans, online personal loans, etc. easily.

REVIEW OF LITERATURE

Development Research Project (2013)\(^1\) attempted to understand the financial needs of poor in long-term and short-term by exploring, how the surplus fund is used to meet short-term, long-term and emergency requirements to develop strategies for financial inclusion and designing financial products. The rural households follow their own strategies of cash management for their daily expenditure and thereby taking advantage of this, several informal financial institutions and instruments are serving this section of society. In this context, the report examines 107 households of Ernakulam district in Kerala, as was suggested by the RBI. The aim of the study was to understand the nature of the cash flows and outflows of a sample of poor households in the district. The project also analyzed the cash flow management strategies of the poor households. Further assessment was done to analyze the structure of the financial assets and liabilities of the poor households. The project focuses on the saving patterns of the poor households and examined factors responsible for the extent of dependence of the poor on formal and informal financial instruments/institutions for savings and credit. Two methods were used in this project for collecting data. First, the sample of poor household using questionnaire and is keeping a track using financial diary method of the same sample. Second, the analysis provided emphasis on rural and urban

CRISIL (2013)\(^2\) measured the extent of financial inclusion in India in the form of an index. It makes use of the non-monetary aggregates for calculating financial inclusion. The parameters used by the CRISIL Inclusix took into account the number of individuals having access to various financial services rather than focusing on the loan amount. The three parameters of the index were the
branch, deposit and credit penetration. These parameters were updated annually and based on the availability of data; additional services such as insurance and microfinance were added. The key findings of the report were as follows: one in two Indians has a savings account and only one in seven Indians has access to banking credit; CRISIL Inclusix at an all-India level stood at a relatively low level of 40.1 for 2011 (on a scale of 100). In short, CRISIL gave ground-level information regarding the progress of financial inclusion in the country’s rural and urban areas.

RBI (2014a) 3 focused on the provision of Financial Services to small businesses and low-income households. Among the main motives of the committee included designing principles for maximum financial inclusion and financial deepening and framing policies for monitoring the progress in the development of financial inclusion in India. Thus, in order to achieve the goal of maximum financial inclusion and increased access to financial inclusion the committee proposed the following measures: provision of full-service electronic bank account; distribution of Electronic Payment Access Points for easy deposit and withdrawal facilities; provision of credit products, investment and deposit products, insurance and risk management products by formal institutions.

The main findings of the report highlighted the following key issues. First, the majority of the small businesses were operating without the help of formal financial institutions. Second, more than half of the rural and urban population did not have access to the bank account. Third, savings in terms of GDP have declined in 2011-12. To address these issues, the Committee recommended that each individual should have a Universal Electronic Bank Account while registering for an Aadhar card. The committee also proposed for setting up of payments banks with the purpose of providing payments services and deposit products to small businesses and low-income households. In addition, banks should purchase portfolio insurance, which will help in managing their credit exposures. Further, the Committee recommended for setting up of a State Finance Regulatory Commission where all the state level financial regulators will work together. For the interest of the bank account holders, the committee recommended for the creation of Financial Redress Agency (FRA) for customer grievance redress across all financial products and services, which would coordinate with the respective regulator.

RBI (2014b) 4 presented a report to study various challenges and evaluate alternatives in the domain of technology that can help the large-scale expansion of mobile banking across the country. The report divided the challenges into 2 broad categories – Customer enrollment related issues and Technical issues. Customer enrollment related issues include mobile number registration, M-PIN (mobile pin) generation process, concerns relating to security as a factor affecting on boarding of customers, education of bank’s staff and customer education. On the other hand, technical issues include access channels for transactions, cumbersome transaction process, and coordination with MNOs (Mobile Network Operators) in a mobile banking eco-system. The report has a detailed comparison of four channels of mobile banking - SMS (Short Message Service), USSD (Unstructured Supplementary Service Data), IVRS (Interactive Voice Response System) and Mobile Banking Application, and evaluates each one of them based on accessibility, security, and usability. To resolve the different problems identified, the report suggests developing a common mobile application, using SMS and GPRS channels, for all banks and telecom operators. The aforementioned
application should enable the user to perform basic mobile banking operations such as enquiring his/her account balance, transfer and remittance of money. The application is expected to be developed in such a way that it provides a simple menu driven, interactive interface to the user. Such an application can be developed by the combined efforts of telecom operators and banks. The application can be embedded on all new SIM cards so that any person buying a new card has a pre-installed application. For customers already using SIM cards, the application can be transferred “over the air” (OTA) using a dynamic STK (SIM Application Tool Kit) facility.

OVERVIEW OF THE INDIAN FINTECH MARKET

The Indian FinTech market has been on an upward growth trajectory over the last five years. This is evidenced by an increase in both the number of FinTech companies founded and the investment they have attracted. From January 2013 to October 2018, approximately 2,000 FinTech companies have been Founded, turning India into a hotbed of entrepreneurial activity (Figure 1). This has also translated into increased consumer adoption of FinTech solutions. In 2018, India ranked second globally in the FinTech adoption rate. The average percentage of FinTech users in the country is 57.9%, behind China’s 83.5%, and much higher than developed countries’ 34.2%. With a strong technological ecosystem as its backbone and a huge market base with a low penetration of financial services (FS), the Indian FinTech market holds immense potential.

The overall transaction value in the Indian FinTech market is estimated to jump from approximately USD 66.1 billion in 2019 to USD 137.8 billion in 2023, growing at a CAGR of 20.18% (Figure 2). The global FinTech market is also poised to achieve high growth levels in the coming years. The overall transaction value in the global FinTech market is predicted to grow from around USD 5.49 trillion in 2019 to USD 9.82 trillion in 2023, a CAGR of 15.64% (Figure 3).
This report comprises three sections. Section 1 provides an overview of the Indian FinTech landscape by exploring the underlying factors driving its growth, key FinTech segments, and challenges faced by the FinTech ecosystem. Section 2 focuses on the key ‘emerging technological’ trends that are transforming the FS sector, and section 3 presents our recommendations for furthering India’s FinTech growth story.
This exceptional growth in global funding was primarily driven by the North American and Asian markets, as deal activity increased across all continents, barring Europe (Figure 7). The US retained top position, with 659 deals totaling approximately USD 11.89 billion, an annual high both in terms of the number and size of deals. However, Asia, driven by China and India, remains well-positioned to unseat North America as the primary market for global funding.

**Figure 5: Asia emerges as the largest FinTech target market for funding in 2018**

**Government Schemes:** These include the Jan Dhan Yojana, Digital India program, and Aadhar’s Unique Identification system that have provided important enabling platforms for technology innovators. In addition, e-governance systems promoted by the current government facilitate transparency by removing the involvement of intermediaries. The removal of surcharges on electronic transactions, tax benefits for consumers and businesses using e-payments, and changes in authentication requirements are other examples of the government’s efforts to encourage the growth of a FinTech ecosystem in India.

**Statement of the Problem:**
Although India has been rising to match the other countries with their FinTech developments, it is clear that India is quite behind when compared to them. India has a huge market for growth in this sector. However, there are many factors, which make it hard for the FinTech sector in this country to rise and be equal to the more developed markets and economies. Although India has a huge population, which favors the growth of the new and budding FinTech sector, the economy and the present scenario of the country is not favorable for its growth. The major difference between the global FinTech sector and the Indian industry is the presence of various factors that hamper the growth of FinTech in India, as discussed earlier: India may be able to stand shoulder to shoulder with the more developed economies when all these factors as mentioned will begin to disappear. The primary requirement for any FinTech start-up to settle will be a consumer base, a high internet penetration, and more minds to work on the project.

- Low Internet Penetration
- Bank Accounts
- An absence of Hardware and More Hands
- Lack of Funds
According to McKinsey, a substantial majority (about 75%) of FinTech lenders are focusing on retail banking, lending, wealth management, and payment systems for MSMEs. The numbers look promising despite the ineligibility for classification as direct or indirect finance to MSE sector that takes all such loans to NBFCs out of the ‘priority sector classification.’ It isn’t surprising then that MSMEs are turning away from traditional, collateral-chasing banks. Even the investor sentiment is positive vis a vis the touted success of FinTech.

**OBJECTIVE OF THE STUDY**

- To know the level of usage of FinTech services.
- To examine the digital banking service usage customers.

**RESEARCH DESIGN**

**Sources of Data**

The data collected for the study is primary and secondary. The study is based on survey method. The Convenience Sampling Technique has been adopted in selecting the respondents for the study. Accordingly, 30 respondents having bank accounts in public and private sector banks have been interviewed and the data were collected for the study. The required data for the study were collected and compiled from the RBI Website World Bank and Global Database were extensively used for the study. Different news articles, books and authorized internet sources were used which were enumerated and recorded and status of financial inclusion over past few years.

**RESULTS AND FINDINGS:**

**India overtakes China in FinTech funding in Q1 2019 and ties up with China in FinTech deal count in Q1, 2019:**

VC-backed FinTech deal count in India and China (USD million), Q1 2019

![Graph showing VC-backed FinTech deal count in India and China (USD million), Q1 2019](image-url)
India overtook China as Asia’s top FinTech funding target market with investments of around USD 286 million across 29 deals, as compared to China’s USD 192.1 million across 29 deals in Q1 2019. The massive slump witnessed by China in this quarter could partly be attributed to its Government’s concerted efforts to rein in the risks associated with the mushrooming of its peer-to-peer (P2P) lenders.

**Number of mobile internet users crosses the 500 million mark:**
Number of mobile and internet users in India

![Diagram showing number of internet users](image)

Over the last decade, there has been a significant rise in access to and speed of the internet (approximately 520 million mobile internet users) across the country. This is a prerequisite from an infrastructural standpoint to access FinTech services. In addition, the cost of internet usage has dropped significantly in the past five years, resulting in an increase in the number of internet users. This, in turn, contributes to FinTech adoption.

**UPI transactions cross INR 1 trillion in value in Dec 2019**

**Growth of the UPI platform**

<table>
<thead>
<tr>
<th>November 2016</th>
<th>November 2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of banks on UPI</td>
<td>21</td>
</tr>
<tr>
<td>No. of Transactions on UPI</td>
<td>0.3 million</td>
</tr>
<tr>
<td>Value of Transactions on UPI</td>
<td>billion INR</td>
</tr>
</tbody>
</table>
The launch of UPI by the National Payments Corporation of India (NPCI) has resulted in the roll-out of interoperable payment services amongst FinTechs and incumbent institutions, leading to the widespread adoption of digital payments across merchants and customers. The platform was used by 92 banks and witnessed 620 million transactions worth INR 1 trillion in November 2019, making it one of the largest payment platforms across the world.

Payments and alternative lending segments attracted the maximum funding in India in 2018

In 2018, the Indian FinTech market received total VC/private equity (PE) investments of approximately USD 1.83 billion across 165 deals. Payments accounted for the largest share with USD 709 million across 21 deals, followed by alternative lending with USD 530 million across 67 deals, mirroring global trends (Figure 12). InsurTech and WealthTech emerged as the next best funded FinTech segments in 2018.

Payments have been at the forefront of India’s digital revolution, with digital payment transaction volumes (worth USD 3.5 trillion) touching approximately 24.13 billion in 2018. The demonetization drive launched in November 2016 and lucrative returns on mobile wallets and UPI transactions (which led to their widespread adoption) have been key to driving exponential growth in digital transactions.
In addition, the rise of digital commerce, innovation in payments technology using AI, blockchain, the Internet of Things (IoT) and real-time payments; and the introduction of mobile point of sale (POS) devices have led to a reduction in the cost of acceptance infrastructure and also contributed to growth.

**Tokenization enhances security without hampering the customer experience:**

In an age where digital transactions are booming, the security of customers’ payment data has become extremely crucial. In light of this, card tokenization is slowly gaining popularity in India. Tokenization is the process of replacing sensitive information like card/account details with a random value that is provided by the bank in the form of a token. During the transaction, it is the
value on the token that is exchanged and not the user data. This ensures that merchants cannot store customer data, thus reducing the chances of fraud. With the RBI releasing a circular permitting its use in select use cases, tokenization is set to play a crucial role in securing payments in the country.

The respondents included in the users are 19 male and 11 females. Majority of them are qualified to business and below. As few as 5 male and 3 females are graduate (Table).

<table>
<thead>
<tr>
<th>Digital Banking users classification of respondents</th>
<th>Male</th>
<th>Female</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>None</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Business</td>
<td>10</td>
<td>8</td>
<td>18</td>
</tr>
<tr>
<td>Graduation</td>
<td>5</td>
<td>3</td>
<td>8</td>
</tr>
<tr>
<td>Office</td>
<td>4</td>
<td>0</td>
<td>4</td>
</tr>
<tr>
<td>Gender (Total)</td>
<td>19</td>
<td>11</td>
<td>30</td>
</tr>
</tbody>
</table>

Source: Primary data

**SUGGESTIONS**

It is suggested to create awareness among the banking customers through various innovative strategies enabling them to increase the usage of digitalized banking services. The security measures must be strengthened by using an advanced protecting system. The cost of using digital banking services must be reduced by minimizing the service charges and the provision of high speed internet facility must be enabled in rural areas to facilitate easy and quick digital transactions.
CONCLUSION

Normally customer’s confidence and trust in traditional banking system will make customers less likely to adopt new technologies. New technologies will not be successful until customers are satisfied with privacy and security aspects. It also requires some time to earn confidence among the customers even it is easier and cheaper than the traditional methods.

REFERENCES


