Cracking the fintech code

By Ashish Bharadwaj

What is fintech?

In a generous sense of the term, financial technology companies, or fintechs, combine financial services with modern technology. This amalgamation of an age-old commercial practice with the churning of forces of tech innovation is both revolutionary and unsettling. What financial systems do. There is no single definition of fintech. In some cases, this is because of non-existence of a harmonised legal framework, and in other cases because of differences in regulatory obligations.

The problem is compounded by the multiplicity of business models and a variety of financial products and services that are on offer. Nevertheless, the fintech industry can be largely understood on the basis of characteristics that define underlying business models, whether or not a company is involved in one or more of the following innovative ways:

Provide finance for private individuals and businesses: This is done through crowdfunding or by extending credit in cooperation with partner banks. Popular crowdfunding platforms can be differentiated on the basis of the kind of consideration given to investors for their investments. It could be donation-based, reward-based, crowd-investing or crowd-lending.

Manage and dispose financial assets through various channels: This includes social trading platforms where individual investors can benefit by observing the strategies and portfolios of others in the social group. Another set of companies deals exclusively with personal financial planning and management based on software and mobile applications on one hand and application programming interface (API) technology on the other.

Offer applications and services related to national and international payment transactions: This includes platforms where banks are not necessarily required to serve as intermediaries, such as virtual currencies (commonly known as cryptocurrencies) and blockchain. A cryptocurrency is born and raised in a decentralised digital world by transforming user data into various units to create digital currency units. These units can be used to make online payments outside the framework of any financial institution or a central bank. Bitcoin is the first and most commonly known, but there are other variants of cryptocurrency. Several digital payment systems are built on blockchain technology to secure online transactions.

Beyond Bitcoin

Blockchain is a form of distributed digital bookkeeping system that preserves and secures all records of online transactions including those carried out with cryptocurrencies. The biggest attraction of this technology are transparency and application in numerous fields including land records, health data, employee records, litigation, financial transactions and many more. These platforms also include those fintechs that offer functionalities that are handled via mobile phone, such as payments through e-wallets or cyber wallets and bank transfer solutions.

Provide or facilitate acquisition of insurance (including P2P insurance): Offering online comparison of financial products or services, and offering IT infrastructure-related solutions to financial service providers. This is called insurance technology (or insurtech) and it is aimed at reducing the cost for users of insurance products and services. Insurtech companies seek to provide highly dynamic and customised policies by analysing consumer data recorded by smart devices and appliances of daily use.

Help users and businesses comply with market-specific regulations: These businesses take the help of software and applications that are dedicated to address regulatory and compliance issues in financial services. It is also called regulatory technology (or regtech). The objectives of this technology are to automate and digitise rules on anti-money-laundering and prevent bank scams by verifying user credentials.

Its prospects in India

Interestingly, the regulatory framework governing fintech has grown into one that allows for disruption but in a contained manner. There were major regulatory regurgitations after the financial crisis. The Dodd-Frank Wall Street Reform and Consumer Protection Act, 2010 in the United States was the largest set of regulatory overhaul changes that the financial services industry witnessed since the Great Depression of 1929. These changes affected major financial institutions on one hand and presented huge opportunities to new entrants.

In 2018, in its landmark Aadhaar judgement, the Supreme Court of India barred private companies from accessing biometric data, causing a tectonic shift in the burgeoning Indian financial services sector. Around the same time, the Reserve Bank of India took a pioneering step to regulate non-banking financial companies and peer-to-peer lending platforms in a boost to the industry. We still need to know what can be done about the high risk perception associated with fintech and, more importantly, where India stands in the race to create innovative financial technologies for the future.

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