Growth of India's FinTech Industry: Recent Developments

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Introduction

FinTech or financial technology, is the application of technology to provide new financial services to the existing or new market segments in an economically viable manner. FinTech is a broad category that includes a wide range of technology, but the fundamental goals are to transform the way people and organisations access their finances. FinTech comprises startups, technological businesses, and existing financial institutions.

FinTech solutions are posing a threat to existing financial infrastructure as more and more services migrate to a new technology platform. With a robust growth potential, Indian banks and financial service providers have been steadily utilising technology to expand reach, customer service, and cost optimisation. When conventional banks and financial institutions consider technology as a facilitator of business propositions, FinTech uses digital technologies to create new business propositions and target new market segments that were previously unattainable.

Current state of the FinTech Industry in India

FinTech has been around for decades, but FinTech companies have revolutionised the way customers engage with financial services in the last few years. FinTech has become an increasingly essential focus area for all key stakeholders in the Indian financial services industry. Today, India is the global FinTech Superpower, with the highest FinTech adoption rate in the world, at 87%, much higher than the global average of 64%.

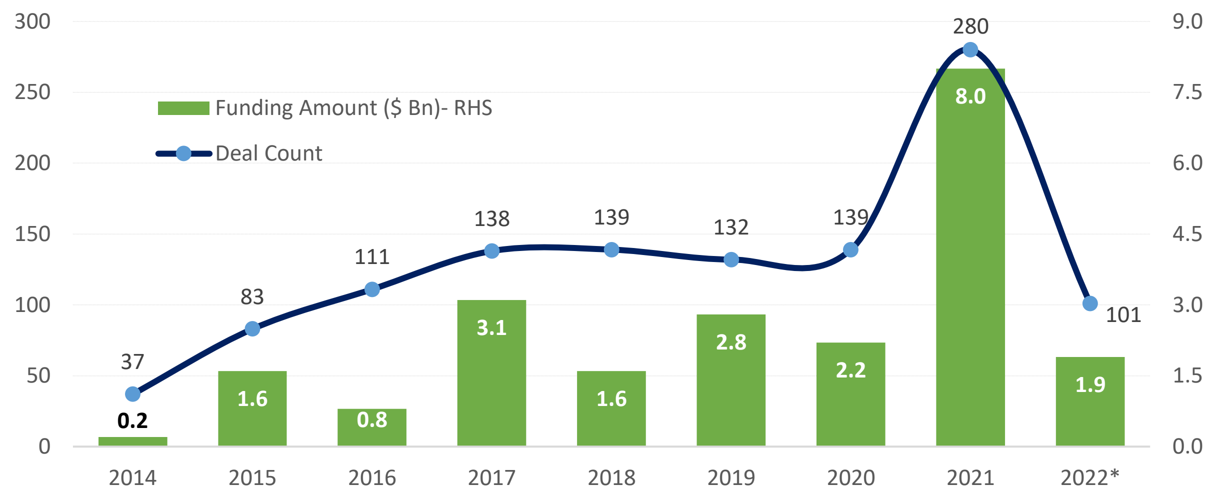
India is one of the fastest growing FinTech marketplaces in the world, with 6,636 FinTech startups. The Indian FinTech business was worth $50 billion in 2021 and is expected to reach $150 billion by 2025. Payments, Lending, Wealth Technology (WealthTech), Personal Finance Management, Insurance Technology (InsurTech), Regulation Technology (RegTech), and other subsegments comprise the Indian Fintech business ecosystem. India has 24 FinTech startups that have achieved 'Unicorn Status' with a valuation of more than $1 billion as of 14 July 2022. Most notably, FinTech accounts for one out of every five startup Unicorns in the country.

Table 1: The State of Fintech Unicorns in India				
Number of Unicorns		**24**		
Combined Valuation		**$69 Billion**		
Total Capital Raised		**$13 Billion**		
Sector Specific Fintech Unicorns				
Sl. No.	**Company Name**	**Segment**	**Valuation**	**Total funding**
1	Razorpay	Payments	$7.5 Billion	$742 Million
2	PineLabs	Payments	$6.0 Billion	$1.4 Billion
3	Paytm	Payments	$5.9 Billion	$2.4 Billion
4	PhonePe	Payments	$5.5 Billion	$1.7 Billion
5	Policybazaar	Insurtech	$4.6 Billion	$767 Million
6	CRED	Payments	$4.0 Billion	$722 Million
7	Chargebee	Payments	$3.5 Billion	$468 Million
8	Digit	Insurtech	$3.5 Billion	$531 Million
9	Upstox	Investment Tech	$3.4 Billion	$359 Million
10	Groww	Investment Tech	$3.0 Billion	$393 Million
11	BharatPe	Payments	$2.9 Billion	$701 Million
12	Bill Desk	Payments	$2.5 Billion	$241 Million
13	ZERODHA	Investment Tech	$2.0 Billion	Bootsrapped
14	CoinSwitch Kuber	Cryptocurrency	$1.9 Billion	$301 Million
15	5ire	Cryptocurrency	$1.5 Billion	$230 Million
16	MobiKwik	Payments	$1.5 Billion	$184 Million
17	zeta	Fintech SaaS	$1.5 Billion	$340 Million
18	CredAvenue	Lendingtech	$1.2 Billion	$227 Million
19	CoinDCX	Cryptocurrency	$1.1 Billion	$109 Million
20	Acko General Insurance	Insurtech	$1.1 Billion	$458 Million
21	open	Neobanking	$1.0 Billion	$141 Million
22	Onecard	Payments	$1.2 Billion	$750 Million
23	slice	Lendingtech	$1.0 Billion	$291 Million
24	OXYZO	Lendingtech	$1.0 Billion	$200 Million
Source: Inc42, State of Indian Fintech Report Q2 2022, Invest India				

Indian FinTech Startup Funding Landscape

FinTech funding in India has increased at an exponential rate in recent years. Since 2014, Indian Fintech has raised over $30 billion. Only in 2021 did India obtain funding totalling $8 billion from 280 transactions. FinTech innovation is widespread, particularly in retail and wholesale payments, financial market infrastructures, investment management, insurance, credit delivery, and equity capital raising. It has the potential to significantly alter the financial landscape. While the Payments and Alternative Finance segment accounted for more than 90% of the sector's investment flows in 2015, there has been a significant change toward a fair distribution of investment across sectors, including InsurTechs, WealthTechs, and so on. The sector's enormous potential is clearly apparent in the global FinTech funding scenario.

Chart 1: Indian FinTech Startup Funding Landscape



*Source: Inc42, Invest India; *: Till 31st May 2022*

An increasing number of Indian banks are collaborating with FinTech firms for business expansion and cost optimisation. Banks no longer view FinTech as rivals, but rather as important partners in expanding their reach and engaging with customers. Banks are investing in two types of FinTech businesses. The first is concerned with returns on investment, while the second is concerned with strategic alignment with their agreements with startups.

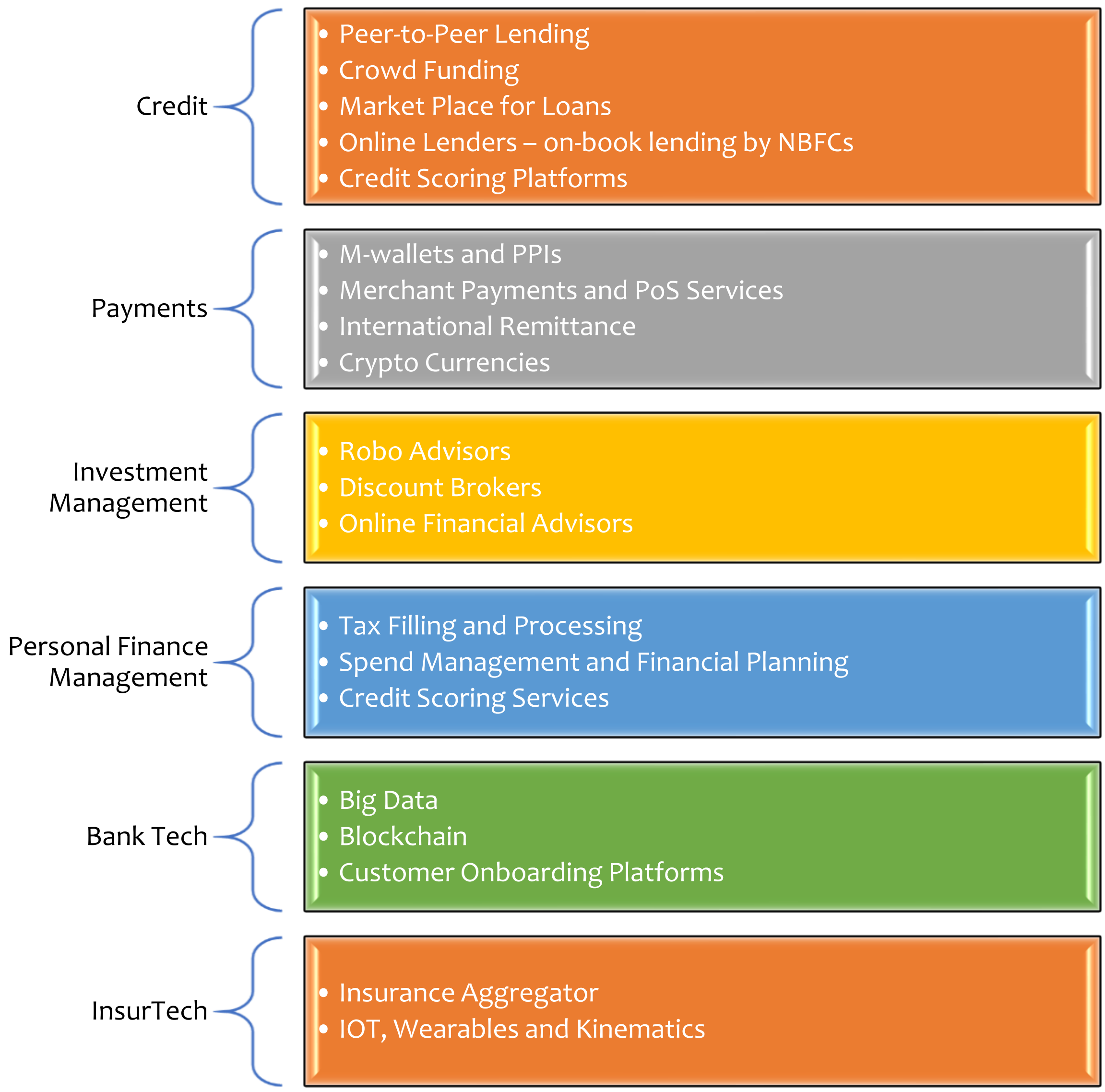
Directions of FinTech Development in India

Adoption of FinTech in India has several economic benefits, including promoting financial inclusion, broadening the offering of financial products and services, increasing efficiency in financial service delivery, improving accessibility, affordability, and customer experience, efficiency in credit delivery processes, better targeted products, improved risk management, including better underwriting models, and improved adoption of RegTech, which reduces compliance costs.

Following the government's demonetization drive in November 2016, the focus on digital payments is unique since payments remain an innovation area with extremely low penetration and areas of friction that new FinTech businesses may address to provide value. Over the previous decade, India's payment environment has evolved into the most sophisticated payment system in terms of digital payments, which have increased at a CAGR of 50% by volume and 6% by value.

Deloitte has classified FinTech in Indian contest into twenty sectors spread over six key financial services areas. Digital payments have been at the forefront of driving India's FinTech business within various categories.

Chart 1: Indian FinTech Industry: Areas and Segments



Regulatory Concern of the FinTech Industry in India

FinTech regulation is required due to the challenges they pose to the financial system and the new risks they introduce. These risks impact overall financial stability and market integrity. Regulators face a difficult balancing act between promoting innovation and managing risks to financial stability, which necessitates greater engagement of all stakeholders to work toward common principles for managing FinTech activities, including business and revenue models, governance, conduct, risk management, and regulatory aspects for promoting a sustainable ecosystem.

Worldwide FinTech firms are subject to these three types of regulations. Activity-based regulation, in which identical actions are regulated equally regardless of the legal status or type of the entity doing the activity. It might also be entity-based regulation, which requires laws to be applied to licenced firms engaged in comparable and specified activities, such as deposit taking, payment facilitation, lending, and securities underwriting, among others. It can also be outcome-based regulation, with firms required to ensure certain fundamental, common, and technology related aspects.

With the increased use of technology and digital services, there has been a rise in digital fraud and consumer dissatisfaction. To address the rising issues, the RBI has taken some supervisory initiatives to address the risks associated with Fintech activities. Most FinTech firms in this space, including P2P lenders, Alternative Credit Scoring platforms, and Crowd Sourcing platforms, are brought under the regulatory ambit.

RBI has been extra vigilant in cyber security area and has been conducting phishing simulation exercises for select Supervised Entities (SEs) to assess their email security standards and cyber security preparedness. Customer service is another area which is engaging the attention of the RBI due to the harsh recovery methods used by certain lenders, without having adequate checks and controls over their recovery agents.

Because the RBI has remained risk averse, its regulations have sometimes curbed the exponential expansion of FinTech enterprises. With the implementation of the Unified Payments Interface (UPI) and the imposition of strict KYC compliance standards in 2017, PPIs lost their attraction in offering wallet services. In recent days, regulatory scrutiny of digital lending, prepaid payment instruments, and buy now pay later (BNPL), excess tax on Crypto transactions have increased worries among FinTech businesses.

Sustaining growth of Indian FinTech Sector

The Indian economy's strategic positioning favours the FinTech industry. The most appealing element for FinTech is the combination of steady economic growth and low penetration of financial services. One more key facilitator of FinTech growth in India is the India stack Open API platform, which lets FinTech businesses to leverage India's unique digital infrastructure for presence less, paperless, and cashless financial service delivery. Growing internet and smartphone penetration is hastening the process, since India already has the world's second-highest number of smartphone users and the world's second-largest Internet user market. With a median age of 28, favourable demographics are one of the most important variables in ensuring a self-sustaining market for the FinTech services.

Technological advancements and cloud service adoption are resulting in asset-light models with nearly zero-unit costs at transaction levels, allowing for subsidisation without any need for building scale. FinTech firms are passing on the advantages of reducing transaction costs to end customers, hence boosting their offerings. This element is emphasised further by the legacy-free environment in which most FinTech businesses operate, requiring them to rely on cloud-based services to match their entire cost structures. Most significantly, regulatory leniency toward FinTech is encouraging the industry. Indian regulatory agencies, including as the RBI, SEBI, and IRDA, have taken an accommodating approach toward the developing FinTech industry, without imposing restrictive standards to overregulate it.

Conclusions

The Indian FinTech business has expanded significantly in recent years. Technology has been a crucial enabler in the growth of a digital economy. FinTech businesses, armed with powerful data and analytics capabilities, asset-light platforms, and near-zero processing costs, are complementing, and in some cases challenging, traditional banking and financial services organisations. FinTech innovators have been able to capitalise the late entry of existing banks in the technology domain by unbundling financial services. India is rapidly evolving and is one of the world's fastest-growing Fintech markets. Advanced technologies and a customer-centric approach are what bring this thriving industry its profound growth. While FinTech and Banks are collaborating, entry of BigTechs have been changing the scenario much faster through their quick technology adoption strategy. BigTechs are reversing the trend of unbundling of financial services done by FinTechs.

Furthermore, as FinTech firms grow, they are expected to face increased regulatory scrutiny. A reasonable regulation with clarity, on the other hand, will strengthen the sector in the long run and facilitate the Indian economy in growing at its potential rate by allowing its growth drivers to fuel the engine of economic advancement.

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