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REVOLUTIONS IN DIGITAL FINANCE

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Abstract

Technology has transformed how we work, communicate and travel. In contrast, modern digital technology has not yet transformed financial services. Open data is the key to change in this sector of the economy. The time has come for the financial services industry to join the open data revolution. Open data means interoperability of digital information to increase its usability and accessibility. When open data is brought to private sector, moreover, one of the benefits will be information portability for consumers. Today advances in technology have made it easier for customers of banks and insurance companies, among other financial institutions, to share their information with others. Rather than storing key documents in shoe boxes and file folders, consumers and small businesses can pass along digital online and banking credentials. This happy story of progress however is far from complete because of concerns around privacy and security, and the intimate choke points on data sharing.

Keywords: *Finance, Digital finance, Financial Technology*

Introduction

It's hard to overstate the impact of strong financial services industry as a driver of economic growth. Deep capital markets and strong financial institutions give consumers easy ways to save, invest, borrow and plan for their future. Enterprises and small businesses, in turn, depend on financial institutions to raise capital for growth, efficiency and infrastructure expansion. This cycle of saving, investing and lending is crucial for emerging economies like India to sustain economic growth. It is common knowledge that India does not score very well in this regard. Over half of the population does not have an active bank account, only 23% of all Indians have usable credit history, and 80% of medium and small business do not have banking relationship.

Technology Driven Financial Service Innovation

There are more than 500 financial technology start-ups in India who have collectively attracted over $1.4 billion in funding since 2012. While mobile payment start-ups have garnered a lot of attention, there are many other attacking a range of services that have been the bailiwick of banks and financial service providers – consumers & small business lending, remittances, wealth management, personal finance and related areas such as credit scoring and stock trading. Together these make financial services the single largest market opportunity for start-ups in terms of economic value. The big question is if market is ready for change and if these firms can deliver and scale. There are few key ingredients that have come together to create a fertile environment for disruptive solutions. These are:

Unprecedented reach

While less than half the population may have a bank account, over 90% of consumers own a mobile phone. Smart phone sales have taken off and expected to touch 500M units in five years, providing unprecedented mobile internet access. From start-ups to banks, every player in financial ecosystem suddenly has reach and consumer access that was impossible even five years ago.

- **Use behaviour of a digital generation**

  In less than a decade, there has been a massive shift in consumer behaviour among a young Indian population. Starting with e-commerce, consumers are embracing a new generation of mobile Internet solution for a service ranging from taxis, music, movies and food ordering to medical care and furniture purchase, among others. It's not hard to see this extend to financial services, fundamentally changing the way Indians expect these services to be found and delivered.

- **Target high Impact Solutions**

  Most start ups are focusing on specific point and attempting to deliver value, cost reduction, and efficiency enhancement that can attract consumers. There are start ups reimagining the loan search and fulfilment process to make it more efficient for consumers while reducing the cost of customer acquisition for banks. Another category in financial technology providers are building lending platforms for small business working capital loans as well as pioneering peer to peer lending. Lending by itself is a massive market. Digital lending is less than 2% of market today. There is enough promising innovation in this category to tackle the core issue of boarding credit access and banking reach for consumers and small businesses. There is significant start up momentum in a range of other areas such as mobile payments, online insurance, remittances, robo – advisory & credit scoring that promise to bring disruptive change. However to succeed, there are few challenges unique to India that these start ups and overall ecosystems have to address.

- **Data Access & Quality**

Unlike developed markets, there are still significant gaps in financial and operational data availability in India. Lending start ups have built impressive credit underwriting models. But they need regular access to trustworthy and high quality data to have impact. There are two issues – one of coverage (three quarters of population does not have credit score) and data access (many small business does not have reporting system to tap into).

- **Co –opetition with banks**

Incumbent Indian banks are not fading away anytime soon. The reality for any financial technology start ups is the need to work with the range of banks and financial institutions. They need understanding of and access to Indian banking and also have to differentiate themselves from dozens of start up peers who are lining up with the same requirements. This calls for both sales skills and domain understanding to persuade banks, in addition to great technology.

- **Regulations**

The good news is that is both the government and RBI view start ups as being able to bring new ideas and technology to the table. That said, navigating and regulatory maze and securing licences is challenging for small start ups. A recommended way is to proactively meet and educate the regulator (SEBI, IRDA, RBI depending on the solution) and stay abreast of evolving view points.

- **Trust**

Banks may have lot of inefficiencies and are often lagging in technology. However consumers do trust them. Start ups will need to win this trust by ensuring a high quality, transparent, and safe transaction experiences. To scale beyond being a niche provider, these firms will also have to raise significant capital to build a national brand and a broad set of services.

Innovation on the Front End

Trade finance customers seek the same things that other corporate banking customers want: process transparency, risk reduction, credit when needed, and the rapid, low-cost facilitation of transactions. In recent years, banks have used digital technology to make it easier and cheaper for customers to access such services. Deutsche Bank’s Autobahn platform offers clients an ever-growing variety of apps for cash flow management, supply chain management, trade finance, and more. But for trade finance, best-in-class innovation has come predominantly from fin techs. Prime Revenue and Market Invoice are winning business in supply chain and receivables financing by offering customer interfaces that simplify interactions and reduce time-to-cash. A large gap has opened up between the leaders and the rest.

Banks should not underestimate the importance of high-quality digital front ends. These interfaces do more than improve customer convenience. By acting as gateways for supplying customers with complementary services over and above mere transactions, they can strengthen relationships in a way that fin techs struggle to achieve. Getting the front end right allows banks to be seen as service partners rather than document processors, thus letting them sustain their fees in the increasingly competitive digital world.

Impact of Digital Structural Change

The opportunities provided by digital structural change are undoubtedly multifaceted and a long-term forecast of where they will lead cannot yet be made. The most serious risk for market participants is by contrast existential in nature: that they will be forced out of the market. The road to survival for several traditional actors is thus paved with painful consolidation measures and cost intensive reforms that are, however, important for holding their own in the new competitive environment of the future.

The growing penetration of modern internet technologies gives rise to new market entry opportunities, especially for technology providers. The lucrative opportunities for the new players in turn ramp up the competitive pressure on the established players. Due to digitisation the established companies find themselves being exposed in some areas that could also develop into Achilles' heels. They provide fast-growing internet firms with the opportunity to occupy certain market niches in order to a) monetarise their digital content and b) make their own range of products more attractive to an even wider public. For some time internet behemoths have been putting out their (digital) feelers across numerous sectors, investing billions of euro’s, experimenting in a variety of markets, also outside their core business, and offering new business models.

The potential consequences of digital structural change and an inadequate adaptation in individual sectors could be seen clearly over the last twenty years in the music industry. In publishing and the media, too, business processes are being revolutionised by digitisation. For several years the wave of digitisation has also been shaking up the financial sector. It affects – as expected – the area of easily standardise able and non-knowledge-intensive services. These include payment solutions, automated financial services, online banking and simple financing products such as consumer credit or the allocation of venture capital to start-ups. Similar things are happening in the insurance and healthcare markets; other sectors will undoubtedly follow. Everywhere there is catching up to be done with regard to expanding modern information and communications technologies and digital infrastructures.

A New Landscape

The global financial crisis changed the landscape. Foreign banks scaled back their activities in some African countries, while new local banks increased their presence. The relative success of microfinance institutions in some countries (especially those that introduced a new technological platform to manage micro savings and deposit accounts) encouraged domestic banks to expand their networks. At the same time, nonbank financial institutions, such as savings and loans and cooperatives, formalized their activities. In response, regulators began introducing alternative models that helped cut intermediation costs. Bank representatives at such outlets can perform authorized tasks, such as opening bank accounts, processing loan applications and loan repayments, and so forth.

These changes were driven by demand. Market participants pressured regulators to build their capacity to cope with innovations and to develop institutions to support financial sector growth. Greater credit information sharing and the development of information for market participants, deposit insurance, and financial intelligence units generated a virtuous circle. Suddenly, businesses did not have to give their employees time off to take money to their villages to care for relatives or small farms. Employees no longer had to travel long distances carrying cash and exposing themselves to robbery and other dangers. Relatives back home did not have to make long trips and risk assault or blackmail by local criminals who tracked the frequency of their travels. The digital revolution allowed people to make financial transactions and money transfers from the comfort of their homes. The lower cost left them with more disposable income, and they now had a secure way to store cash, even those working in the informal economy.

Thanks to mobile payment developments, a new wave of Polish start-ups is getting ready to fulfil every single need of Polish customers, expand into foreign markets and compete with global brands. A good example is iTaxi – a taxi-hailing service, quickly became one of the most popular apps in Polish big cities and a business environment for over 10,000 taxi drivers. Client focus, user-friendly interface and a recommendations-based system help iTaxi win new clients and attract business partners' attention. Though, iTaxi will now have to prove its competitive edge against Uber, the global leader in this field, which has decided to enter and conquer the CEE markets. As a result, Polish clients will have a wider choice of competitive services and will pick the one that brings better value.

Conclusion

Digital financial services not only contribute to financial development, they also support financial stability. With less need for cash for transactions, more economic agents can send and follow financial market signals, contributing to a more solid and vibrant financial system. The environment for monetary policy improves as a result. In addition to lowering the costs of transactions, financial inclusion opens the door for potentially game-changing opportunities: innovative pension plan support and government-targeted social protection, expansion of regional payment systems within regional blocks, enforcement of policies to stop money laundering and the financing of terrorism, and a better environment for forward-looking monetary policy to replace years of financial repression and reactive policies.

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