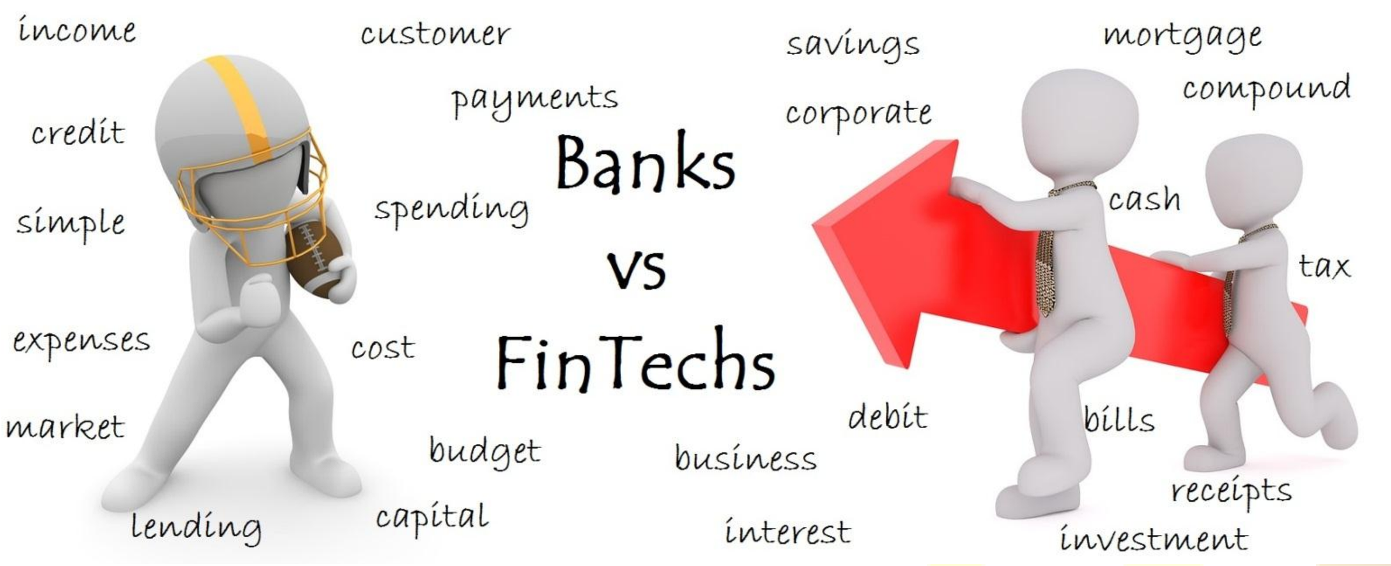
Tat CAPITAL
Corporate Finance & FX Advisory

India’s banking challenges in the FinTech era, and the role of Aussie firms

Pras Indrakumar



India’s banking challenges in the FinTech era, and the role of Aussie firms

Indian FinTech industry is without doubt growing at an outstanding pace, giving the highest RoI of 29% against the global average of 20.1%. (Source: PwC - Redrawing the Lines - 2017). Statista reports that the transaction value of the Indian fintech market is $44,068mn in 2017, with an expected CAGR of 20.2% to reach $91,999mn by 2021.

With governmental reforms including demonetisation, Digital India, Aadhaar, GST, financial inclusion, etc., the scope for further initiatives and innovations in this sector looks more promising. As per NASSCOM, the Indian fintech software market is expected to reach $2.4 bn by 2020, doubling its existing market size of $1.2 bn; the total Indian fintech market is currently valued at $8 bn, with an expected growth rate of 1.7* by 2020.

With such economic impacts backed up by the demand of a large user base, let’s look at the prominent focus areas in India’s fintech market, and the companies that offer these services:

Fastest growing fintechs & their sector focus:

- Payments:

One of the well-performing and largest sub-niches of the Indian fintech market is Digital Payments, wherein the transaction value totals to $43,831mn in 2017. Services including Mobile/online payment solutions, such as wallets, P2P transfer and points of sale (PoS) are witnessing highest user adoption, heavily benefitting the SMEs.

Government programs including Unified Payments Interface (UPI) and India Stack (APIs to create presence-less, paperless, and cashless solutions) have also played an instrumental role in the nation’s shift toward mobile payments. As per PwC’s Fintech India Report 2017, this digital payments sector is estimated to grow to USD 500 billion by 2020, representing around 15% of GDP in 2020.

Paytm - the rising popularity of India’s largest payment startup Paytm since the demonetisation period affirms this transition, where the company had 7 million daily transactions during Nov’16. Its current user base is about 225 million users, and is approx. valued at $5.8 billion.

- Founded in 2010 by Vijay Shekhar Sharma, this popular fintech company deals with mobile payments/wallets, e-commerce & payment banks, raising several millions in each of its funding rounds incl. $1.4 billion investment by Masayoshi Son's SoftBank Group Corp. It was the largest funding round by a single investor in an Indian startup.

MobiKwik - Founded in 2009 by Upasana Taku and Bipin Preet Singh, it is another popular Mobile payments, recharge & wallet company, which has raised around $162 million so far in its funding rounds.

Ezetap - A Payments/PoS company that offers end-to-end payment solutions. It has raised $51 million from investors Social Capital, Helion Venture Partners, etc.

Others including payment gateway company Razorpay (11.6m), P2P payment and money transfer app Chillr (7.5m), subscription billing service for SaaS companies Chargebee (6.2m), multi-purpose prepaid cash card company Itzcash (35.3m), etc. also fall under this niche. Itzcash has also received around 100m investment from software company Ebix. The importance of this segment can also be understood by the number of payment platforms provided or acquired by bigger financial services and corporations such as Jio Money, SBI Buddy, ICICI Pockets, etc.

➢ Alternative Lending:

The second most funded and one of the fastest growing sub-niches in the Indian FinTech space, where around 37% of GDP is contributed by MSMEs. As per CB insights, there are 158 new startups in AL as of 2016, which could play a huge role in reaching the unbanked and newly banked section of the population.

As of October 2016, AL has received $199 million across 33 deals, almost twice the 2015 funding of $103 million across 21 deals. Let's look at some examples:

LendingKart provides working capital to MSMEs in a quick, easy and collateral free way with minimal paperwork, raising $42M in its funding rounds.

- Founded in 2014 by Harshvardhan Lunia and Mukul Sachan, this online lending platform has expanded to 462 cities, disbursing close to 6500 loans.

Bank Bazaar is an online marketplace, which offers customized rate quotes on loans and insurance products.

- Founded in 2008 by Rati Rajkumar, Adhil Shetty and Arjun Shetty, BankBazaar has raised $80 million so far, and has recently announced stepping into the Malaysian market with $7.76m (INR 5 crores), and is adding another $15.5m (INR 10 crores) to its Singapore market, as part of the company's international expansion plan.

Capital Float - The digital lending platform for SMEs has raised $88.53 million so far, and even has partnerships with companies incl. Shopclues, Paytm and Uber.

- Founded in 2013 by Sashank Rishyasringa and Gaurav Hinduja, Capital Float has disbursed INR 1000 crore as of January 2017 and is looking at reaching a value of Rs.5000 crores in the next two years, along with its plan to reach out to kirana store owners, small mom & pop stores and other small businesses.

Vistaar Finance - is another online lending platform to SMEs, which has raised $76 million so far. It was founded in 2010 by Brahmanand Hegde and Ramakrishna Nishtala.

Other examples include:

P2P Lending:

Faircent is a virtual marketplace for money lenders and borrowers, which has raised $8.25 million so far in its funding rounds.

- Founded in 2014 by Rajat Gandhi, Nitin Gupta and Vinay Mathews, it has 6000 registered lenders, 30,000 registered borrowers, with an average INR 1 crore loan disbursal every month.

SME Lending:

NeoGrowth - is a small business lending platform, which caters to small and medium-sized retailers and online vendors and sellers. Founded in 2013 by Dhruv Khaitan and Piyush Khaitan, it has raised $43.62 million so far.

Rubique is an online marketplace that offers wide range of end-to-end loan solutions to individuals and MSMEs, raising $6 million so far.

- Founded in 2014 by Sandeep Nambiar and Manavjeet Singh, it specialises in optimal matchmaking algorithm to offer best deal in the shortest possible time.

Other companies incl ApnaPaisa ($20.2m), India Lends ($5m), OnEMI ($5m), etc. also fall under this niche.

- Insurance:

These fintechs offer insurance products namely health insurance, auto insurance, travel insurance, home insurance, etc.

PolicyBazaar is a leading online insurance platform for SMEs as well as individuals, which has raised $70M so far in total funding. It was founded in 2008 by Alok Bansal, Yashish Dahiya.

Companies such as Bank Bazaar (mentioned earlier), insurance aggregator and selling platform Coverfox ($27m), Online selling and comparison platform for insurance Easypolicy ($2.2m in Seed), business insurance company SecureNow ($3m), etc., fall under this niche. SecureNow, for instance, offers group health insurance, workers' compensation, fire insurance, officers' liability insurance, among other products.

- Personal Finance:

Companies offer personal finance services such as assisting consumers in filing taxes, managing their wealth, carrying out securities trade, etc.

Cleartax is an e-filing platform that helps individuals complete their income tax returns, and has received $15.42m in funding so far.

MoneyView is a personal finance management app that helps in organising expenses, getting reminders for bills, following personalised budgets, etc., and has received $10.11m in funding so far.

- Banking Tech:

Fintellix - is a fraud and risk analytics company offering risk compliance solutions for banking, which has received $15m from investors such as Sequoia Capital, IDG, etc.
Fino Paytech - is a financial inclusion technology provider dealing with banking correspondence, which has received $52m from investors incl. Bharat Petroleum.
Loylty Rewardz - is a loyalty relationship management company, which has raised $24.4m in investment.

➢ Investment Tech:

Cogencis - is a real-time market data and financial news terminal on public markets ($16.5m)
FundsIndia - is a robo advisory firm for public market investing incl. mutual funds, with a funding of over $15m.
Scripbox - is a robo advisor that enables investing in mutual funds ($3.22m), which has received undisclosed amount from Omidyar ventures in Series B and $2.5 million in Series A from Accel Partners.
5nance - too is a robo advisor for public market investing ($3m)

There are several fintech companies under other categories too, such as -

- Blockchain: Zebpay-ZebIT Service and Unocoin ($1.75M)
- Merchant-focused services, wherein outsourced CFO, contract management services, etc., are also offered. Ex: Sirion Labs ($16.95m) is a leading SaaS provider, managing outsourced contracts and invoices for enterprises.

The below chart from EY FinTech Adoption Index 2017 report further shows where the subcontinent is standing with respect to top 5 fintech markets:

Figure 7: **Comparison of the top five markets with the highest FinTech adoption for each FinTech category**

	Money transfer and payments		Financial planning		Savings and investments		Borrowing		Insurance	
1	China	83%	China	22%	China	58%	China	46%	India	47%
2	India	72%	Brazil	21%	India	39%	India	20%	UK	43%
3	Brazil	60%	India	20%	Brazil	29%	Brazil	15%	China	38%
4	Australia	59%	US	15%	US	27%	US	13%	South Africa	32%
5	UK	57%	Hong Kong	13%	Hong Kong	25%	Germany	12%	Germany	31%

Notes: The figures show the average percentage of respondents in each market who reported using one or more FinTech service in that category.

The image clearly shows how well India is performing in the fintech space. Within India, the payments and lending markets have been the top most sub-niches, with rising entry, innovation and demand.

According to YourStory, 23 payment & 26 lending firms have seen more than a billion dollar funding over the past 2 years.

No doubt, the overall scenario incl. ease of doing business, and FDI reforms to make investments and business environment smoother, is aiding the sectoral growth by leaps and bounds.

Under the vision of Andhra Pradesh CM ChandraBabu Naidu, Visakhapatnam, for instance, is looking to be the fintech hub of India by 2019 with several program initiatives to contribute to this burgeoning niche, as well as to become the global fintech hub by 2023.

With digitisation, rising awareness & comfort in using modern technology, the prospect for other sub-niches like banking tech, e-tax filing, loyalty management, etc., only looks bright, and they have also started to gain traction and funding interests. According to a nationwide survey by PwC, newer segments like personal finance & enterprise solutions are expected to gain strong foothold in the subcontinent's fintech arena in 2017.

Challenges banks are facing:

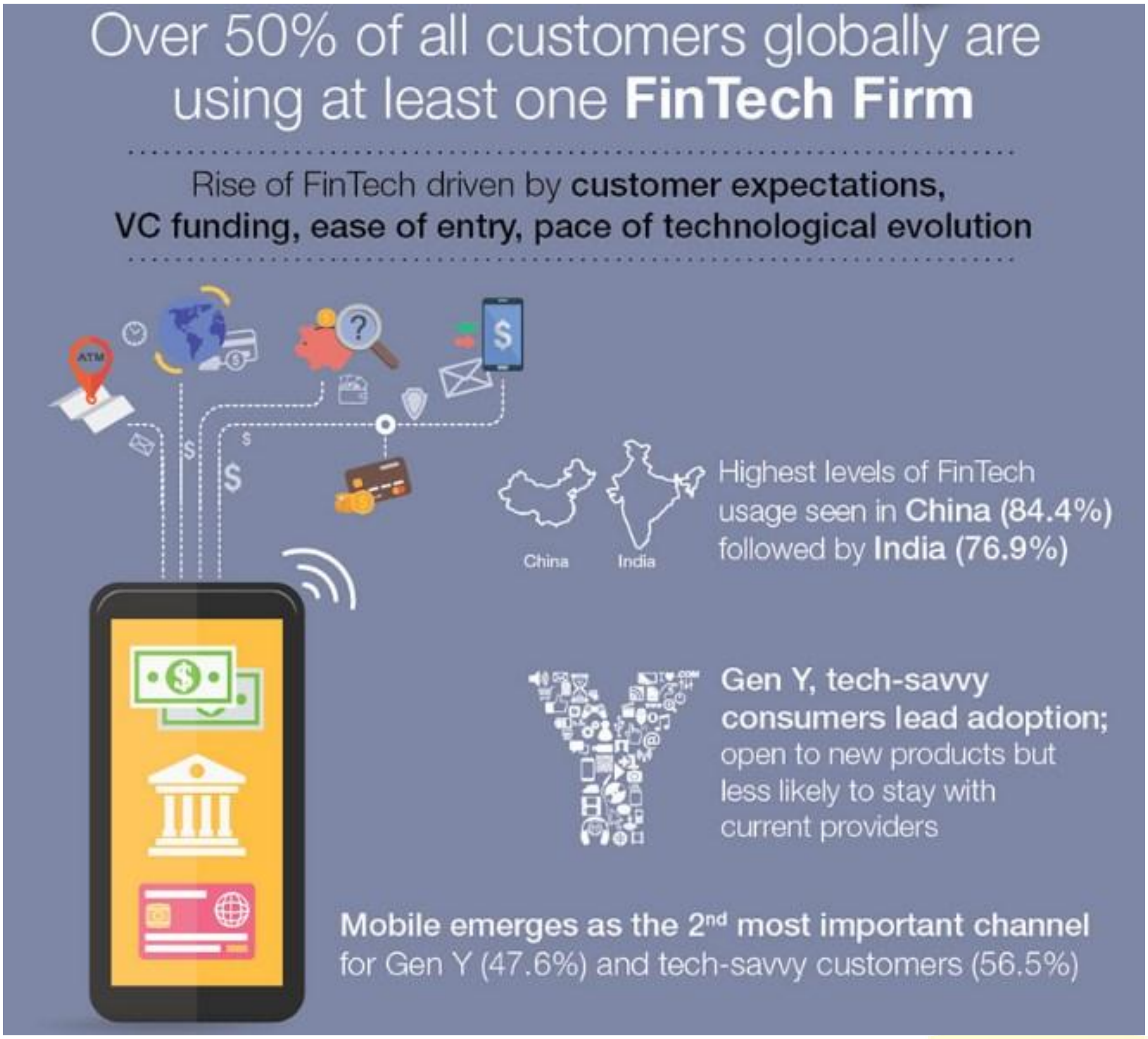
India has predominantly been a cash based economy, wherein people from rural and remote areas have managed to stay under the radar without being part of any formal banking system. Small and local businesses likewise, such as micro, small & medium-sized enterprises (MSMEs) are also significantly cash based.

The urban & metropolitan crowds on the other hand look for easier, cheaper, and time efficient ways to carry out day to day financial activities, relying heavily on internet and mobile based services.

When such a vast country's diverse population has different needs according to their strata, business and location, the gamut and potential of financial services will need to be equally varied, tailor made, and simple. For Indian banks, thankfully though, they still dominate the country's financial landscape, and recent financial inclusion and demonetisation reforms have definitely upped their expansion potential.

However, the recent fintech tide, which has been causing ripples all over the globe and in India, could be a cause of concern, if relevant measures to dish away the traditional, complex, redundant procedures, and to bring in modern, digitised and simple steps are not given importance.

A recent report by Capgemini and European Financial Management Association has announced a 55-60% fintech adoption by Gen Y and tech savvy customers in India & China, making it the highest non-traditional adoption globally.



Through the right probability of technology and innovative business models, fintechs, if we see, have the potential of disrupting the banking sector, as they offer almost all popular banking services in simpler, less expensive ways, with easier accessibility and availability, through quicker and hassle-free approach.

A joint study by Tata Consultancy Services and Clayton Christensen Institute for Disruptive Innovation reported:

"In each product category, new entrants pose a competitive threat to banks, but the conditions are not always ripe for disruption. Instead, many fintech innovations are being launched to sustain or improve existing products, making them attractive for both new entrants and existing banks. Therefore, as long as incumbent banks are incentivised to adopt these solutions, rather than ignore them, disruption could be less of a factor. But this does not mean disruption is impossible, particularly if fintech entrants are able to scale up from a foothold in an underserved market."

When a tech tycoon like Bill Gates remarks on the transformational advent of mobile banking, and how people, especially the poor, need banking but not banks (Source: [2015 annual letter]), it highlights the impact of the fourth industrial revolution that these modern technologies are bringing forth.

With that in mind, let's look at some concerns/challenges that our banking system faces:

According to McKinsey, stressed assets without any loan-loss cover exceed $96 billion, and almost 91% - viz., amounting to $87 billion of the provisioning gap is with state-run lenders. This could prove catastrophic once it affects their capital, wiping out their net worth altogether.

An [ET article] highlights this morbid time for banks, criticising the system of collaterals, and the need to weigh in based on the business itself. Ex: Singapore's sovereign wealth fund GIC Pte partly liquidated its decade-long stake in UBS Group AG & added investment in Mumbai-based SME lender Capital First Ltd. to 14%. The fintech firm's retail assets have grown 24-fold in six years to about $3 billion, with a bad-loan ratio of less than 1%.

So the management consulting company Mckinsey has suggested options such as quarantining assets that would eventually right the situation, liquidating the ones that don't, and working with professional asset managers to turn around the rest of debtors.

However, one thing is clear, losing market share to fintech is inevitable, mainly for public sector banks, if they don't up their ante in the overall system.

The operational cost of a fintech is substantively lower than banks, with the latter also facing high regulation. It is bound by Foreign Account Tax Compliance Act (FATCA) and Anti-Money Laundering

(AML) acts, etc., so if a consumer needs a loan, a lot of procedures and documentation is involved, to get the go ahead. Even when it comes to trading platforms, documentation & management, financial analytics, payment system, etc., banks are not yet ahead of the curve.

In KPMG's Pulse of Fintech Q3 2016 report, it had mentioned the importance of banks understanding the weight of next-generation payments, as without innovation in this space, they could see an adverse impact on their revenues.

With existing models, where the steps are numerous, requiring documentation and authentication, it would be better if the banks are able to give a streamlined, digitised alternative, rather than having the customer walk to the branch offices every time.

Even handling much of the customer base and queries is undertaken face-to-face, with no option to resolve issues over the internet, or have people raise bugs when an important feature in the Internet Banking does not give the desired result. For instance, the system brought in by Kotak bank recently is a good example of innovation in this regard. The launch of 811: India's first downloadable account within five minutes. It allows users to open a bank account digitally, wherein eKYC is done through Aadhaar and PAN. This is a great step towards modernizing the olden ways that required branch visits and in-person verification.

Infact, by 2020, digital transactions are estimated to be more than a quarter of transactions in the banking domain and by 2022, digital banking will have more than 50% penetration. This puts the importance placed on technological innovation and upgradation in the existing models right at the top, as already mobile banking adoption rates are higher than web banking. This then makes it an immediate/crucial need to cater to the 'on-the-go' population.

If this is at one end of the market, there are also plenty of opportunities to be tapped in the 80% non-digitised customer base.

Naveen Surya, MD of fintech company Itzcash, in fact remarked,

> "Everyone is trying to target the top 10% that has resulted in oversupply and that's why conflict is created. The problem is to create a variety of typical Indian solutions, which are more complex to build, for the next 70%."

The comment by Nitin Chugh, Country Head of HDFC Digital Banking reveals this sentiment too, when he said,

"When we organised the innovation summit in February, we had a category of rural fintech in that. But, to our surprise, not even one startup came up with a product for that bracket."

If banks could strategize their product offering and custom make it to suit the rural and underprivileged market, it could prove to have a compounding effect, as the numbers of that set of customer base is quite vast.

Another potential for market is capitalising on the fintech struggle in B2B models, as they tend to thrive better in B2C. Turning that to the bank's advantage is an interesting and crucial challenge, as this helps banks gain business confidence, and thereby higher market share. The Inc article mentions the example of fintech firm Signzy, wherein as a B2B company, it had its investors asking them to switch to a B2C model. Truly, banks have better advantages in serving the SME market, more so lending, as their cost of capital is much lower.

Though few industry experts argue that fintechs will not have the kind of existential impact on banks such as the one had by Netflix on Blockbuster; as a player in the financial domain, they can definitely pose some serious challenge in the product space. Growth of P2P payments is an example, which is forcing the bank to modify drastically their pricing and profit models. This puts the need for being a level player right on top, at least to ensure market retention.

Another interesting aspect of the fintech market is its flexibility and range of offering, as the newcomers address all or any aspect of the financial market. Let's take GST for instance. A new sub-sector called GST enablers has made its way, offering timely service for what would be an yearly affair for millions of taxpayers.

This emphasizes the need for banks to include more arrays of product offering, making their financial service holistic in nature. Even if it requires an external collaboration, the likelihood of customers engaging in their bank's services will top other lateral entries.

In short, the need for holistic as well as long-term engagement with customers, with easier access and availability is quintessential.

More importantly, there are also PSU banks with a large customer base, but very little innovation. Unlike the involvement of the private banks in the fintech race, there hasn't been a leap towards innovation in their turf, and that is a definite cause of concern at such changing times.

There also seems to be a risk averse attitude in terms of investment in recent times, which could be considered as an edge for an established system like banking, to get back in the lead. For instance, reduction in the average ticket size for early stage funding, with seed funding seeing a decline from $1.0 million in 2015 to $0.8 million in 2016, and series A moving from $5.4 million in 2015 to $4.2 million in 2016. Even if this indicates the stability that fintech startups are gaining through reduced capital needs, it is upto the banking system to make or mar the opportunity with corresponding efforts to address the challenges, and forge ahead.

Competition vs. collaboration:

Whilst there are challenges for both banking and fintech markets, partnerships, acquisitions and initiatives between the two segments are becoming common.

YES Bank's Managing Director Rana Kapoor had said, "The mantra is to collaborate, not compete. Banks need to be smart enough to realise that given the rapid pace of innovation overall, all innovation cannot be done within their organizations. There will often be nimbler, smaller start-ups creating path-breaking solutions addressing a particular market problem."

Opposing the view of traditional banks which saw fintech as a competition, he added, "I strongly believe that 'collaboration' is the way forward and it is important to build alliances, relationships & technologies to spur what I like to call as the ART (alliances, relationships & technologies) of Digital banking."

The views of HDFC's Digital Banking Country Head Nitin Chugh seems to be in tandem: "Our approach was to see if we can take a solution for our customer without any reason of conflict. So, even today, no fintech (startup) comes and tells them that work with us or we will take your business. People come and tell us that we would love to work with you. And this collaboration is happening only in India as compared to other markets where banks still see fintech startups as competition."

Currently, HDFC is engaged with almost 75-100 startups, and their innovation team has examined about 1,000 ideas in the last nine months says Nitin.

Fintech startup Signzy's head said, "We believed from day one that banks have the knowledge, banks have the experience and you cannot discount that. So, as a startup, you are nimble and lean, and if you can leverage each other's strengths, you can collaborate." Riyaz Ladiawala of Heckyl Technologies likewise commented,

"Indian fintech companies lack the business acumen. To make a product is one thing, but to monetise it is a completely different aspect altogether. Banks understand the monetisation part well. For startups, the product becomes the hero but understanding what the bank wants or the risk parameters or the regulations or the cultural issues at the bank takes a back seat."

These comments indicate that mostly, collaboration seems to be the preferred option for both parties, as it gives an option for them to work together cost-effectively, sharing expertise and strength, rather than going for disruption, as it creates a more financially included society.

Example - The collaboration of Kotak Bank & Interface Business Solution (IBS) to create Kotak Jifi, a seamless banking experience with no minimum balance/charges. It is India's first digitally and socially connected bank account, where users had to sign in via Facebook, with the option to invite friends to join.

"We became the world's first bank to offer Hashtag Banking on Twitter, which led to many more such partnerships with fintechs. Such partnerships are win-win" said its Chief Digital Officer Deepak Sharma.

Infact, an [ET article] reports that digital transactions are expected to grow Rs. 800-1000 crore to Rs. 2500 crore, almost thrice the volume in the next few years through innovation & disruption, reflecting the need for digital transition.

Bala Parthasarathy, cofounder of credit app Money Tap, who has business ties with RBL Bank, even remarked how it's cheaper to take a loan from a bank once we qualify and manage to wade through the paperwork. Whilst highlighting this key role of banks in today's world, and partnership benefits, he went on to point examples of Lending Club, Prosper and few Chinese P2P lenders, and how these start-ups had a rough time before learning this aspect.

However, there has been a debate of rivalry too. ICICI's chief technology and digital officer Madhivanan, for instance, remarked against the collaboration sentiment and said, "There is nothing that a bank can't do that any fintech startup can. It's an issue of priority and striking a balance." Further, there are also instances where banks have blocked an external app such as Flipkart's PhonePe, Paytm, etc., showing this competitive vibe.

Prime Venture Partners' managing partner Sanjay Swamy has commented,"Of course, there is competition and some of it will play out publicly. But neither can do it alone."

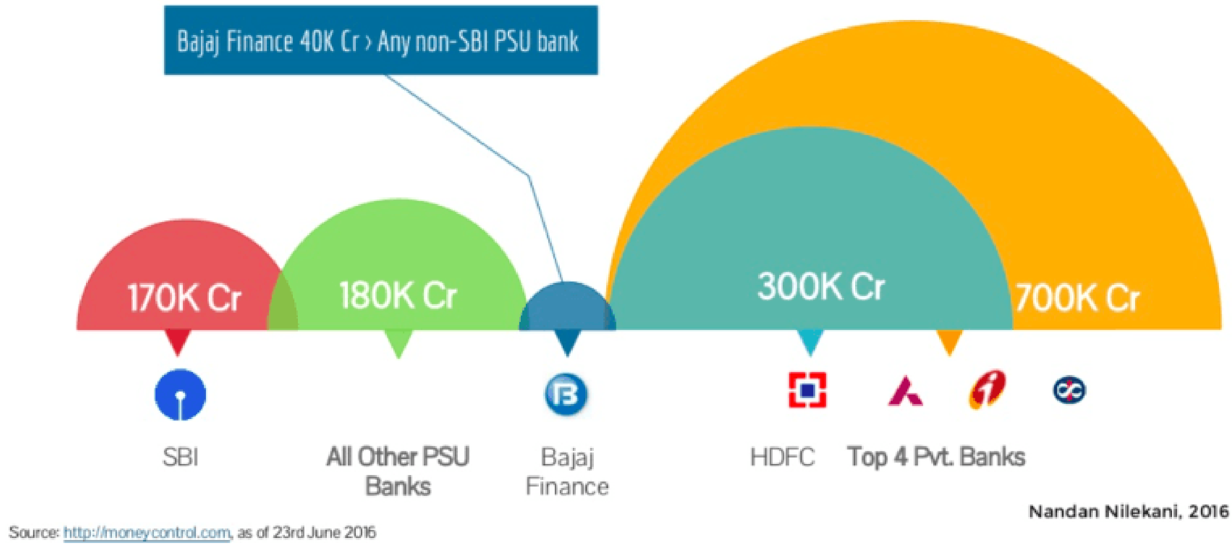
Thankfully, in India, if we take a look, there is already an open innovation at massive scale with interoperability built in, wherein govt. initiatives like UIDAI, UPI, NPCI, Aadhaar, India Stack, etc., have taken the momentum forward, making it available for everyone, leading the collaboration vision from the centre level. Such a progressive government at the center emphasising on the need for Digital India, and using the demonetisation reform to pull the strings, launching BHIM app, asking banks to go fully digital from onboarding to lending, etc., is definitely giving rest of the businesses an example to follow.

The fact that a central banking figure like Reserve Bank of India (RBI) supports this collaborative effort just like the government solidifies the premise. Former RBI deputy governor R Gandhi had remarked how banks and other financial institutions will highly benefit from adopting this burgeoning system, at both business and customer level.

A positive sign on this road map is the flurry of fintech initiatives taken by few of the private banks, showing their proclivity to modernisation and to experiment with new core banking solutions to keep up with the times. The fintech ranking site has an interesting article that takes a look at the fintech growth/strategy of banks, wherein examples such as quick digital bank set up, DCB's biometric ATM, wearable tech to earn and redeem points while walking, have been mentioned.

Despite being launched in the last decade or two, most of the private banks in India have come a long way in offering services, and achieving profitability, even surpassing the PSU banks: (images below)

Company Name	Net Profit (Ending Mar 16) (Rs. cr)	Net Profit (Ending Mar 16) $ Mn
HDFC Bank	12,296	1848
ICICI Bank	9,726	1462
Axis Bank	8,224	1236
Yes Bank	2,539	382
IndusInd Bank	2,286	344
Kotak Mahindra	2,090	314
Karur Vysya	567.63	85
Federal Bank	475.65	72
IDFC Bank	466.85	70
Source: Moneycontrol, LTP and goMEDICI.com analysis		



All these help us see how both individual efforts and partnerships are going hand-in-hand to keep the momentum running.

Let's look at few more examples:

- Kotak Mahindra-Deloitte partnership applied a blockchain trade finance solution, with a focus on end-to-end financing. "We are leveraging this technology to give our clients hassle-free and profitable trades finance solution on an almost real time basis," commented Kotak's President of Corporate Institutional & Investment Banking KVS Manian.

- YES Bank, likewise, has been part of both internal and external innovations in the fintech space. Its largest, transformational 'API Banking' to perform banking activities from client's own ERP system saw 62 users with overall throughput value over USD $750 mn (INR 5,000 crore), reducing Turn Around Time (TAT) days to hours, and increasing operational efficiency through auto-reconciliation.

- Transfer & Payment app Chillr has tied up with 10 banks on the IMPS platform, wherein its mobile app has over a million monthly active users, with monthly transactions recently crossing INR 500 crore.

- IndusInd bank offers an enterprise-wide, fraud management system that operates in real time across various banking products, channels, customers, employees and third parties, and this CustomerXPs' Clari5 solution has revolutionized fraud and AML management within the bank.

There are other tie-ups such as AI startup Active.ai's chatbots for banks, Signzy's digital onboarding and eKYC solutions, YES Bank - PhonePe partnership, etc.

While all this shows that the momentum has kicked in, for end users and customers, the product offering is what makes the cut, and whichever segment offers this to them, they get to win & embrace their loyalty. One thing is for sure, this promises a more diverse market with collaborations of all kinds, sizes, and niches, as -

- This gives scope for fintechs as well as young private progressive banks to make worthwhile contribution and be recognised for it, which is otherwise daunting in a world dominated by large and big players.
- Also for the rural population, institutions such as banks are held in high esteem, and trusted easily. To penetrate such a market with efficient services, this collaboration move could be the key.
- Even for bigger established banks, the pace of innovation is rather slow, as they focus on other operations and everyday BAU. With such impediments that could mire the fruition of indigenous solutions, co-operation and collaboration between banks and fintechs will be beneficial for both parties.

FinTechs, at one end, gain access to banks' scale of operations/customers, and banks get to capitalise on the modernity and expertise that fintechs bring in.

Where are international firms and investors:

The high barriers of entry in both B2B and B2C segments of the financial services industry that was prevalent earlier has been swept away post the fintech revolution, with both partnerships and solo offerings seeing mass adoption. Fintechs, as we have seen so far, have enabled financial services to be offered with ease, pace, transparency and convenience.

With rising demands, investments in the Indian fintech market have been pouring in. Global and local corporations/investors and VCs are making their way into Indian investment landscape, eager to tap into the vast user base, rising consumption, the yet unserved/unbanked population, whilst profiting from the country's tech-friendly regulatory environment.

With the startup scene gaining heat in the sub-continent, 2016 saw a 40% rise in the number of incubators and accelerators, making India inch to no.140, bagging the 3rd highest place of incubators/accelerators.

Payments niche, as we already saw, has been a huge hit, receiving the most funds within the fintech landscape, more so since demonetization. Now an user gets to pay for cab rides, hotel food, movie tickets, etc. using an app like paytm, along with making money transfers by just using a phone number, perform e-commerce transactions using wallets, or avail insurance or instant loans, etc.

However, other niches like Alternate Lending (which is coming second), Insurance, Banking, Investment, etc., are also joining in the funding race. In an interesting INC article, it points out to how even these comprise only 10% of the fintech space, with many more to come.

Most of the key investors, if we see, are investing across various companies in the Indian fintech landscape, which shows their belief and the potential of the huge fintech market in India. Let's take a look:

- As per a report by data platform VCCEdge, Indian fintechs have seen $2.35 billion investments across 325 deals, excluding Softbank's recent funding of $1.4bn in Paytm,
- As per PwC's 2017 Fintech India report, VC-backed global investment was a record high $14.6 bn in 2015, but dropping to $12.7 bn in 2016 due to global economic uncertainty as well as demonetization impact.
- With 370 angel deals in 2014 to 691 in 2015, investments also grew from $247 mn to $1.5 billion.
- Funding to private companies rose from $175 mn in 2014 to $2 bn in 2015, mainly due to the massive funding to Paytm and then went to $530 mn in 2016.
- Inc42 looks at Indian Fintech funding scenario for 2014-16, and reports $1.77 bn has been raised across 158 deals, with VC firms Sequoia Capital, Accel Partners, etc., along with Angel investors Mohandas Pai, Rajan Anandan topping the investment charts.
- Paytm's 2015 funding alone captures 38.5% of the total investment.

Let's look at few of these as examples:

Paytm

- In February 2015, Ant Financial took a 25% stake in parent company One97 to support the growth of its mobile payment and commerce platform in India, and in March, One97 had raised $200 mn.
- In September 2015, Alibaba Group invested another $500 mn, taking the total investment to $700 mn. This makes Alibaba Group the biggest stakeholder in One97 Communications, owning 40% of stake in the company.
- The fintech company, as we saw earlier, received $1.4 bn investment from Masayoshi Son's SoftBank Group Corp., the largest funding round by a single investor in an Indian startup.
- Other investors include SAIF Partners

Policy Bazaar

- In April 2015, this Gurgaon-based digital lending platform had raised $40 mn in a round led by PremjiInvest.
- Other Key investors include Tiger Global, Ribbit Capital, Inventus Capital Partners, and Intel Capital

MobiKwik

- In Series B April 2015, the company had raised over $25 mn led by Tree Line Asia. Other investors in the round included Cisco Investments, American Express, and existing investor, Sequoia Capital.
- In Series C January 2016, it raised $50 mn led by Japan's GMO and Taiwan's MediaTek. Existing investors Sequoia Capital and Tree Line Asia also participated in this round.

Lending Kart

- In Series A July 2015, this SME lender raised $10 mn from Saama Capital, Mayfield Fund, angel investor Shailesh Mehta, and Ashvin Chadha.
- In Series B June 2016, it raised $32 mn from Bertelsmann India Investments, with participation from Darrin Capital Management, India Quotient, and existing investors Mayfield India and Saama Capital.

Bank Bazaar

- In Series C July 2015, this financial marketplace company raised $60 mn from Fidelity Growth Partners and Mousse Partners. Existing investors Sequoia Capital and Walden International also participated in the funding round.
- Other investors include Amazon India

Capital Float

- In Series A February 2015, this Bengaluru-based company raised $13 mn, led by SAIF Partners and Sequoia Capital, with participation from existing investor Aspada.
- In Series B May 2016, it raised another $25 mn led by Creation Investments Capital Management LLC, with participation from existing investors Sequoia, Aspada, and SAIF Partners.

Vistaar Finance

- In September 2015, the company received an investment of over $30 mn from WestBridge Capital, with participation from other existing investors Omidyar Network, Elevar Equity, Saama Capital, and Lok Capital.
- Funding raised as of 2015-16 was $39 million.

Faircent

- It has raised $8.25 mn from investors incl. Aarin Capital, Brand Capital, JM Financial, M&N Capital Partners, Ad-for-equity investment arm of Bennett Coleman, Mohan Das Pai, Arun Tadanki, Doreswamy Nandkishore and Kshitij Jain.

Other examples:

Sequoia Capital has invested in companies like ApnaPaisa, Fintellix, Cleartax, Chillr, etc. Accel Partners has invested in Coverfox, QwikCilver, MoneyView, Chargebee, JusPay, Scripbox. Bangalore's credit app Money Tap, acquired by Glispa Global Group in 2016, had earlier raised $12.3 mn, with plans to expand across 50 cities in India.

SME Lender Neogrowth has received funding from IIFL Wealth Management Seed Venture Fund, Omidyar Network, Khosla Impact, Aspada Investment Co. IDG has invested in Fintellix, CreditMantri, Agile Financial Technologies, Heckyl. SAIF Partners has invested in Coverfox, Tracxn, etc., and Tiger Global has invested in Chargebee, Coverfox, Razorpay, MoneyView.

What are Aussie firms good at & where can they help:

Let's begin with KPMG's 3-step process that sets stage for digital innovation in the banking domain:

- ascertaining what needs to be changed, what services require a completely new model, and how to prioritise these based on user and business impact.
- exploring in-house expertise and identifying capability gaps to throw light on what needs external fintech partnerships.
- assessing future opportunities by transcending the immediate ecosystem to usher in newer services to stay ahead.

According to Mckinsey, digital Australia has the potential to contribute AU $140 to $250 billion to Australia's GDP by 2025, based on currently-available technology alone. It shows the kind of innovation and lead Australian firms have to aid the digital space here in India.

Infact, Australian banking industry is touted for continuing to perform well compared to its global peers at this age of financial disruption. Its major banks reported a cash profit after tax of $15.6 billion for the first half of 2017, up by 6.2% compared to 2016 first half year figure. According to KPMG, Australian banks are well capitalised with robust profits, and capability to meet new global capital/liquidity regulatory requirements.

If this is at one end, the fintech wagon too is picking up steam. Infact, nine Aussie fintechs have already featured in the H2 Ventures-KPMG's Fintech100 list of world's top innovators in 2016. Fintech firms including digital mortgage marketplace HashChing, Finnies/Telstra's Business Awards winner Prospa - an online SME lender, etc., have made it to this coveted list, wherein HashChing's co-founder and COO Atul Narang had said, "HashChing was included in the top 100 due to its unique business model, innovative use of technology, and first mover advantage in the fintech space."

At Telstra's NSW Medium Business Award show, Prospa co-founder/CEO Bertoli said,

"We've supported around 12,000 business owners, injecting more than $400 million into the Australian small business economy, but there are over 2 million small businesses across Australia, so that 'aha, we've made it' moment is, for us, a long, long way off."

While it is true that both sides of the coin are engaged in serious momentum, dominance of the Big 4 Aussie banks (National Australia Bank, Commonwealth Bank, Westpac and ANZ) in the land down under has also been evident.

With that in mind, this article, highlights, why is fintech slow in Aussie comparatively:

- Innovation from within the sector, reducing the need for cheaper & convenient options.
- Use of market power by traditional financial firms to maintain market share.
- Difficult market entry due to restrictive regulatory settings

Financial services, if we see, often run on the four pillars of payments, credit, wealth management, and risk mitigation. While in the rest of the world, Paypal in US, or Paytm in India, has shown strong fintech presence in the payments space, Australia has not allowed such dominance.

This is because Aussie's major banks have already spearheaded the niche with one of the world's most advanced online and cashless payments systems through

- Eftpos (electronic funds transfer at point of sale),
- PayAnyone (online account-to-account transfers) and

- BPay (online bill payments system)

That's a formidable place to be.

As for lending, the big four together are said to be controlling 80% of lending, and fintechs are emerging only across P2P Consumer/SME lending, where the major banks have voluntarily withdrawn, with their preference channelled towards mortgage lending. Therefore, companies like SocietyOne/RateSetter in consumer lending, OnDeck/ThinDeck in small business lending, and MoneyPlace in both consumer and small business lending, were able to establish themselves.

This is definitely an example of financial disruption allowing individuals/businesses to borrow/lend online. SocietyOne infact introduced P2P lending in 2012, followed by DirectMoney in 2014, the country's first listed marketplace lender, as these have the flexibility to offer differential lower rates, based on single case credit-risk assessments, which is not quite possible in a banking setup.

Direct Money's CEO Peter Beaumont had said,

"In response to the rising demand from consumer borrowers and the appetite from institutions to invest in the asset class, peer-to-peer platforms have increasingly become marketplaces for parties who were definitely not peers".

SocietyOne had likewise seen exceptional demand, with the company recently setting a new loan record of $250 million, which is the amount its investor funders have lent the borrowers.

Seeing such exceptional demands, banks are also looking at digital benefits to enhance customer experiences. If not all, at least the larger Aussie banks have made fintech a core part of their strategies:

- ANZ has been looking to capitalise and collaborate for digital investment and expansion;
- NAB has released PBOP - its personal banking origination platform, making it easier to opt for personal banking services;
- CommBank & Westpac has been looking at blockchain technology service;
- Westpac has even gone a step ahead to take a look at robots and drones.
- Fintech firm zipMoney and Westpac even went into one of the biggest deals recently, with the bank owning a 40 million equity stake.

The interest in fintech innovations is growing across the board, across all markets and other financial firms. Ex: insurance company Suncorp has developed a bill splitting app for mobile phones.

Aussie banks have infact invested much on the digital and mobile front that are a global first in many scenarios, such as the "pay anyone" online functionality, and having a world-leading mobile banking engagement. The rise in customer satisfaction scores from 66.8 percent in 2004 to 78.2 percent in 2012 shows the weight given to user priority and convenience by these banks.

In fact, in KPMG Banking on the Future Report 2017, edition 3, it mentions the crucial role played by customer experience (image below)

So, coming to the Indian side of things -

One of the dominating space of fintechs in India is in the payment space, and having an established and much coveted payment system back at Aussie, this is definitely a huge scope of opportunity for Indian banks to retain their share of payment space through effective collaboration. Customers look for easier and quicker payment options across multi channels and segments, and having their banks offer such seamless experience will create rippling demands.

As per a 2017 joint study by Assocham-EY, 19% of India is still coming under unbanked population. Despite financial inclusion through Pradhan Mantri Jan Dhan Yojana (PMJDY), there are still segments of people in remote areas with no access, and the ones enrolled are also still new to banking system. As per the 2011 census, 833 million are in rural areas and a significant number of them have little or no awareness of new-age banking services.

Helping banks to capitalise on these underserved segments of the population - in the rural, remote areas, more so women engagement, through targeted unique selling points could give a huge lead for the bankers in the country. As we saw earlier, even fintechs have not gone enough in this segment, leaving a part of the population almost unattended.

Payment banks, for instance, are in fact looking to cash in on this segment, so as to offer tailor-made products for bottom-of-pyramid (BOP), rural, the unbanked sect and women. This kind of smart segmentation along with advanced tech will help them achieve critical mass, requiring the banks to leverage on their existing resources or form fintech collaborations, where necessary, to gain that edge.

Reserve Bank of India (RBI) has already granted 'in-principle' approval to 11 payments banks in August 2015, wherein India's fintech giant Paytm and another fintech firm FinoPayTech are aiming for a launch this year. Airtel payments bank and India Post payments bank (IPPB), on the other hand, have already commenced operations.

So what Indian banks need now is a new and innovative approach to gain strong foothold to this class of customers.

A crowdfundinsider article, also suggests the need for India's banking system to be on top of security measures, while engaging in modern digitization strategies. So cryptography based collaboration and corresponding skilling is another highly beneficial area to address the concerns.

Speaking of concerns, lending owes in Indian banking is tremendous, and Indian fintechs have definitely capitalised on that opportunity. An efficient overhaul in the processing, as well as tailor making banking services for B2B segments will give them a lucrative opportunity to benefit from.

There have been examples of bank-within-the bank model, such as DBS Bank, which runs Digibank independent of its legacy environment. With its completely new technology platform, along with targeted, continuous delivery of small solutions, the newer model will help streamline each of its sub-niches almost in par with leading fintechs.

Let's now look at few use cases of leading Aussie fintechs, wherein each of them throw light on a fintech factor that could potentially suit the banking appetite of end customers:

- Afterpay offers a secure post payment method to its customers, wherein users have a choice to receive the product first, and pay for the products they want to keep within 14 days.

- Stockspot assesses customer risk appetite through an algorithm, automatically matching investors with independent, low-cost ETFs.
    - Robo-advisory based services, such as Stockspot, which eliminates human conflicts of interest in wealth management, and reduces investment fees could be a promising add-on for customers interested in trading and wealth mgmt.
- In the same trading niche, Simply Wall Street, offers snowflake maps indicating drivers of shares and equity market outlook.
    - The firm struck a deal with National Australia Bank's trading division, and it not only helped the bank to re-engage customers, but increased the user base of Simply Wall Street, mutually benefiting both parties.
- Identitii's blockchain software helps financial firms to exchange information on any transaction. This allows real-time verification and prevention of frauds, as it complies with the banking systems.
- Spriggy, pocket-money management app for kids aged 8-18 years, is another interesting fintech innovation that targets parents and young people alike to manage money together.

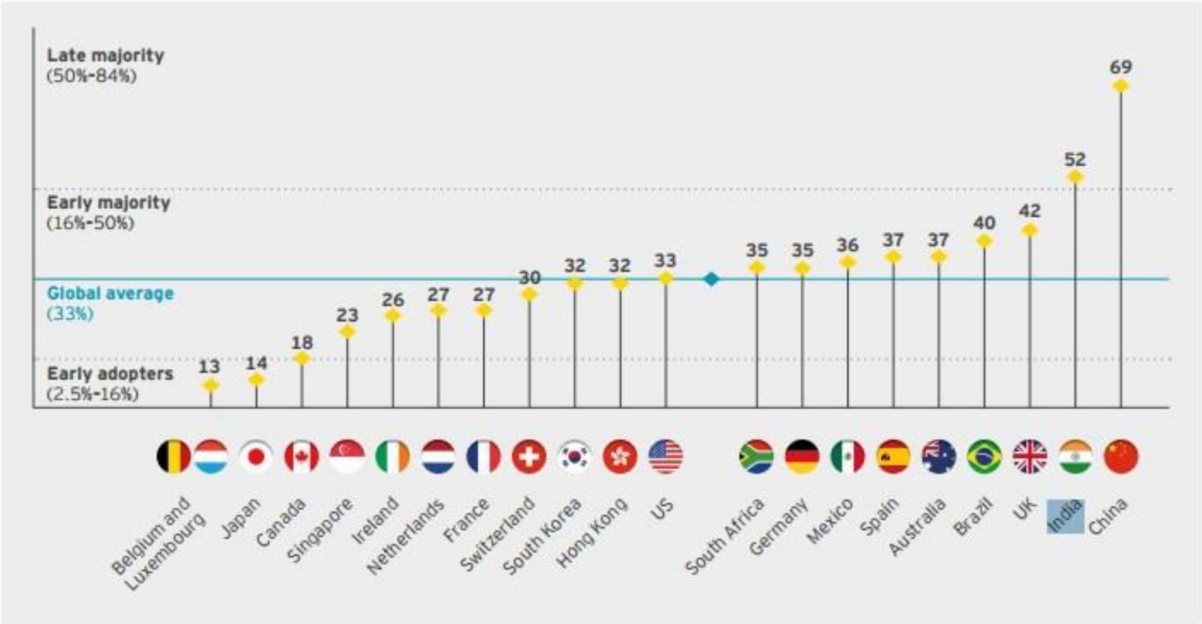
These are just few scenarios, but there could be several such integration in terms of risk management, advisory, etc., propelling the Indian bank growth trajectory to go up by several notches due to its 'fintech' factor.

Conclusion:

India, as we have seen across our various insights, is in its exponential growth phase, and its various reforms under the new governmental regime is offering beneficial business environment with bigger and better opportunities for international business relations.

In the EY FinTech Adoption Index 2017 report, it mentions that India has an adoption rate of 52%, second only to China's 69%.

Figure 3: **Progress of FinTech adoption globally and across 20 markets**



Notes: The figures here show global adoption rates for 2017, including adoption rates for each of the 20 markets, plotted against stages of the innovation adoption curve. All figures are shown in percentages.

Let's look at some numbers in India's digital revolution:

- More than 200 million bank accounts have been opened in just one year. Thanks to PMJDY, this is more than the no. of bank accounts in the U.S.
- More than 300 million new debit and credit cards have been issued in the last four years, bringing the total number of cards to more than 600 million.
- India is now the world's third largest market for smartphones with over 300 million users and UPI* could turn each of those phones into a bank. Infact, wallet users of fintech company Paytm alone has crossed 200 million users.

*UPI or Unique Payment Interface allows money transfer to another person's bank account or financial instrument of choice through mobile number input. Because of its open API, within four weeks of its launch, dozens of apps by smaller teams saw the light of day. Such has been the giant leaps by India on various initiatives such as GST, Aadhaar, etc., which will benefit the economy with its cumulative effects of return.

If Indian banks were to join the UPI platform, they will be posing a formidable challenge to fintechs, as the array of other banking services add further to their strength. Since banks already enjoy a level of customer trust and confidence, it also gives them a definite head start. It could perhaps only be a matter of time before these banks attain technological finesse, and we are already beginning to see some aspect of digital innovation from Indian banks in both private and public sectors.

However, it is now crucial for banks to capitalise on their innate strengths such as reach, customer base, resources, etc., and combine that with digital agility and drive. While cost reduction might play a role in current profitability, growth initiatives in the new niches of block chain, cloud, robotics, etc., could give them the desired leap in the foray of being a financial leader at such changing times.

From an Aussie perspective, joining in Asia's highest growth phase and a huge user base will return benefits by leaps and bounds. Aussie's trade relations with Asia already grew on an 18% yearly avg. in the early 2000s, from USD 46 billion in 2002 to USD 250 billion in 2012.

When India is in fact giving the world's highest fintech ROI at 29%, it all the more proves the potential of this vast market. With rising income levels, expanding population, and increasing demand, a business integration with India is both instrumental & inevitable for Australia's growth story, be it in terms of trade, capital, or people, and the time is now.

Tat CAPITAL
Corporate Finance & FX Advisory

Phone: +612 8387 5901 | Email: info@tat.capital | Website: www.tat.capital
Address: Level 14, Suite 1403, Spring Street, Sydney, NSW 2000, Australia