Redefining the Indian payments space: Partnerships between big techs and conglomerates

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Foreword

Dear readers,

It is my pleasure to bring to you the latest edition of PwC's Payments newsletter. In this edition, we explore the entry of big techs, their partnerships with conglomerates and the implications on the digital payments industry.

In addition to our views, we have captured insights into market forces that make the FinTech and digital payments industry lucrative and explored the way forward for the industry based on our experience across the payments landscape.

I hope you will find the newsletter to be a good and insightful read.

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Introduction

Introduction

A big tech company is essentially one of the biggest and most dominant players in the information and technology (IT) space.[1] Traditionally, leading technology and social media companies were identified as big techs, though over-the-top (OTT) media platforms, energy companies and online marketplaces have also been identified as big techs in recent times. These companies boast of deep technological expertise, vast balance sheets, huge repositories of customer data, wide customer reach and a knack to develop disruptive technologies that have the potential to disrupt the way any industry functions.

Financial services have been riding this wave of technology-enabled disruption for nearly a decade now. The processes of financial services transactions and distribution of products have undergone a complete transformation from a channel perspective to how banks store and process transactions and data (cloud storage, data outsourcing, etc.).

Digital payments is a specific area within financial services that has received immense traction from technological innovation. The methods of initiating, sending, processing and settling payments have been revolutionised in the past few years. In each step of the payments value chain, both technology and market reach have played important roles in streamlining and innovating legacy processes, which in turn have resulted in convenience for end users to access payments services. Omnichannel models where customers initiate transactions on one channel (online/physical) and complete on a different (physical/online) one are prime examples of enhanced customer experience.

1. https://www.pcmag.com/encyclopedia/term/big-tech

In addition to enabling technology-led payments adoption, big techs have developed their own digital payment platforms. Many big techs have also partnered with banks to offer both digital payments services and physical payment modes like co-branded cards. In such a model, banks primarily act as the backend processing unit whereas the user interface (UI)/customer interface is provided by big techs.

More recently, big techs have also started providing digital payments offerings in partnership with large conglomerates. The combination of big techs' technology prowess, large repositories of customer data, large domestic reach and market offerings by conglomerates enables a partnered payment offering between the two to quickly penetrate the market and reach a wider audience in terms of acceptability and usage. Such partnerships have paved the way for newer payments use cases, technology-led enablement and more importantly, faster go-to market times and wider acceptance rates.

Introduction

Apart from the technology prowess of big techs, they are being able to penetrate and scale the payments market so quickly because of the following reasons:

1	2	3	4	5	6
High capital availability of big techs.	Most big techs are not completely regulated by central banks (or other regulators) and have a better leeway to innovate the payments market.	The business model is primarily platform based. This is a key factor as financial institutes find synergies when partnering with a diversified conglomerate, wherein payment offerings can be easily extended to the existing customers of the conglomerate.	Customer data is readily available with big techs which can be analysed to understand customer behaviour, needs and wants – critical factors for success in the payments ecosystem.	Most big techs have a huge customer base that they can leverage to commercially distribute payments offerings to end users.	Although the margins in payments are wafer thin, big techs work on the objectives of customer acquisition, and gathering and utilising payment data to build other profitable overlay services rather than immediately generate revenue.

Market forces making the payments industry lucrative

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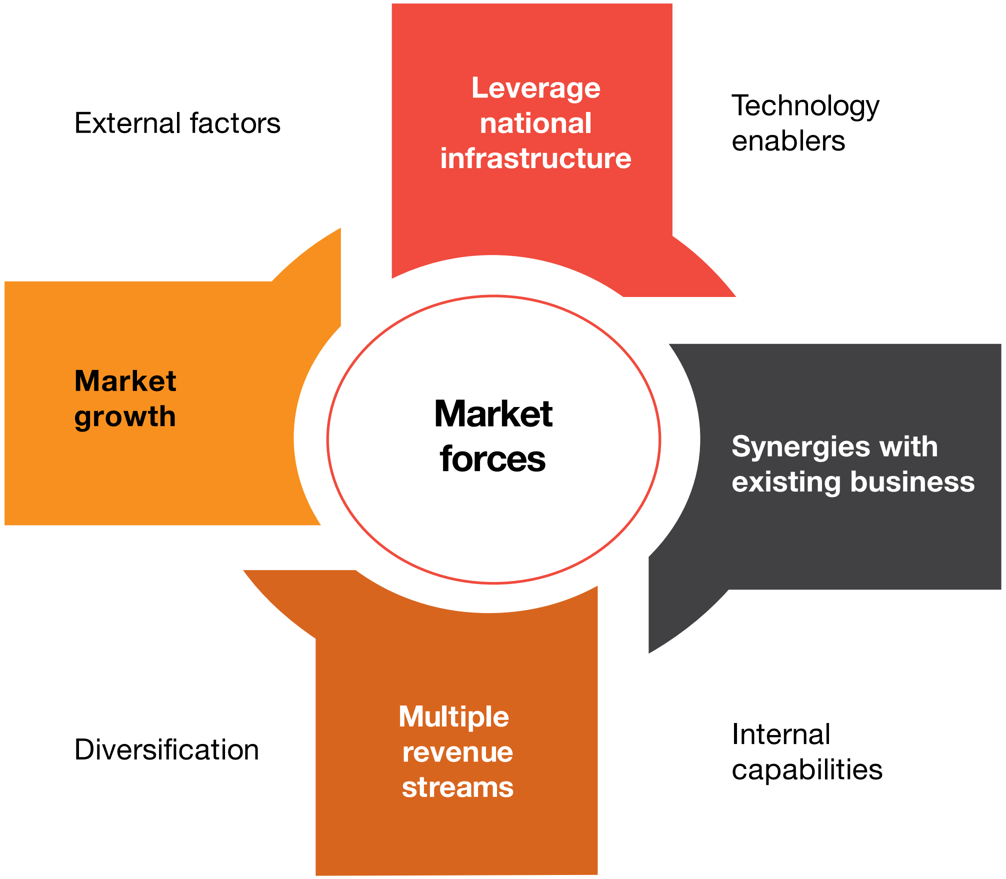


Source: PwC analysis

The payments industry in India is attracting the attention of many big techs who are looking to develop innovative payments products and enter the market. These companies anticipate to find a range of opportunities to leverage their existing capabilities in the Indian payments space.

External market forces such as the existing national infrastructure of Unified Payments Interface (UPI) and the Jan Dhan-Aadhaar-Mobile (JAM) trinity, along with the emerging market and its growth potential, make the Indian payments industry a lucrative area for investment. The payments industry is one of the leading industries in the financial sector that enables big techs to derive synergies with their existing internal capabilities. Big techs and conglomerates find it to be a good diversification option in terms of both increasing their respective consumer bases and business streams.

1. Synergies with existing businesses

- **Technical capability:** Big techs have strong infrastructure capacities such as cloud, strong computational power, highly skilful employees, innovation labs, along with the experience of working in different business spaces. The combination of all these factors helps in diminishing the entry barriers into the payments industry.

- **Leveraging customer base and data:** Big techs have huge customer data to explore detailed behavioural analytics that could be leveraged for the payments industry. For example, a leading cross-platform messaging service has over 400 million users in India.[2] Such a customer base helps in having customer-rich information and smoothens the customer acquisition process.

2. https://techcrunch.com/2019/07/26/whatsapp-india-users-400-million/

Market forces making the payments industry lucrative

- **Financially strong to survive losses due to low margins:** Big techs usually have strong financial backing. This gives them a competitive advantage over legacy players in the payments industry as well as smaller companies and start-ups that struggle to survive in this extensively competitive industry that has a long break-even period.

2. Huge market/growth potential

The digital payments industry has a huge market size as well as significant growth potential that attracts big techs. As per a report by the Reserve Bank of India (RBI), digital payments crossed 200 billion transactions per year in India and grew at a compound annual growth rate (CAGR) of 11% in the last 5 years.[3] The deepening of digital payments, along with Government efforts to strengthen this sector, has given investment opportunities to big techs.

With big techs entering the payments market, the opportunities are only bound to increase as more than 80% of the transactions in India are yet to be digitised. India has a huge set of small offline merchants who are still untapped and waiting for a technology innovation for them to be brought into the digital payments spectrum – a potential opportunity big techs can look to tap into.

3. Leveraging national infrastructure: JAM trinity, UPI, low cost data and connectivity

India has invested in building a strong digital infrastructure that can be leveraged by big techs and integrated with user-friendly application programming interfaces (APIs). Such infrastructure eliminates high capex requirement and risks associated with building a new infrastructure for payments. Moreover, JAM trinity and the availability of low-cost internet have digitally enabled customers. This allows big techs to innovate and get customers onboarded smoothly and quickly.

3. https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/CDDP03062019634B0EEF3F7144C3B65360B280E420AC.PDF

Market forces making the payments industry lucrative

4. Multiple revenue streams

In the payments industry, data leads to the building of newer revenue streams and big techs who have a repository of big data can leverage it to build more overlay and value-added services. This can be used for personalised engagements with customers and enabling cross sell and upsell of additional services.

Payments-related data is crucial for other industries for customer profiling, assessing payments in supply chains, assessing credit worthiness of individuals, drawing customer insights and developing new products. This opens multiple partnership options for big techs.

The data is also used for refining their artificial intelligence (AI) and machine learning (ML) capabilities (which a lot of other players struggle with) that will eventually help them in building multiple revenue streams in the low profit margin payments business.

Impact on the payments industry

Impact on the payments industry

Big techs and conglomerates are expected to have a disruptive impact on the payments industry. They are expected to penetrate the market and create new business opportunities in the industry. Their participation will also speed up the consolidation of the industry. Big techs entering the payments market will have the following impact on various payment players:

Customers

Big techs and large conglomerates will bring reliability to customers, along with providing them with payments-related services. Customers will trust these players more with their data and bank account details as they are familiar with these organisations. It will also be more convenient for users to make payments with messaging or social media platforms as these are more integrated with their personal lives and existing lifestyles.

The partnerships between big techs and conglomerates will be able to penetrate the segments financially excluded by traditional players, resulting in comprehensive financial inclusion

The focus on customer engagement by big techs will enable them to build more intuitive and well-integrated UIs for smoother transaction flows. Big techs also offer effective and responsive customer services. This will potentially lower the attrition rate of customers adopting digital payments.

Competitors

Big techs and conglomerates will have a significant impact on their competitors. For example, a leading Indian digital payments company saw the market share of its digital payments reduce to just 16% in July 2019,[4] compared to two of its competitors that had a market share of 35% each (out of 822 million UPI transactions).

The entry of more big techs in the payments space will lead to more mergers and acquisitions (M&A), and collaboration opportunities for industry players such as payment gateways, aggregators, traditional issuers and acquirers.

4. https://economictimes.indiatimes.com/small-biz/startups/newsbuzz/upi-usage-soars-but-paytm-share-sinks/articleshow/70580450.cms

Impact on the payments industry

Banks and other traditional players

Banks are evaluating the impact of big techs entering the payments industry. While some have already partnered with big techs, a few others have initiated discussions to explore technology partnerships. They would like to leverage their coopetition (competition + cooperation) relationships with big techs and conglomerates to extend their services to a larger population.

There is a huge segment of customers who are deprived of basic banking facilities and services such as credit due to stringent know your customer (KYC) norms, poor credit history and unavailability of proper documents. The highly regulated structure of banking operations often makes it difficult for the unbanked and underbanked population to avail banking facilities and services.

Big techs leverage technology such as natural language processing (NLP) for documentation, AI/ML to check payment data and determine credit worthiness, and video-based KYC checks. Partnering with banks and financial companies allows big techs to process applications faster and quickly disburse credit. This ensures that the unbanked and underbanked segments get access to credit.

Small and medium enterprises (SMEs) and micro, small and medium enterprises (MSMEs) are unexplored segments for banks and financing companies. Government-run schemes such as loans issued by the Micro Units Development and Refinance Agency (MUDRA) cater to the needs of MSMEs. But since most MSMEs have an informal way of conducting their operations, it is difficult for banks to monitor their financial activities. Big techs can onboard these MSMEs for payments and provide a comprehensive overview to banks about their payments/financial operations. This will help banks to flag possible non-performing assets (NPAs), monitor their financial performance, engage in upselling and have a better engagement with MSME clients. With traditional players partnering with big techs, a number of newer business opportunities are expected to open up.

Impact on the payments industry

New business opportunities

The entry of big techs will open up new business opportunities for the payments industry.

Big techs have good capacities and financial resources to invest in disruptive technologies such as blockchain payments. They can build anti-money laundering (AML) and fraud investigation tools by leveraging payment data sources. The entry of big techs and large conglomerates is expected to bring innovation in the payments domain and newer ways of enabling various payments processes.

Since big techs are present in multiple countries where they provide their payments services, cross-border payments is another area that big techs are expected to explore. Current regulations and AML checks are the barriers for this market. If big techs can figure out a way to adhere to such regulations, they can provide less time-consuming and cost-saving cross-border payments services.

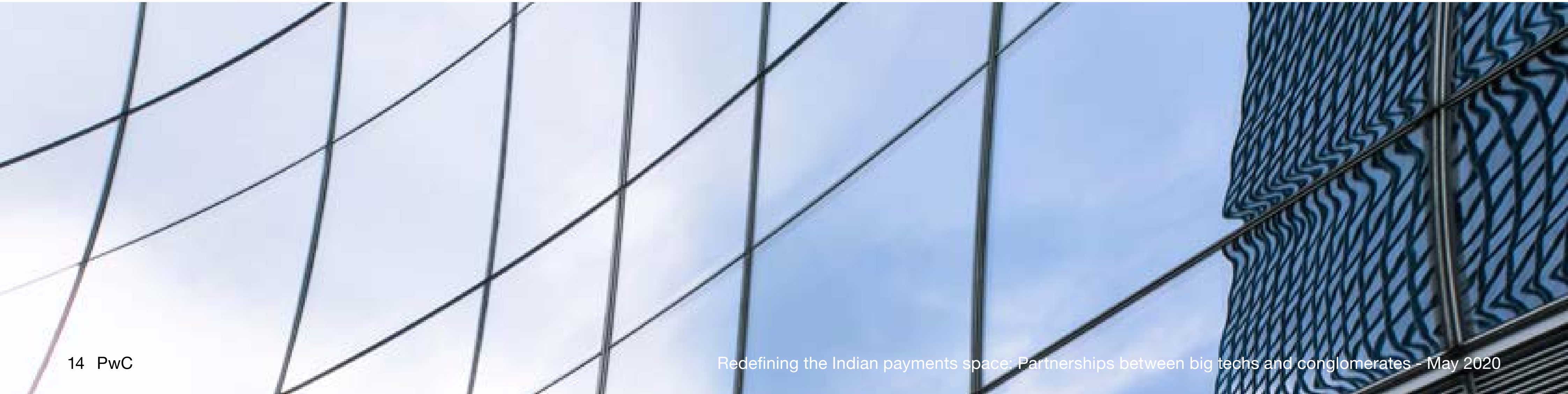
Regulators

The payments industry is rapidly emerging and evolving. Thus, regulations around payments must also be updated accordingly to ensure that the industry thrives and the rights of the common people are protected. The involvement of big techs is very crucial to form a robust policy structure for the payments industry.

Regulators must be watchful of big techs entering the payments industry. They must regularly monitor the activities of these players and gradually bring them under the regulatory ambit.

Regulators must also ensure fair competition among all the players in the payments industry. They must look to protect domestic payments players who might feel intimidated with the arrival of cash-rich big techs. Data localisation norms formed by the RBI are a small step in this direction.

Currently the RBI has a complaint management system for e-payments. It is expected to cater to new innovative payments products launched by big techs and conglomerates entering the payments industry.



Way forward

Way forward

With the tech-conglomerate partnerships gaining traction, the following use cases are picking up pace in the payments space.

Customer data led innovative payments offerings	With the potential amalgamation of big techs and conglomerates into a single platform, there are possibilities of conglomerates effectively using the customer data of big techs to offer innovative payments offerings and refine user journeys. However, to achieve this, it is important that there is seamless sharing and processing of customer data at both ends.
Tech platforms will play a big role in payments services	Technically advanced payment platforms will be playing an important role to bring multiple merchants and users on a single platform. Partnerships with big techs will enable conglomerates to extend their services on a widely-used technology-enabled platform service.
Overlay services	Big techs offer an opportunity to conglomerates to build overlay services on top of their payments services that can be easily integrated with multiple partners using open APIs. These overlay services, when integrated on a common platform, have the potential to enhance margins for players by being a one-stop application for users, given the business and technical synergies between big techs and conglomerates.
Potential international reach	For any firm, global expansion is a time-consuming and risky proposition involving multiple complexities which include factors like costs, regulations and competitor risks. Due to the inherent global reach of most big techs, it becomes easier for conglomerates to utilise big tech platforms to offer their products and services to a global audience.
Data analytics	One of the most important resources possessed by big techs is the vast amount of customer data. Big techs have concentrated heavily on data analytics techniques like data visualisations and predictive analytics using tools like AI and ML. With these data analytics techniques already integrated in big tech platforms, conglomerates will be able to utilise these tools for contextulaised sales and marketing of payments services.
Single super payments application	Due to the vast amount of financial resources available with both conglomerates and big techs, a partnership between them has the potential to break industrial and geographical boundaries. If factors like disparate global regulations become favorable, it is possible that such partnerships can result in the development of one-stop global payment super applications that can include newer use cases like cross-border peer-to-peer (P2P) payments.

Payments news updates

Payments news updates

Amazon Pay Later launches in India

Business Traveller

E-commerce giant Amazon has announced the launch of its credit service called Amazon Pay Later in India. Under this, customers can avail instant credit that they can use to buy daily essentials, electronics and clothing items among others.

Read more.

Jio-Facebook deal likely to boost adoption of crypto-blockchain in India

Business Standard

Deal may result in Jio piloting a cryptocurrency that can be used for discounts or reward points within its telecom, entertainment and e-commerce spaces once regulatory hurdles are cleared

Read more.

YouTube adds UPI as a mode of payment for Indian users of YouTube premium

Business Line

YouTube has launched Unified Payments Interface (UPI) as a mode of payment for its users in India for both YouTube and YouTube Music

Read more.

Google could soon launch a Google Pay-based debit card

Money Control

Money Control

Google could soon enter the smart payments card business to compete against the likes of Apple and Huawei.

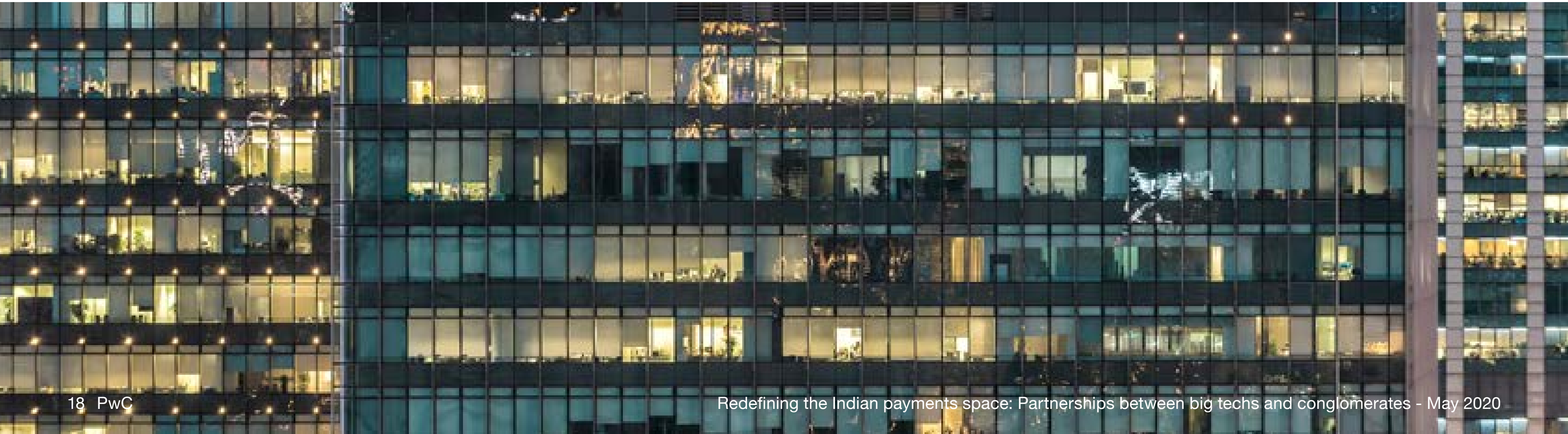
Read more.

Google Pay, India's PhonePe - most frequently downloaded apps in February 2020

The Paypers

Google Pay has been reportedly the most downloaded Fintech app (globally) during February 2020 with 15.6 million downloads, according to Crowdfund Insider.

Read more.



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