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THE WAY FORWARD FOR INCUMBENTS IS TO BUILD A DIGITAL PLATFORM, ADOPT FINANCIAL TECHNOLOGIES AND COLLABORATE WITH FINTECH COMPANIES.

The FinTech sector in India has seen a funding boom in the last five years, with funding increasing at a CAGR of 98% in the past six years . Today, there are more than 1200 active FinTechs in the country and their number is growing constantly. FinTechs are continuously trying to decrease their customer acquisition cost along with enhancing their customers' experience with the help of technology. Moreover, innovation among startups has disrupted the traditional financial services value chain, brought in new customers, caused incumbents to scale up their operations, and ultimately created multiple options for customers.

Setting the context

The Government of India has taken multiple initiatives to boost last-mile connectivity and include the financially underserved in the economy. Some of these initiatives include implementation of several schemes, the establishment of government-backed institutions and encouragement of differentiated business models such as payment banks, non-banking financial institutions and small finance banks. This has been amplified by FinTechs, most of which are supported by government initiatives such as Aadhaar and IndiaStack. FinTechs are using digital customer on-boarding techniques, which have proven to be cost-effective compared to traditional methods. They are serving last-mile customers with the use of feature phones and the help of a one-time password (OTP) to process transactions.

Sectors snapshot

The FinTech landscape in India has witnessed a notable rise in digital payments and alternative len ding modes in the last couple of years. Government initiatives such as the introduction of UPI and P2P payment guidelines by the RBI have been the key drivers of growth. Other trending sectors include insuretech, wealthtech and regtech, which have seen a positive growth in funding during the past few months. However, while FinTechs have seen significant traction in the market, there is still substantial headroom for growth in the segment, compared to developed countries such as the US.

Digital payments

Digital payments have been dominating India's FinTech sector in terms of funding and usage. Several FinTech companies such as PayTM, Google Pay and Amazon Pay are trying to reach the last mile with the help of advanced technology. And the availability of multiple payment mechanisms such as UPI, QR codes and wallets, with services available on several platforms for users, make them popular, compared to the offerings of traditional financial institutions. These new age FinTechs have also developed solutions that work offline (e.g. kirana stores, MSMEs, toll and transit and smart cities), and online modes (e.g. eCommerce and government tax payments). This has resulted in reduced usage of cash, which has declined drastically in the last couple of years from 78% to 68% . According to NITI Aayog's report titled, Digital Payments – Trends, Issues and Opportunities, the digital payment sector in India is projected to reach US$1 trillion with the share of mobile payments rising to US$190 billion by 2023.

Alternative lending

Alternative lending is the second highest funded segment in FinTech after payments. According to The Economic Times' Prime Research report, alternate lending start-ups received US$288.4 million in funding in the first six months of 2018 for 36 deals. Ten years ago, getting a loan was a cumbersome process and borrowers had to approach banks for loans with proof of their credit-worthiness. New age lending startups are coming up with alternative credit scoring models to bridge the credit-supply gap of US$230 billion in the MSME sector by using technology and reaching out to people with thin-file credit histories. Moreover, with the RBI deciding to regulate P2P lending in the country, more and more startups are entering this sector and the market is expected to reach US$4-5 billion by 2023.

InsureTech

InsureTech in India has seen a huge growth in this last one year. In view of the ultra-low penetration of insurance in India (2.76% in life insurance and 0.93% in non-life insurance), the sector presents a significant opportunity to players to tap the market with new-age solutions. According to Venture Scanner, insuretech in India has seen total funding of US$462 million till the first half of 2018 with the presence of 66 startups. New age startups are using multiple platforms to cross-sell their products. Consequently, with the introduction of micro-insurance, context-based insurance and insurance in a sachet concept, more and more customers are attracted to the segment.

RegTech

The financial crisis in 2008 was the greatest learning for regulators around the world and has motivated startups to find their roots in Regtech, since with ever-changing regulatory requirements, traditional players need to comply with regulators' standards. RegTech startups are focused on improving the way in which they manage compliance requirements by breaking down statutory obligations into easily understandable workflows and automating these aspects of reporting with the use of data.

FinTechs in these sectors make use of products such as chatbots, trading platforms and investment products. They have also created marketplaces to sell the products from different sectors. Such marketplaces offer financial services and products such as insurance, credit cards and loans under one roof, which makes them popular with customers.

Ways in which incumbents can respond to the FinTech challenge

Considering current trends in the FinTech industry, traditional BFSI players are looking at these options as a risk to their business. And while incumbents have been largely focusing on the profitable segments, FinTechs have reached out to the underserved and have carved a ni che segment for themselves. According to the Global FinTech Survey conducted by PwC with senior executives from the financial services industry, more than 80% believe that their business is at risk. According to 56% of the respondents, their companies have disruption at the heart of their strategies; 82% expect to see increasing partnerships with FinTechs in the next five years.

We see traditional players responding these risks in three ways.

1. Collaborating with FinTechs

In the present scenario, a collaborative approach is seen as being best suited to the needs of traditional players in view of their lack of the required skillsets to build FinTech-like models and the investment associated with this (refer Fig 1). Traditionally, there has been significant resistance from traditional players to innovate due to their:

1. Resistance to change
2. Operational inefficiencies
3. Lack of innovation culture in their top management

According to Prof. Jean-Philippe Deschamps' Innovation Governance Model, innovation needs to be driven by top-level executives in a company. In addition, to make it more effective, innovation needs leaders with a high degree of consistency in their priorities, messages and actions.

Traditional BFSI players that imbibed innovation in their culture have had a first mover advantage. Among one of the companies PwC surveyed was a leading investment bank in India whose innovation culture was driven by its top management. The bank decided to put in place an innovative culture and collaborated with PwC to transform its operating model by embedding in it new-age solutions, based on technologies such as Artificial Intelligence and machine learning. There were 50+ brainstorming sessions conducted to generate ideas across the bank's different divisions. These ideas were then categorised into different opportunity themes. Applications were invited from startups that were capable of implementing the ideas. The programme received applications from 150+ startups and 1 out of 3 start-up applicants were based outside the country. After multiple levels of filtration, the best startups were shortlisted to test the idea at the proof-of concept stage. The successful ones were then tested at their pilot stage and embedded into the system.

The programme can be considered a success story due to the participation of multiple international startups that would otherwise not have been considered for a partnership by the investment bank. What is important is that the push to drive innovation came from the bank's senior management in collaboration with PwC, which was the key cause of its success.

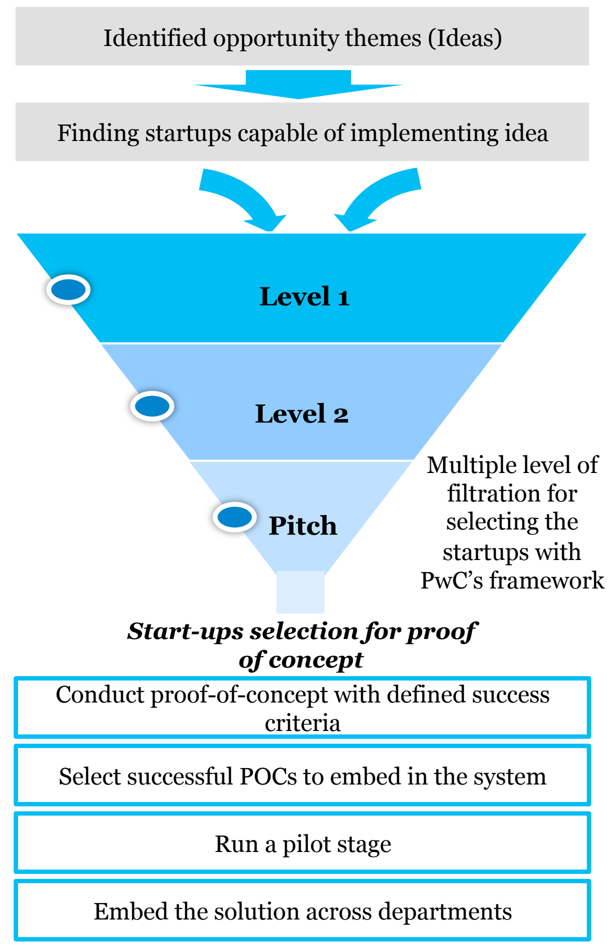

Fig. 1 Collaborating with FinTechs.

2. Building FinTech-like businesses

Building FinTech-like businesses (Fit-To-Disrupt strategy) is another way for incumbents to respond to the upcoming FinTech challenge (refer Fig. 2). Some traditional banks have opted for this strategy to create their own wallets and lightweight digital account-opening options for their customers. On other hand, some NBFCs have created online or mobile lending options, which complete loan processing within a few minutes.

To build FinTech-like businesses, BFSI players (producers) can opt for strategies including revamping their existing businesses or launching new divisions or brands. This will be an added advantage for incumbents to tap an additional set of customers from their competitors and thin file/new to credit customers. However, while opting for any of these strategies, incumbents need to build certain capabilities, keep-

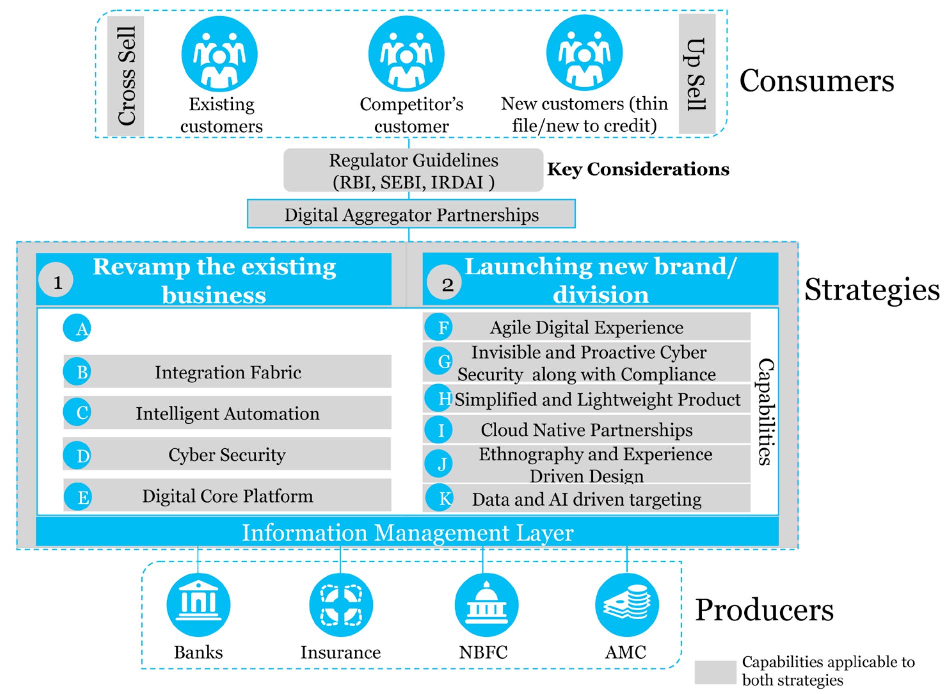

Fig. 2 Building FinTech-like businesses.

ing the regulatory paradigm in mind. They should also conceptualise their strategies and have in place programme management skills and an encompassing innovation culture in their organisations. To do this, they need an outside perspective. This role can be filled by consulting firms. PwC has wide experience in helping incumbents across multiple private sector and investment banks, government-backed SME lenders and broking houses strategise such initiatives.

3. Product platformisation

We see product platformisation as the third-best way for incumbents to respond (refer fig. 3). There are four disconnected but conjoined trends we have been observing in the FS ecosystem:
1. Huge amount of data generated via digital touch-points
2. Emergence of aggregators enabling access to consolidated and segmented SMEs
3. Need for agility and efficiency in driving partnerships across the ecosystem
4. Industry focused aggregators providing access to retail consumers for targeted marketing

These trends have created an opportunity for incumbent Financial Services organisations to partner with digital first aggregators (in the financial and non-financial segments) and create targeted product offerings to deliver to end consumers, and thereby achieve enhanced scale and cost efficiencies.

This can be realised by creating an autonomous digital platform that can integrate with manufacturers of products on one side and digital aggregators on the other. The platform can be powered by an intelligent analytical engine to generate relevant, contextual and need-based product offers for end consumers.

From the perspective of technology, most digital aggregators are already operating in an API-based ecosystem. And with an increasing number of incumbents jumping on the API bandwagon, the time to market to realise such partnerships via the platform has also decreased considerably, enabling accelerated integrations and value creation.

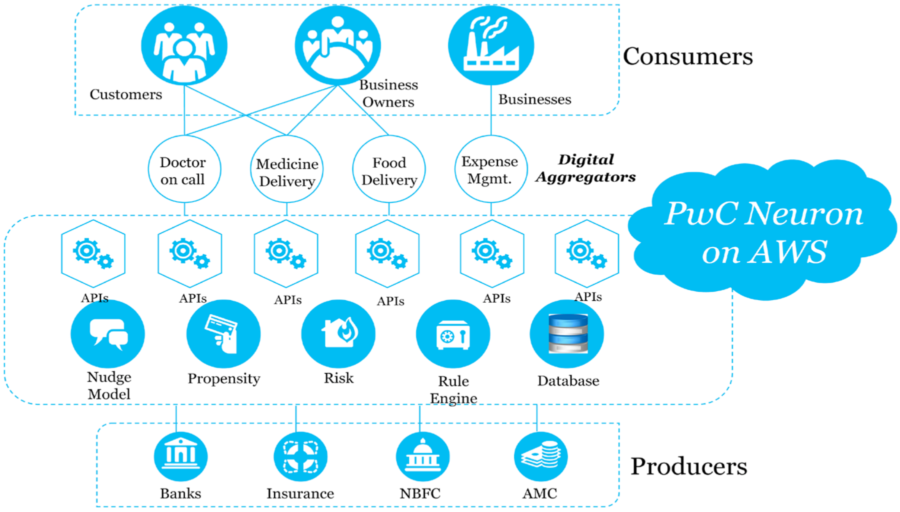

Fig. 3 Product platformisation.

Overall, the platform will give incumbents increased access to the market through partnerships and improved efficiencies in customer acquisition. For aggregators, the platform will provide an alternative revenue stream with minimal friction and time to market, targeted outreach, increased engagement and delivery of value to their end customers. PwC has created its own platform on AWS, PwC Neuron, which helps incumbents consume products directly via APIs and on-board quickly.

The following is the key to unlocking potential in new financial service products:
1. Focus on selling through digital channels Base your go-to-market strategy entirely on digital channels, focus on customers' behaviour and create experiences on screens that will delight them.
2. Replicate sales intelligence through 'nudge' models

Your digital platform should have intelligence built in to target customers at the right time with the right message, which can attract their attention and get them hooked.
3. APIs to reduce time to market through partnerships

Availability of APIs will make it plug-and-play model for you to get on-boarded easily and reduce time to market drastically. There are several digital touchpoints available through which one can connect with customers these days. However, to make such partnerships successful, swiftness in integration through APIs is essential.

Conclusion

Considering the favourable environment for FinTechs in India, many of them are coming up with disruptive solutions across the sectors. Moreover, increased funding by investors in the past few years has motivated startups to strive and create solutions to reach last mile customers with the help of technology. It is clear that to remain competitive and relevant in the market, all incumbents, irrespective of their size, will have to focus on innovation. They will need to look at it from a long-term perspective and enter strategic partnerships with innovative startups or initiate and implement their own solutions. They can also opt for product platformisation solutions to ride the FinTech wave.

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Vivek is a part of PwC's Global FinTech Council and has published Thought Leadership reports on FinTech in India. He is an active speaker on FinTech and works with multiple FinTechs. Vivek has over 18 years' experience in working with the Government, regulators and the Financial Services industry to utilise data, analytics and technology, drive business transformation and create new business models, while complying with regulations and delivering social impact.

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