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EVENT REPORT

CONFERENCE ON UNLOCKING THE POTENTIAL OF NEW AGE FINTECH:

Towards an Inclusive, Innovative and Progressive Ecosystem

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Conference on Unlocking the Potential of New Age Fintech:

Towards an Inclusive, Innovative and Progressive Ecosystem

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1 | Introduction

The digitisation of financial services and payment systems has significantly contributed to the economic growth of India. One of the reasons behind rapid increase in financial inclusion is the pace of fintech innovation and the underlying infrastructure. Innovative offerings by fintech companies coupled with the proliferation of digital public infrastructure (DPI), especially UPI, have led to the development of inclusive payment solutions for previously unreached populations. Driving the next phase of financial inclusion would require the confluence of all stakeholders in charting the way forward and addressing the concerns.

In light of the evolving fintech landscape, The Dialogue hosted a conference on August 1st, 2024 titled *"Unlocking the Potential of New Age Fintech: Towards an Inclusive, Innovative and Progressive Ecosystem",* bringing together leading experts from the fintech and financial services sectors to explore the challenges and opportunities in the industry. Over the course of the keynote address and the two panels, experts delved into the intricacies of the fintech sector, its potential in driving the financial inclusion, role of the regulator and DPI and the need to address the challenges related to financial fraud to gain trust of the consumers.

The keynote address was delivered by **Shri Baijyant Jay Panda, Member of Parliament, Lok Sabha and National Vice-President, Bharatiya Janata Party (BJP)** Subsequently, the first panel titled "Driving the next phase of financial Inclusion: Role of DPI and Fintech" was moderated by Mr Kazim Rizvi, Founding Director, The Dialogue. The discussion featured the following panellists:

- **Harsha Bhowmik**, Director (Digital Economy and Fintech) Department of Economic Affairs, Ministry of Finance
- **Shilpa Mankar Ahluwalia**, Partner and Head Fintech, Shardul Amarchand Mangaldas
- **Vinay Kesari**, Director, Operations and Strategy, Setu AA
- **Neha Aggarwal Jain**, Partner, Regulatory Services, Deloitte

The second panel titled *"Building Trust of the Consumers: Addressing the Issues of Financial Fraud"* was moderated by Ms. Monica Jasuja, Chief Growth and Partnership Officer, Twid. It features the following panellists:

- **Ranjeet Rane,** Head of Research, Reserve Bank Innovation Hub
- **Suresh Vytla,** Director South Asia, LexisNexis Risk Solutions
- **Shalini Shingari,** Senior Director, Pine Labs

The following themes emerged from the discussion of this panel:

2 Driving the next phase of Financial Inclusion - Importance of DPI and FinTech Companies

The central theme of the conference was financial inclusion, which remains a critical challenge and opportunity within the fintech sector. The discussions highlighted the progress made in expanding access to financial services but also underscored the ongoing gaps that need to be addressed. It was highlighted how efforts towards realising financial inclusion were initiated at the beginning of the century, but this process was completely transformed when digital innovations permeated the financial sector and the JAM trinity was initialised. India's DPI stack (India Stack) enabled high levels of financial inclusion with the percentage of people included within the financial sector reaching 87%. It is believed that without fintech DPIs, this level couldn't have been reached even in 40 years.

The panellists examined various strategies to improve financial inclusion, including leveraging digital technologies to reach underserved populations. Innovations in mobile banking, digital wallets, and microfinance were discussed as effective tools for broadening access to financial services. The role of government policies and regulatory frameworks in supporting these innovations was also emphasised. India has made significant progress in operationalizing fast digital payments for both P2M (Person to Merchant) and P2P (Person to Person) transactions. However, the same strides have not been seen in the area of credit lending, which is crucial for the growth of Micro, Small, and Medium Enterprises (MSMEs), particularly in their early stages. MSMEs are vital to the economy, contributing significantly to the manufacturing sector and employment. Therefore, their growth is essential for the country's overall economic development.

2.1 Need for an Incubative Regulatory Regime

The first panel extensively delved into the regulatory aspects of fintech. The panel discussed that regulating fintech is a complex challenge, as innovation and product development often outpace regulatory frameworks. Striking the right balance between fostering innovation and preventing consumer harm is crucial. One critical area where regulation can play a significant role is in customer acquisition. While fintech companies have excelled in acquiring customers, regulations can enhance this process by ensuring transparency and data governance. One of the panellists suggested that data licensing and data access frameworks should be developed for the fintech entities to access data that can fuel their innovation. Towards this, the regulators can also build guardrails and data protection practices. It's essential that consumers retain control over their data, understanding what is collected, where it is stored, why it is needed, and who has access to it. Another panellist suggested the creation of centralised KYC system to sm

The panellist also pointed out that regulations can help standardise data collection and credit underwriting processes, ensuring that credit access for small and medium-sized businesses (SMBs) is more accurate and inclusive.

The role of self-regulatory organisations (SROs) in fintech is another important aspect that was discussed by the panellists. Wide-sectoral participation in SROs is crucial, as it brings together diverse voices and perspectives within the sector. This makes SROs a powerhouse of information and a valuable resource for industry stakeholders. Furthermore, SROs can act as an extended regulatory wing, potentially developing a verification system that allows customers to verify whether a fintech company is part of the SRO-FT framework. This would enhance consumer trust and ensure better adherence to industry standards.

Lastly, the panellists highlighted that while the JAM trinity (Jan Dhan, Aadhaar, and Mobile) has significantly contributed to financial inclusion in India, however, to build on this foundation, regulations must also focus on financial literacy. Mandating financial literacy programs, particularly those aimed at bringing women into the financial fold, could be a vital regulatory measure.

There was a consensus on the need for a multi-faceted approach to financial inclusion, which includes not only technological solutions but also efforts to improve financial literacy and education. The importance of designing inclusive financial products that cater to the needs of diverse populations was highlighted. Additionally, the panellists discussed the potential of digital public infrastructure to facilitate financial inclusion by providing a more accessible and efficient platform for delivering financial services. In both these instances, the role of private players is important considering their agility and appetite for innovation.

2.2 Access to Credit

The discussion highlighted the role of private players and the whole digital public infrastructure can play in improving credit access. One of the panellists highlighted that credit and access to credit is one area where we still have a lot of ground to cover as a country.credit as a percentage of GDP is somewhere about 50% which is way below the global average which is about 150%. Credit card penetration in India is about 3.4% compared to the global average of 34%. Anyone who has ever run a small business or a large business knows, credit is what fuels growth. Therefore, there is a need to refurbish the credit ecosystem.

Towards this, scaling digital credit is one of the key important areas. NPCI has added credit lines on UPI which is a great initiative. Further, AAs have the potential to provide financial institutions with the data needed to make informed lending decisions. While banks often have the necessary capital, they frequently lack sufficient data to accurately underwrite loans for deserving individuals or businesses. The high cost of underwriting loans in India is another barrier, particularly for MSMEs, which typically require smaller loans that are not currently feasible for banks to underwrite. In this context, it was suggested that banks should start relying on alternative data sources to make better-informed credit decisions. Regulation can help in standardisation of various data collection and credit unwriting processes. The development of a risk mechanism algorithm was also proposed. This algorithm could help assess whether a loan is being used for its intended purpose, further reducing the risk for lenders.

It was also noted that traditional credit systems alone cannot achieve last-mile delivery without the involvement of private players and AAs. Therefore, Account Aggregators could play a transformative role in advancing credit lending to underserved populations, thereby supporting the growth and sustainability of MSMEs in India.

2.3 Enhancing Export of DPI

The consideration of exporting India's fintech solutions, particularly in the context of the Unified Payments Interface (UPI), highlights the importance of an ecosystem approach. Leveraging the various players within this ecosystem can facilitate the export of these innovative solutions to other countries. The globalisation of UPI, driven by initiatives from NIPL, NPCI, and the Reserve Bank of India (RBI), aims to extend UPI's capabilities beyond Indian borders. UPI, as a homegrown product, is a powerful tool in global politics, especially in a landscape where payment systems may become monopolised. Constant collaboration is sought to help countries in need of this technology.

The globalisation of UPI involves exporting three major considerations:

- **Merchant Integration and Acceptance at PoS Channels:** One of the key models focuses on connecting merchants and enabling UPI acceptance at point-of-sale (PoS) channels globally.
- **Supporting Countries with Proprietary Payment Solutions:** Some neighbouring countries face challenges in building their proprietary payment solutions. India's approach is not to offer UPI as a Software as a Service (SaaS) but to integrate it in a manner that allows these countries to implement the solution without compromising their data control and other critical details.
- **Reducing Remittance Costs:** Another major issue is the high cost of remittances. Bringing these costs down to around 3% would be significant, not only for reducing processing fees within India but also for creating a global environment with low remittance rates through an interoperable global network.

Public-Private Partnerships (PPPs) play a crucial role in exporting Digital Public Infrastructures (DPIs). There is a strategic angle to this, as India has demonstrated thought leadership and transformed it into action. It is essential to capitalise on the competitive advantage that India currently holds.

When it comes to exporting these solutions, the space is still evolving. Institutions are approaching this with a mindset that prioritises the public good. The goal is to adopt successful models in the home country and assist the export country in implementing them. Open-source solutions serve a common good, offering certain benefits to all, and enabling the creation of innovative services on top of existing ones. This approach ensures that these innovations remain accessible to the rest of the world, fostering global progress and development.

3 Addressing the Challenges of Digital Financial Fraud

The threat of fraud is ever-evolving, and fraud mitigation strategies must evolve constantly. Higher fraud cases lead to loss of business, investment, and customer loyalty and increased service unreliability. This could lead to a loss of trust in the industry for customers, significantly impacting fintech startups.

3.1 Robust Grievance Redressal

During the discussion, it was observed that while some firms have implemented redressal systems, these are often not available around the clock, hindering timely resolution for consumers. With digital payment frauds in India increasing fivefold in 2024 alone, the urgency for more robust and accessible complaint channels was emphasised. The rapid growth in digital payments, coupled with financial illiteracy and the unwise use of technology, were identified as major contributors to the rising instances of fraud. The sudden proliferation of cyber companies offering security services in India further underscores the escalating threat.

Financial fraud has far-reaching consequences for the entire sector. Unchecked fraud reveals underlying instability, which can deter potential investors and damage the industry's reputation. Trust is paramount in digital financial systems—platforms that maintain customer trust are more likely to survive and thrive. However, frequent instances of fraud erode this trust, making it difficult to rebuild consumer confidence.

3.2 Central Fraud Registry

A significant topic of discussion was the operationalisation of a Central Fraud Registry. This registry would record all instances of fraud across the country, enabling the identification of patterns and the development of targeted solutions through policy interventions or algorithms. However, the challenge lies in the tragedy of the commons—no one is willing to contribute to such a registry, despite its potential benefits. Establishing a centralised data registry that facilitates the sharing of data and intellectual property across entities could enhance collaboration and improve fraud prevention efforts. This approach, framed as a public good, aims to provide a comprehensive techno-legal solution capable of supporting instant responses to fraud.

3.3 Need for Techno-Legal Solutions

The discussion also highlighted that a purely techno-legal solution cannot fully address the issue of fraud. Since fraud occurs at multiple levels and stages, a concerted effort involving all relevant stakeholders is essential for effective prevention and redressal. Regulation, combined with process and product innovations, was seen as the way forward. The complacency of merchants towards fraud prevention was also noted as a significant obstacle, with many merchants reluctant to invest in necessary security measures.
The role of AI and machine learning (ML) in fraud detection was another key area of discussion. The potential for these technologies to identify patterns and outsmart fraudsters was highlighted, with suggestions to "scam the scammers" by learning from their methods. Analysing customer behavioural patterns was also proposed as a means of creating safeguards to prevent unintended outcomes. However, challenges remain in implementing these technologies, especially for small businesses that may lack the resources for advanced fraud detection systems.

3.4 Strengthening the Regulatory Frameworks

In addition to technological solutions, the importance of foundational legal frameworks, such as those provided by the Digital Personal Data Protection Act (DPDPA), was emphasised. These frameworks are crucial in helping companies implement effective controls and prevent fraud. Proper Know Your Customer (KYC) processes and the accountability of banks were also discussed, with a call for systems that can flag potential issues early to prevent escalation.

The discussion acknowledged that post-facto redressal mechanisms are often inadequate, particularly in the context of real-time settlements. This inadequacy contributes to the loss of trust in digital financial systems, further highlighting the need for proactive fraud prevention measures. The discussion concluded with a recognition of the long-lasting effects of financial fraud on the entire sector, reinforcing the need for a comprehensive, multi-faceted approach to tackling this growing issue.

The conversation concluded by discussing the role of financial literacy and awareness in preventing fraud. Panellists suggested that policies should transition from rule-based to pattern-based approaches, incorporating guidelines such as those from the RBI to improve the effectiveness of financial products. A human-centric approach in product design was advocated to address consumer protection more effectively. It was emphasised that financial literacy needs to be coupled with enforcement actions. The effectiveness of current policies and regulations was questioned, with a focus on ensuring that compliance measures result in actionable steps rather than mere formalities.

4 WAY FORWARD

Following are the key action points that emerged from the conference:

- The data in the Central KYC Registry could be leveraged to build various services and products, since the data present is verifiable, reliable and safe.

- To aid credit access, there is a need to utilise alternative data sources. Several alternate credit finance platforms now offer in-depth analysis of an SME's business leveraging various data points such as expenses, overheads, and revenues of an SME to create a comprehensive database.

- Account Aggregators can play a role in providing robust techno-legal support required for exchanging data across various financial institutions. By operationalizing reliable consent-based mechanisms, AAs can help in building trust among consumers.

- Regulations can assist with delineating standards of data collection and credit underwriting processes and norms. In this regard, SRO-FTs could assist in formalising as well as enforcing certain good practices.

- A data licence could be established specifically for licensed fintech entities. A publicly accessible database of these licensed fintech entities would be created, and only those listed would be permitted to handle user data.

- The capabilities of AI, ML and blockchain must be harnessed in creating a centralised database of financial data. Behavioural data of consumers must be analysed to identify patterns of transactions. Anomalous transactions could be then detected and prevented at the first instance. Good actors can then be qualified, creating a system to weed out bad actors automatically.

- Post-redressal mechanisms must evolve with the growing pace of digital payment innovations. A disharmony between technology and regulation could lead to erosion of trust among consumers.

- Fraud prevention systems could be deployed as a DPI, facilitating public-private partnership and innovation potentially leading to robust techno-legal solutions.

- There must be soft mandates enabling standardised IP and data sharing practices for fintechs. Consumer protection must be instilled as a business differentiator to make it a pertinent aspect.

- Products and services must be inclusive and human-centric. Access barriers created through dark patterns and lack of vernacular languages must be eliminated.

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