



## Safeguarding the Fintech Sector

This editorial is based on [“Trust as the guardrail for fintech”](#) which was published in the Hindu Business Line on 21/02/2023. It discusses the need for policymakers to expand the fintech sector regulator's capacity for effective monitoring and enforcement.

**For Prelims:** Fintech Sector, Financial Inclusion, Cybersecurity, Computer Emergency Response Team, Angel Investor

**For Mains:** Capital Market, IT & Computers, Cyber Security, Scientific Innovations & Discoveries

The Fintech segment in India has **seen an exponential rise in funding** over the last few years; the **sector received funding worth USD 9.8 Bn in 2021**, led by the Payments segment (**53% share of fintech funding across all fintech verticals in India**).

Prior to the arrival of the [digital stack](#), **financial services were largely a 'status-quo' space for Indian consumers**. It has been **dominated by the sheer strength of physical brand presence** and has borne the burden of being a product seller rather than a solution provider.

With enhanced digital capabilities, **the smarter incumbents started combining data sciences** and capabilities to address consumer convenience to offer better solutions.

As far as consumer engagement and solutions are concerned, **fintech companies are challenging traditional players** in the areas of lending, insurance, asset management, and wealth management.

The onus is on the **segment-regulators to build their supervisory moats to maintain fiscal resilience** in the era of convergence of emerging technology and finance. This would **need the regulators to build their own tech capabilities**, including real-time market surveillance and entity-supervision competence.

### What is the State of the Fintech Sector in India?

#### ▪ About:

- The fintech sector in India has grown dramatically during the pandemic, with the number crossing 7,500 fintech startups. During 2014 to mid-2022, the sector received more than USD 30 billion in funding.
- It is estimated that **Indian fintechs represent about USD 100 billion of Enterprise Value (EV)**, compared to an overall EV of Financial Services (FS) of USD 1.4 trillion, in 2021.
- The Indian fintech sector is poised to **capture nearly USD 350 billion in EV by FY 2026-27**, contributing more than 15% of FS EV. Similar is the story of **insuretechs** and **wealthtechs**.

- **Wealthtech entirely focuses on generating wealth** for investors through the use of technology.
- **Insurtech is often used to describe the use of technology** in the insurance industry.
- **Growth Drivers:**
  - The **main forces driving the acceleration of this sector have been product innovations in customer acquisition**, underwriting, pricing and collections, and customer services.
  - The **rapid growth of fintechs can also be attributed to**
    - Favourable macroeconomic and demographic factors, including rising middle class with higher disposable incomes to buy, borrow, save and invest more.
    - Increasing mobile access and digital adoption
    - Abundant financial services and technology talent in the country
    - Availability of equity and debt capital
    - Government initiatives and regulatory efforts to create a conducive environment.

## What are the Current Challenges with the Fintech Sector?

- **Regulatory Challenges:**
  - One of the significant challenges faced by the fintech sector in India is the **lack of a well-defined regulatory framework**.
  - The sector is regulated by multiple authorities, which can lead to confusion and ambiguity.
- **Access to Funding:**
  - Despite the growth in the fintech industry, **many startups in India struggle to secure funding**.
  - This is due to a **lack of understanding of the sector among traditional investors** and a limited number of venture capital firms that focus on fintech startups.
- **Cybersecurity:**
  - With the increase in digital transactions, **there is a growing concern around cybersecurity threats**.
    - India's [Computer Emergency Response Team \(CERT-IN\)](#) reported that in the first half of 2022, **over 674,000 cyber security incidents occurred in the country**.
- **Low Awareness:**
  - Many people in India are **still unaware of the benefits of fintech services**.
  - Fintech companies **need to work on increasing awareness about their offerings** and the value they bring to customers.
- **Competition from Traditional Banks:**
  - Traditional banks are **also expanding their digital offerings, creating intense competition for fintech companies**.
  - Fintech startups need to continue to innovate and offer unique solutions to differentiate themselves from traditional banks.
- **Inadequate Infrastructure:**
  - Despite the growth in the sector, **India still lacks the necessary infrastructure to support fintech services**.
  - Issues such as slow internet speeds, lack of interoperability, and inadequate digital infrastructure can pose challenges to the growth of the fintech sector.

## What should be the Way Forward?

- **Developing an Efficient Regulatory Regime:**
  - The government can **work with the industry to develop a more streamlined and efficient regulatory regime** that promotes innovation and growth while also protecting consumers.
- **Access to Funding:**
  - The government can **encourage the development of more venture capital firms and [angel investor](#) networks focused on fintech**, as well as create policies to attract more foreign investment.
- **Building Digital Infrastructure:**

- Fintech companies **require reliable digital infrastructure to provide their services effectively**. The government can invest in building a robust digital infrastructure, including improved broadband connectivity and cloud computing services.
- **Promoting Financial Inclusion:**
  - The government can **work with fintech companies to develop innovative solutions** to help underserved and unbanked populations gain access to financial services.
- **Creating Robust Cybersecurity Policies:**
  - As fintech **companies rely on digital technology to deliver their services**, they are particularly vulnerable to cyber-attacks.
  - The government can create robust cybersecurity policies and regulations to protect consumers and encourage confidence in the fintech sector.
- **Addressing Digital Illiteracy:**
  - Addressing digital illiteracy can be incredibly helpful in addressing challenges with the fintech sector.
  - Ways to increase Digital literacy:
    - Increased adoption of fintech services, Reduced fraud and security risks, Increased innovation etc.

### **Drishti Mains Question**

What measures can India take to effectively safeguard the Fintech sector and its consumers from potential risks and threats, while promoting innovation and growth in the industry?

## **UPSC Civil Services Examination, Previous Year Questions (PYQs)**

### **Mains**

**Q. With reference to India, consider the following: (2010)**

1. Nationalisation of Banks
2. Formation of Regional Rural Banks
3. Adoption of village by Bank Branches

**Which of the above can be considered as steps taken to achieve the “financial inclusion” in India?**

- (a)** 1 and 2 only
- (b)** 2 and 3 only
- (c)** 3 only
- (d)** 1, 2 and 3

**Ans: (d)**

- Financial inclusion is the process of ensuring access to appropriate financial products and services needed by individual and businesses including vulnerable groups such as weaker sections and low income groups at an affordable cost in a fair and transparent manner by mainstream institutional players.
- Nationalization of banks helped in branch expansion and thereby reaching a greater number of people. Besides, credit to agriculture, small scale industries and allied sectors has also increased. **Hence, 1 is correct.**
- Regional Rural Banks (RRBs) were set up as government-sponsored, region based rural lending institutions under the Regional Rural Banks Act, 1976. RRBs were configured as hybrid micro banking institutions, combining the local orientation and small scale lending culture of the cooperatives and the business culture of commercial banks. **Hence, 2 is correct.**
- A village adoption scheme was introduced by the banks in 1960s in India with a view to enhancing their reach besides encouraging agri-lending in a costeffective manner. **Hence, 3 is correct.**

**Therefore, option (d) is the correct answer.**

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