Suresh Srinivasan

An entrepreneur, consultant and a professor of strategy at Great Lakes Institute of Management, Chennai. He is also a chartered accountant and comes with decades of industry experience globally.

Is demonetisation a firm foot towards digitalisation?

Vegetable traders use the Quick Response Code (QR code) provided by Indian Bank to receive payments from customers through the banks’ mobile app, in Coimbatore. (Photo: M. Periasamy)

Jan 19, 2017 16:10
Infrastructure will need to be scaled up if digitisation has to succeed

Globally, financial technology — or fin-tech — communities and start-ups are striving hard to disintermediate the traditional banking, and financial services players offering more convenient and simplified solutions at much lower costs. Payments, loans, trading solutions, crowd funding, peer-to-peer lending and the likes are gaining significant importance under the fin-tech umbrella.

Technologies such as Blockchain and crypto-currencies, such as Bitcoin, are no longer 'exotic'; it is just a matter of time before they become ubiquitous. The evolution of fin-tech in the Indian context and the 'shot in the arm' which it has received as a result of demonetisation is truly exciting.

Can the objective of India's note ban and its impact, both short and long term, be viewed merely from the lens of eradicating black money and corruption? At a broad level, maybe yes. However, there are arguments as to whether corruption, cash hoarding and tax evasion can be eliminated at all in an economy like India, where demand far exceeds supply across sectors, be it education, healthcare or employment. However, one solution that can move our economy in the less corrupt direction, is to increase cashless transactions.

Although it is very unlikely that demonetisation will make India less corrupt 'overnight', it will positively impact the growth of fin-tech communities, which have the potential to move the country — albeit slowly and steadily — towards a digital economy that supports cashless transactions.

Inclusion

Financial inclusion, till this point, was always expected to be achieved through increased banking penetration. However, it is now clear that this can also be achieved through digitalisation and by deploying 'emerging financial technologies' that hasten the process of moving a large part of the 'unbanked' society into the banking purview. All thanks to deepening mobility penetration.

In emerging economies like India, fin-tech can facilitate financial inclusion, leapfrogging the growth in the traditional 'physical' banking network, much like what the mobile phones did for the landline telephony.

As a technology, fin-tech is being viewed as a disrupter that could disintermediate the banks — very similar to Uber, which disintermediated cab service. An interesting contrast though is that while cab operators resisted the emergence of Uber and Ola, banks today are working closely with fin-tech start-ups (for example Yes Bank with T-Hub) to become a part of the technology revolution and carve a place for themselves in the evolving financial services value chain.

The importance of fin-tech activities has grown exponentially in the last few months, more so since note ban. Not only are the highly visible areas, such as digital banking, credit and debit card usage and payment wallets growing, but a number of start-up communities that support the eco-system of digitalisation and financial technologies — both from the perspective of banking and financial services and that of the telecom complementarities — are fast emerging out of the shadows on the technology side.

Fin-tech growth

Payments and lending are the primary areas where fin-tech start-ups are active. More than half the start-ups account for these. Asset management and trading account for the rest. Investors have been bullish of fin-tech start-up ventures — close to ₹10,000 crore worth of investment has flown into these start-ups over the last two years, with 2016 alone seeing about ₹7,000 crores infusion.

In addition to Paytm, Freecharge and Mobikwik, other key start-ups which are primarily in the payments business — such as Citrus Pay, Mswipe and Electronics Payments and Services — are rapidly growing. Digital lending and insurance platforms accounted for a large part as well. The likes of BankBazaar, PolicyBazaar, Vistaar Finance, Capital Float and Lendingkart have received a significant share of the financing.

'Payment' is a major area where fin-tech is emerging post note ban. Companies such as Paytm and Mobikwik have posted steep increase in traffic in recent days. Using debit cards and experimenting with wallets, despite those methods of payments being more or less the only choice, have helped change the mindset. This, together with the banks' Unified Payment Interface (UPI) apps and the Bharat Interface for Money (BHIM) app is slowly clearing misconception about e-payments. Electronic payments at departmental and street corner stores are slowly becoming ubiquitous — something the common man has been pushed into.

Customer value, investment and funding

Demonetisation has been an excellent trigger for the fin-tech sector, whereby the customers have been made to realise the value of cashless transactions. Overnight, demonetisation created 'pain points' for the customer and opened up avenues for fin-tech companies to address. This increased the excitement levels at the funding agencies that look at the Indian fin-tech sector. The note ban has thus increased 'digital' adaption and fired up the 'network' effect.

Although this move came at a huge risk to the government, it is for sure a true innovation that spearheads digitalisation and cashless economy.

Technological preparedness

Given the note ban's push towards going cashless and digital transactions, information technology and backend infrastructure need to be exponentially scaled up and connectivity needs to be fail safe.

Even with very a pessimistic forecast of the proportion of population that is likely to go cashless, the resultant 'peak time' usage could be in the range of 60,000 transactions per second (tps) to 120,000 tps.

The current infrastructure and telecom connectivity are nowhere close to the forecasted requirements.

To handle such large volumes, back-end infrastructure needs to be upgraded and maintained by the banks, National Payment Corporation of India Ltd., or private mobile app providers. Telecom infrastructure is also a critical component and players such as Vodafone, Airtel, MTNL and BSNL need to seamlessly connect to the back-end infrastructure as well as to users.

Internet connectivity using data packs and WiFi should be reliable and speeds need to be consistent — many a time, 4G and 3G speeds drop down to 2G. More importantly, the proportion of smartphones needs to increase, replacing feature phones. Currently, only 20 per cent of the total mobile phone handsets are smartphones.

On balance

The mindset of the average Indian citizen, which to date had been deeply rooted in 'hard' savings in the form of cash and gold, is now moving towards financial assets. This is something that various governments have been striving to achieve for decades and weren't successful.

Talking about mindset, with more money flowing into the formal banking system, at least the message is quite clear — that tax evasion will not be a serious option anymore; non tax payers are already being brought under the radar, and going forward, tax evasion will only reduce. In the medium to long term, tax collection is expected to increase — essentially, a solution to reduce levels of corruption.

Other nations have undergone demonetisation and note bans in the past, including Soviet Union, Ghana, Myanmar, Nigeria and North Korea. Many of them were unsuccessful and attracted public wrath. Nearly 60 days later, India, however, is still holding on quite well; although, to a certain extent, pain points do continue to exist.

GDP growth in the current fiscal will suffer for sure; even the RBI has lowered its forecast significantly. But the overall direction the Indian economy is taking seems exciting, although loose ends needs to be tied up.

Incidentally, India too had tried demonetisation in the past; however, the recent note ban comes in the midst of technologies and skills sets — especially in the area of fin-tech which has reasonably gained critical mass in terms of funding, size and scale. If appropriately orchestrated, the economy can fire up digitalisation from all four cylinders!

That said, could the note ban have come at a better time? Or for that matter, can there be a better opportunity for the fin-tech community?