Charting new horizons for fintech lending

Navigating profitability and scalability

Foreword

Manish Jain,
Country Managing Director,
Experian India

" The advent of fintech on the lending landscape has been a key story of the last decade. Fintech with innovative business models have emerged as a serious player in the lending ecosystem especially in the small ticket segment.

Fintech have come of age having experienced full lending cycle now. The portfolio built as well as enabled by fintech have seasoned with lot of learnings from this experience. Existing literature on fintech clearly recognizes the impact fintech have created. Fintech have helped expand the credit market thereby driving the Financial Inclusion agenda. Customers have benefited by way of quicker and more accessible credit. The current focus of fintech lending is largely focused on small ticket segment.

There are some signs of stress in the portfolio and hence active monitoring is required. Further, private lenders through their investment in technology over the years have leaned closer to a 'fintech model' thereby reducing differentiation benefit to the fintech.

Given this backdrop it can be concluded that fintech lending is at the cross-roads. Identifying new 'blue oceans' of growth is an imperative. It is being recognized that prudent lending practice is important for sustainable growth. Focus needs to be on curtailing credit losses and maintaining asset quality. The timing of DLAI (Digital Lenders Association of India) conference 2024 is very opportune. This conference will bring together players in the entire ecosystem to help arrive at the fintech lending agenda for next wave of sustainable growth.

This White Paper "Charting new horizons for fintech Lending: Navigating profitability and scalability" is aimed at providing participants with an objective view on the current state as also recommend pathways for a sustainable and scalable growth. We have following takeaways based on quantitative assessment of the fintech lending book with industry benchmarking:

- Fintech created a niche by identifying and nurturing "blue oceans" as against focusing on available white spaces in the addressable market. In the process, fintech helped drive the financial inclusion agenda.

- Fintech currently have a narrow market focus on small ticket Personal Loan and Business Loan products. There is a need to expand horizontally to new product segments and vertically to downstream business use cases such as account management and recovery.

- Asset quality for fintech requires active monitoring. It is worth noting managing the risk through pricing as a tool has its limitations. Hence, it is important to identify new revenue streams and partnerships which will help build sustainable business.

- Today, Fintech lending is a fine example of how incumbents and new entrants can come together to create value propositions. Given India's low credit penetration levels compared to other developed economies coupled with India's growth story there is ample room for everyone to grow. Partnership with incumbents is both in the interest of end consumer as well as individual participants.

In summary, it is a time to both cherish the impact fintech have created in the lending ecosystem as also pivot to means to improve asset quality. This is not the time to reboot but rather to build on the core competencies of fintech to achieve greater societal goals.

Foreword

Mr. Jatinder Handoo,
CEO, DLAI

" In the dynamic landscape of India's fintech sector, the digital lending industry stands as a beacon of innovation and progress, facilitating access to credit for millions of individuals and businesses across the nation. It is with great pride and enthusiasm that I introduce this seminal report, "Charting New Horizons for Fintech Lending: Navigating Profitability and Scalability.

I am privileged to witness firsthand the transformative impact of fintech lending on our economy. From empowering underserved segments of society to fostering entrepreneurship and economic growth, our industry plays a pivotal role in driving financial inclusion and resilience. This report serves as a sectoral resource for industry stakeholders, offering data backed insights into sectoral development along with the opportunities and challenges that define our journey ahead. Through meticulous analysis and strategic recommendations, it provides a roadmap for navigating the complexities of profitability and scalability in an ever-evolving landscape. In an era defined by technological disruption and regulatory scrutiny, the importance of responsible lending practices cannot be overstated. As guardians of trust and integrity, digital lenders must uphold the highest standards of ethics and transparency, placing the welfare of customers at the forefront of our endeavors. At the Digital Lenders Association of India, we are committed to build an ecosystem that fosters responsible market conduct, supports innovation, collaboration, and sustainable growth. Through advocacy, thought leadership, and industry best practices, we strive to create an environment where digital lenders can thrive while fulfilling their responsibility.

I extend my heartfelt appreciation to the authors, researchers, and contributors whose expertise and dedication have enriched this report. Their invaluable insights illuminate the path forward, empowering us to harness the full potential of fintech lending for the betterment of society.

As we embark upon this journey of exploration and discovery, let us remain steadfast in our commitment to excellence and inclusivity. Together, we have the opportunity to redefine the future of finance, shaping a world where access to credit knows no boundaries.
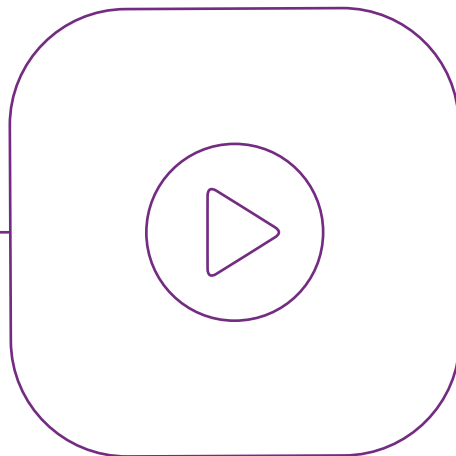
The making of a fintech nation:
Digital lending leads the way

Fintech portfolio assessment:
Profitability & scalability

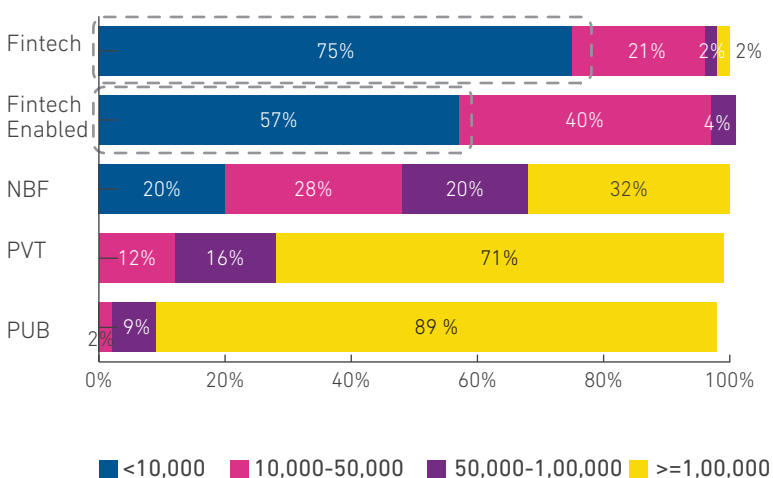## The new fintech:
Lending playbook

THE MAKING OF A FINTECH NATION:
DIGITAL LENDING LEADS THE WAY

- THE FINTECH LENDING MARKET
- DEFINING CHARACTERISTICS
- FINTECH LENDING PLAYBOOK
- IMPACT ON FINANCIAL INCLUSION

Fintech moved from being a fringe player to a dominant lender category in small ticket segment
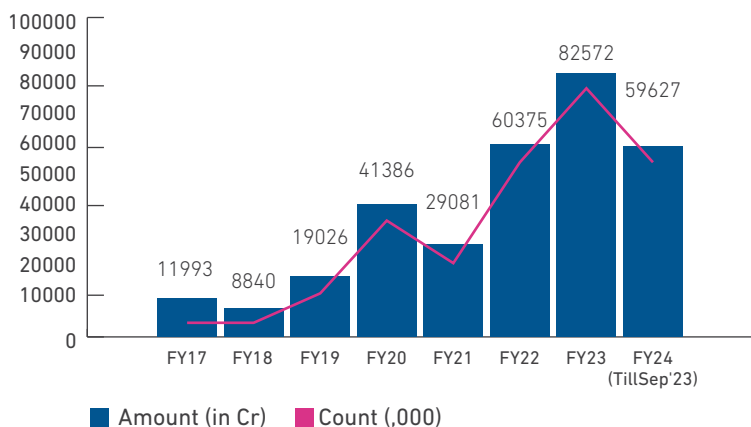
Fig .1.1– Ticket Size distribution across lender categories (Count)

Category	<10,000	10,000-50,000	50,000-1,00,000	>=1,00,000
Fintech	75%	21%	2%	2%
Fintech Enabled	57%	40%	4%	
NBF	20%	28%	20%	32%
PVT		12%	16%	71%
PUB	2%	9%		89 %

Legend: ■ <10,000 ■ 10,000-50,000 ■ 50,000-1,00,000 ■ >=1,00,000

- The current market exhibits a distinct acquisition strategy with different lenders playing in select segments.

- Segmenting the market on ticket size allows us to see dominant player in each cohort. In lower ticket bands fintech and fintech enabled have a dominant position (<1lakh).

Majority of the sourcing under 10K bucket for Fintechs.

Fig.1.2-Sourcing distribution across years (< 1 Lakh Sourcing)

Amount values: FY17: 11993, FY18: 8840, FY19: 19026, FY20: 41386, FY21: 29081, FY22: 60375, FY23: 82572, FY24 (TillSep'23): 59627

Legend: ■ Amount (in Cr) ■ Count (,000)

- The focus on the lower ticket bands by both the lender categories can be attributed to the fact they have core competencies which enable high traction in this segment.

- <1 lakh ticket size has seen an upwards trend since FY17, with a dip only during the pandemic. This ticket size corresponds to ~85% by number of loans disbursed in FY23

Fintech: NBFC with strong focus on technology led acquisition. These lenders have all the acquisitions in their own book.
Fintech Enabled: Loans originating from one lender but aided by Partnership with another Fintech are tagged as Fintech Enabled Loan.
These loans are of small ticket size (< 1 lakh for PL and < 1 lakh for BL). Typically, these would be loans originated by LSP (Lending Service Provider) but on the books of the regulated entity (NBFC or Bank).

Fintech moved from being a fringe player to a dominant lender category in small ticket segment

Fig.1.3-Market share across Lenders by count (< 1 Lakh)
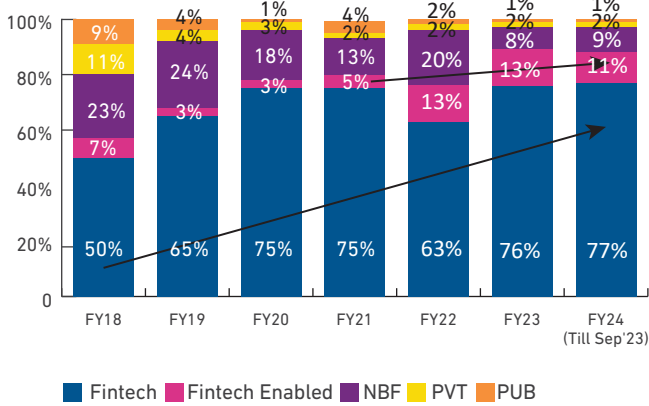
- Market share shown is for ticket size <1 lakh ticket size. Fintech lenders dominate the segment in loan volumes.

- In fact, fintech have consistently grown their market share.

- Currently they make up the 77% of the market.

Fig.1.4-Market share across Lenders by Amount (< 1 Lakh)
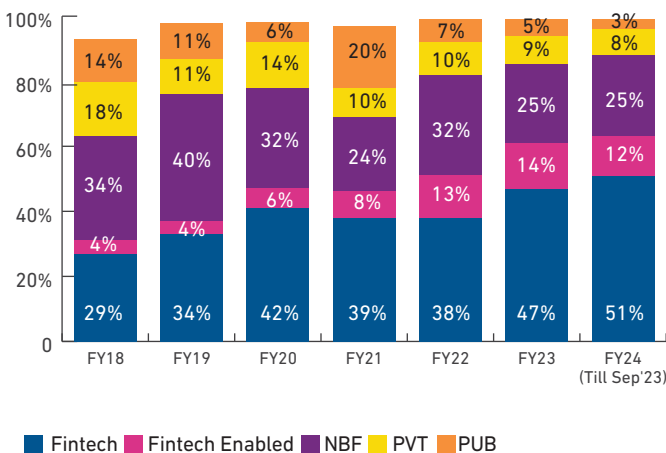
- Fintech have greater penetration in bite size consumption loan within the < 1 lakh lending universe. In high ticket segment traditional lenders have been able to retain market share.

- Fintechs currently own 51% of the market in <1 lakh ticket size compared with 77% by new disbursements.

Fintech growth in core market was double than that of nearest competition and parallel can be drawn with how NBFCs grew niche product segments when they entered the lending scene

Fig1.5-CAGR across lender categories (FY18 vs FY23)
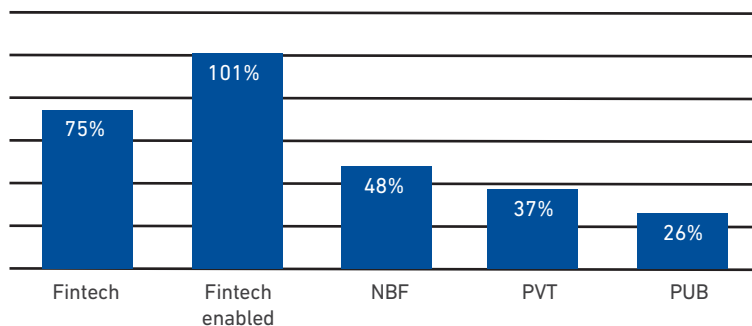
- There has been a growth for all lenders in < 1 lakh Personal Loan credit market. However, Fintech and Fintech enabled have grown at a significantly rapid pace.

- Early entrants in the digital market space or lenders who adopted digital origination reaped benefit.

- Considering growth by amount, Fintech and Fintech Enabled almost doubled their original market of 2018.

Owing to high growth in origination fintech have built large portfolio in small ticket consumption loans (PL < 1 lakh)

Fig.1.6-AUM for PLt<1Lakh Industry as on Sep'23

Legend: Fintech | Fintech Enabled | NBF | PUB | PVT
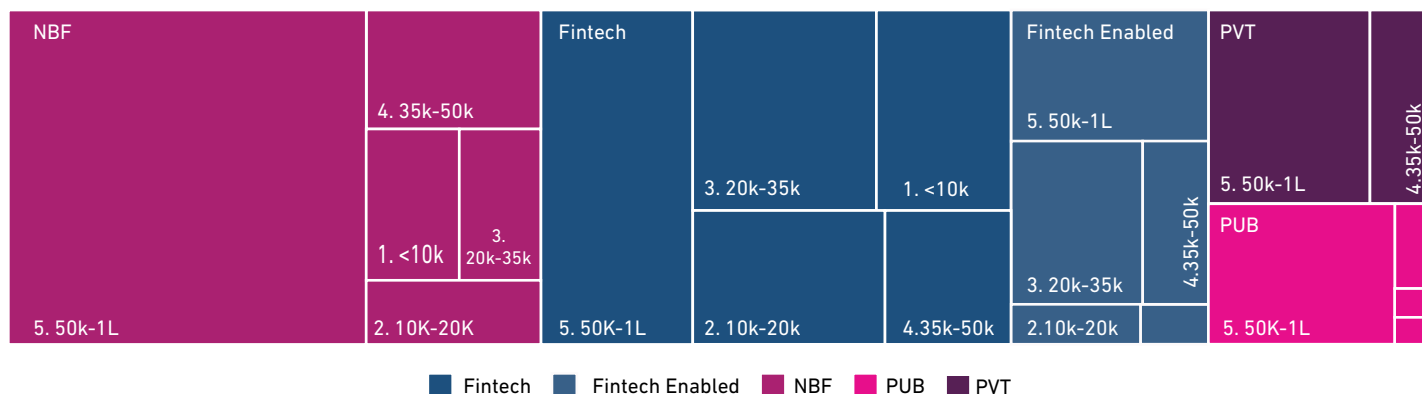
- Personal Loan Portfolio size at end of Sep' 23 stands at ~ Rs 81,000 Cr. NBFCs have the highest market share of 34% followed by Fintech with 33% of the market.

Overall Market Size PL <1L as of Sep'23	
AUM	Accounts
₹81,767 Cr	₹48,692 K

Average Ticket Size
(FY24 till Sep'23)
₹11,576

Fintech have also been active in small ticket business lending segment registering robust growth

Fig 1.7-Sourcing distribution across years for BL < 1 Lakh
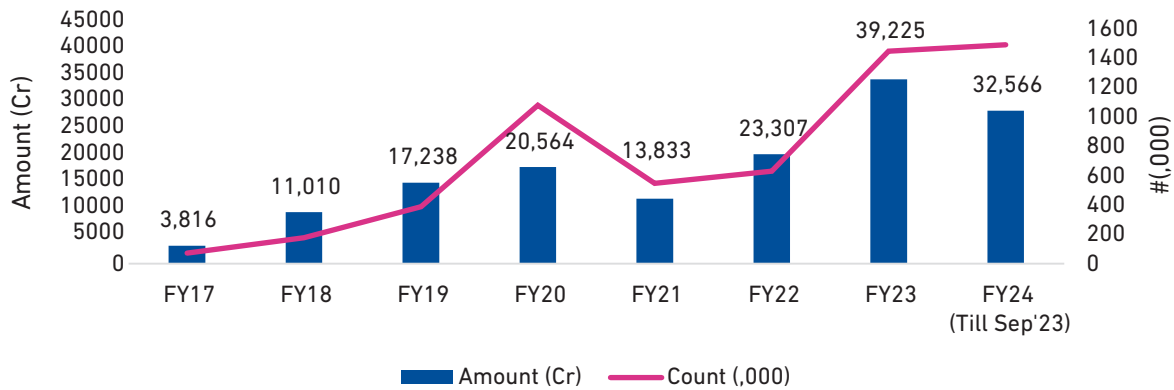
Fig 1.8-Market share across lenders by amount (<1 Lakh)
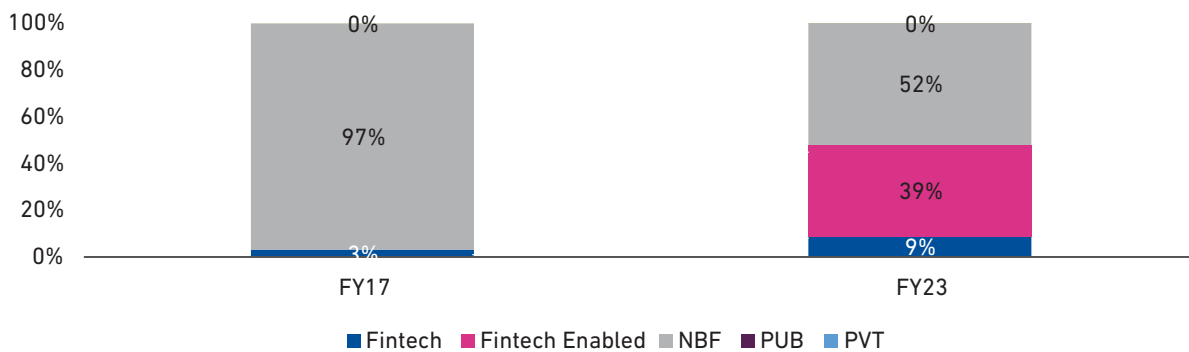
- Small ticket Business Loan (<1 Lakh) grew steeply in recent year, with current financial year sourcing already close to ~85% of full last financial year sourcing.

- Fintech now constitute ~10% of new disbursement by value. They have also been a key facilitator to incumbents.

- Fintech presence, though, is largely focused on working capital needs and asset maintenance finance. Traditional lenders continue to dominate the requirement on fixed capital formation.

Growth in "Bharat" has been the key highlight of the fintech story for Personal Loans

Fig.1.9-FY23 vs FY22 Growth comparisonacross City Tier by Lenders

	Fintech NBFC	Fintech Enabled	NBF	PVT	PUB	OTH
Tier 4	106%	52%	40%	14%	23%	24%
Tier 3	88%	58%	39%	33%	27%	25%
Tier 2	-56% / 79%	53%		28%	19%	24%
Tier 1	-6% / -32% / 53%	40%		10%		10%
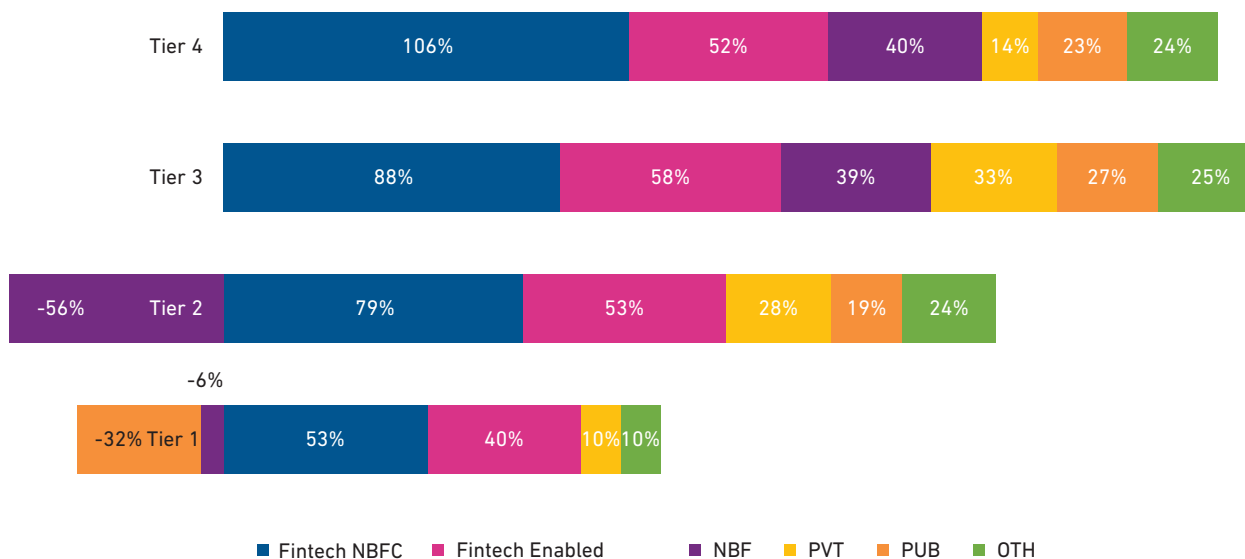
- Fintech have pivoted to small towns which offer higher avenues to increase lending book.

- New geographies provide new 'blue oceans' for fintech as traditional business hotspots are dominated by traditional players.

Growth in "Bharat" has been the key highlight of the fintech story for Personal Loans

Fig 1.10-FY 23 vs FY 22 for Fintech growth spread
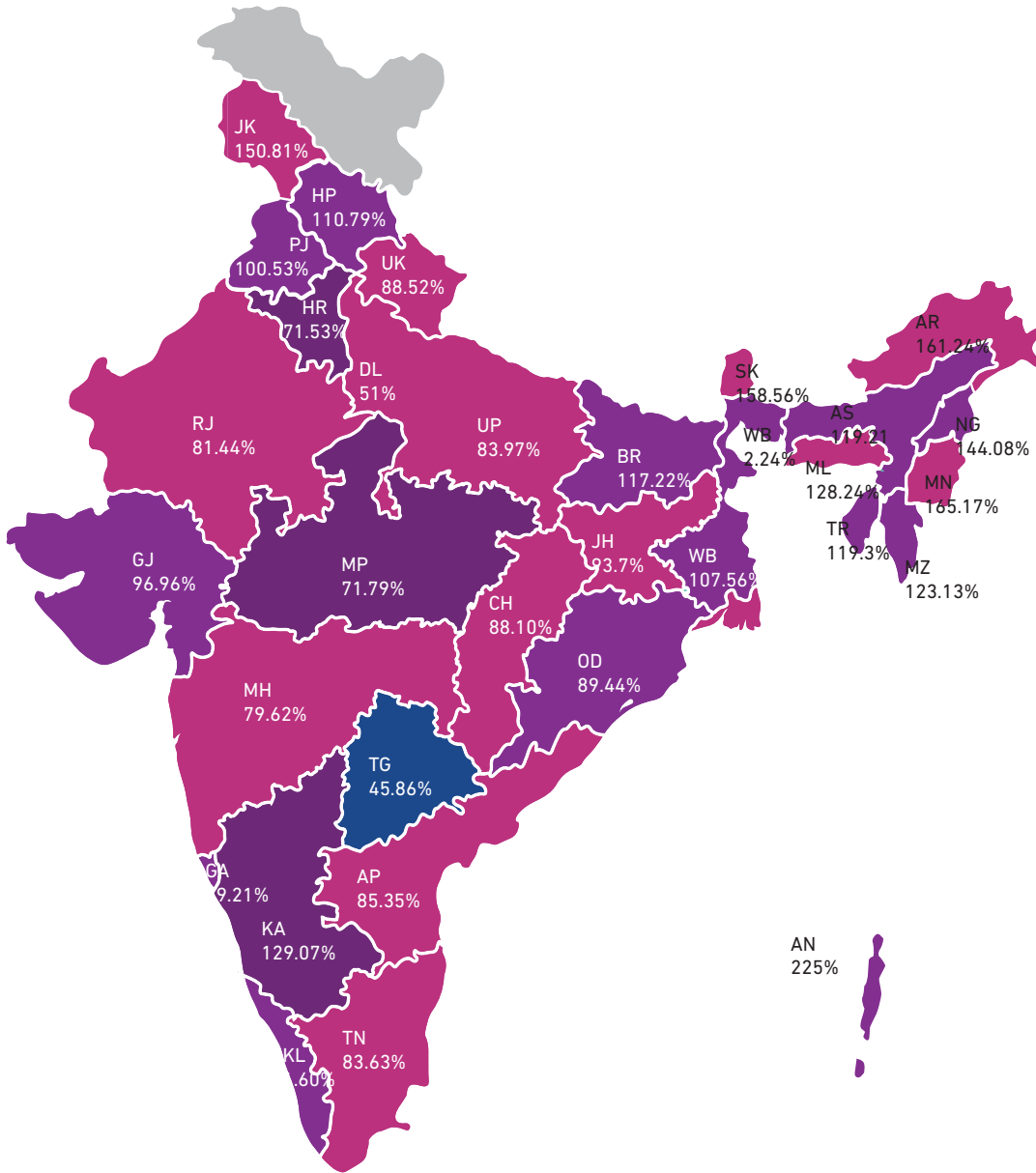
Credit profile of fintech customers are markedly different with other lenders in terms of their product choices and geographical skews

	Where did the Customer start their credit journey	Credit basket of the Customer	Distribution skew across city tiers
Fintech NBFC	58% of loan originations with Fintech NBFCs as the First Lender	68% of customers with first product as CD/PL and 88% again taking a PL/CD, followed by 4% taking CC as next product	50% of loan originations with from Tier 4 followed by 22% from Tier 1
Fintech Enabled	29% of loan originations with Fintech PVT as the First Lender	54% of customers with first product as CD/PL and 18% taking CC as next product	51% of loan originations with from Tier 4 followed by 22% from Tier 1
PVT	14% of loan originations with Fintech PVT as the First Lender	45% of customers with first product as CC and by 30% taking CC as next product	39% of loan originations with from Tier 4 followed by 26% from Tier 1
PUB	11% of loan originations with Fintech NBFCs as the First Lender	59% of customers with first product as CD/PL and 48% taking CD/PL as next product	64% of loan originations with from Tier 4 followed by 7% from Tier 1

Experian Study Based on representative industry sample corresponding to FY23 Personal Loan sourcing, with selection of dominant cluster across each lender category. The clustering algorithm used is hierarchical agglomerative clustering with Gower index

Fintech have focused on younger population who are yet to build their credit profile. Fintech borrowers eventually mature to a good bureau score profile implying a prudent selection at acquisition.

Customers sourced in FY23, their scores correspond to NTC, Sub-prime and Prime Respectively. The objective is to understand the shift in risk profile using bureau Score migration study

Key takeaway: Fintech is increasingly targeting a younger demographic in the NTC profile who are converting towards higher credit bureau scores subsequently

	Age Mix	Fintech NBFC	Fintech Enabled	NBF	PUB	PVT
"Fintechs focusing more on Younger Population in NTC, who eventually do move on to Prime Segment"	<=25	40%	47%	8%	11%	35%
	25 – 35	39%	38%	33%	33%	48%
	35 – 40	8%	6%	17%	14%	4%
	> 40	13%	9%	43%	42%	13%

	Age Mix	Fintech NBFC	Fintech Enabled	NBF	PUB	PVT
"Irrespective of focus on any age bucket, this segment is sticky to sub-prime profile across lenders"	<=25	6%	6%	1%	6%	1%
	25 – 35	41%	42%	23%	33%	44%
	35 – 40	17%	17%	26%	10%	19%
	> 40	36%	35%	51%	51%	36%

	Age Mix	Fintech NBFC	Fintech Enabled	NBF	PUB	PVT
"Highest movement of Fintech from near prime to Sub-Prime, whereas the same for PUB & PVT is to Prime segment"	<=25	7%	8%	2%	1%	2%
	25 – 35	44%	46%	32%	23%	39%
	35 – 40	16%	18%	22%	14%	24%
	> 40	33%	28%	45%	61%	35%

Sub Prime - <650 | Near Prime – 651 – 725 | Prime – 726 – 800 | Super Prime - >801

As on Score as on Sep'23

As on Sep'23	Fintech NBFC	Fintech Enabled	NBF	PUB	PVT	
Sub-Prime	28%	8%	8%	1%	3%	NTC
Near-Prime	12%	5%	7%	7%	4%	
Prime	60%	87%	85%	92%	93%	

As on Sep'23	Fintech NBFC	Fintech Enabled	NBF	PUB	PVT	
Sub-Prime	77%	77%	75%	52%	69%	Sub-Prime
Near-Prime	17%	13%	20%	33%	14%	
Prime	6%	10%	5%	15%	17%	

As on Sep'23	Fintech NBFC	Fintech Enabled	NBF	PUB	PVT	
Sub-Prime	38%	23%	25%	10%	11%	Near-Prime
Near-Prime	38%	42%	46%	45%	43%	
Prime	23%	35%	29%	45%	46%	

Multitude of collaborative operating model innovations led by Fintech co-exist today

	1. Co-Lending	2. Direct Lending
	A co-financing structure where both the organizations are risk bearers in agreed proportion	A financing structure where both the loan origination and risk is borne by the same entity
Risk Bearer	Partial Risk	Complete Risk
Loan Origination	Routed Sourcing	Self -Sourced
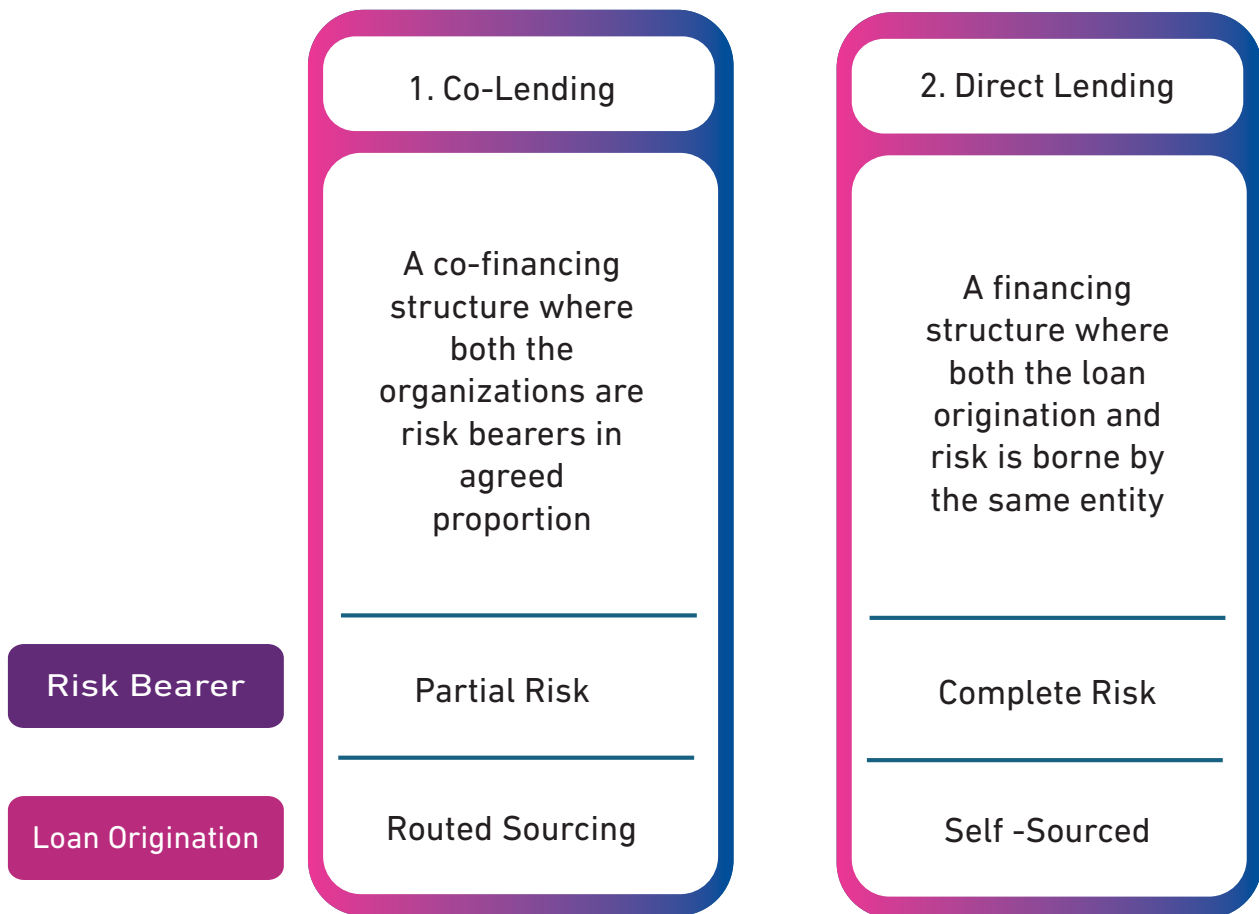
3. Fintech Facilitated

This structure is such where lenders rely on fintechs for loan origination but retaining the risk on their books
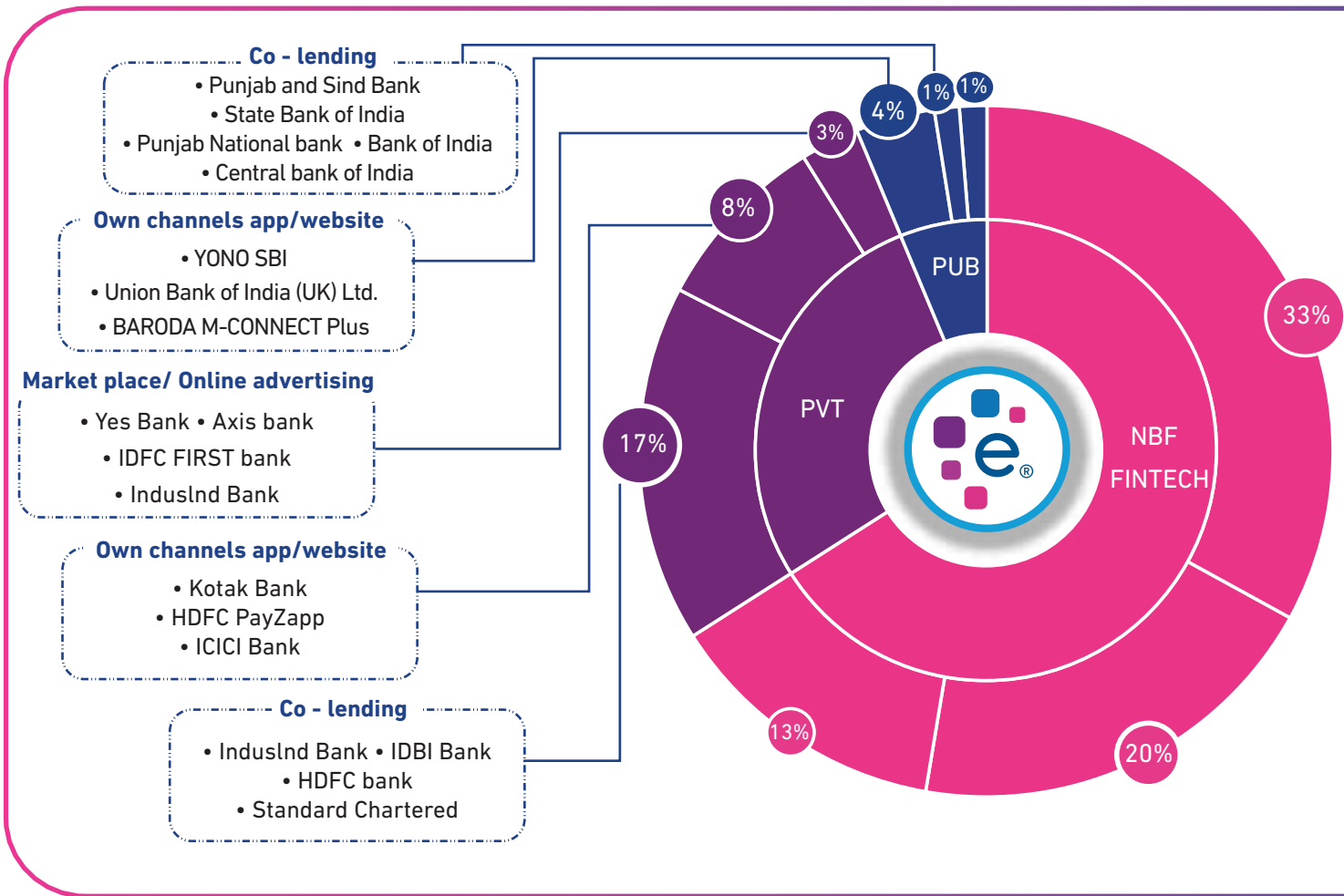

Partial Risk

Routed Sourcing

4. 'Pseudo' Fintech

When lending institutions create separate assets and/or channels like super apps for loan origination with self risk bearing

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Complete Risk

Self -Sourced

Digital lending ecosystem now constitutes diverse lenders and mix of origination models

Co - lending
• Punjab and Sind Bank
• State Bank of India
• Punjab National bank • Bank of India
• Central bank of India

Own channels app/website
• YONO SBI
• Union Bank of India (UK) Ltd.
• BARODA M-CONNECT Plus

Market place/ Online advertising
• Yes Bank • Axis bank
• IDFC FIRST bank
• Induslnd Bank

Own channels app/website
• Kotak Bank
• HDFC PayZapp
• ICICI Bank

Co – lending
• Induslnd Bank • IDBI Bank
• HDFC bank
• Standard Chartered

1% 1%
4%
3%
8%
PUB
17%
PVT
33%
NBF
FINTECH
13%
20%

Market place/ Online advertising

- Indian Bank • Bank of Baroda
- UCO Bank • Indian Overseas Bank
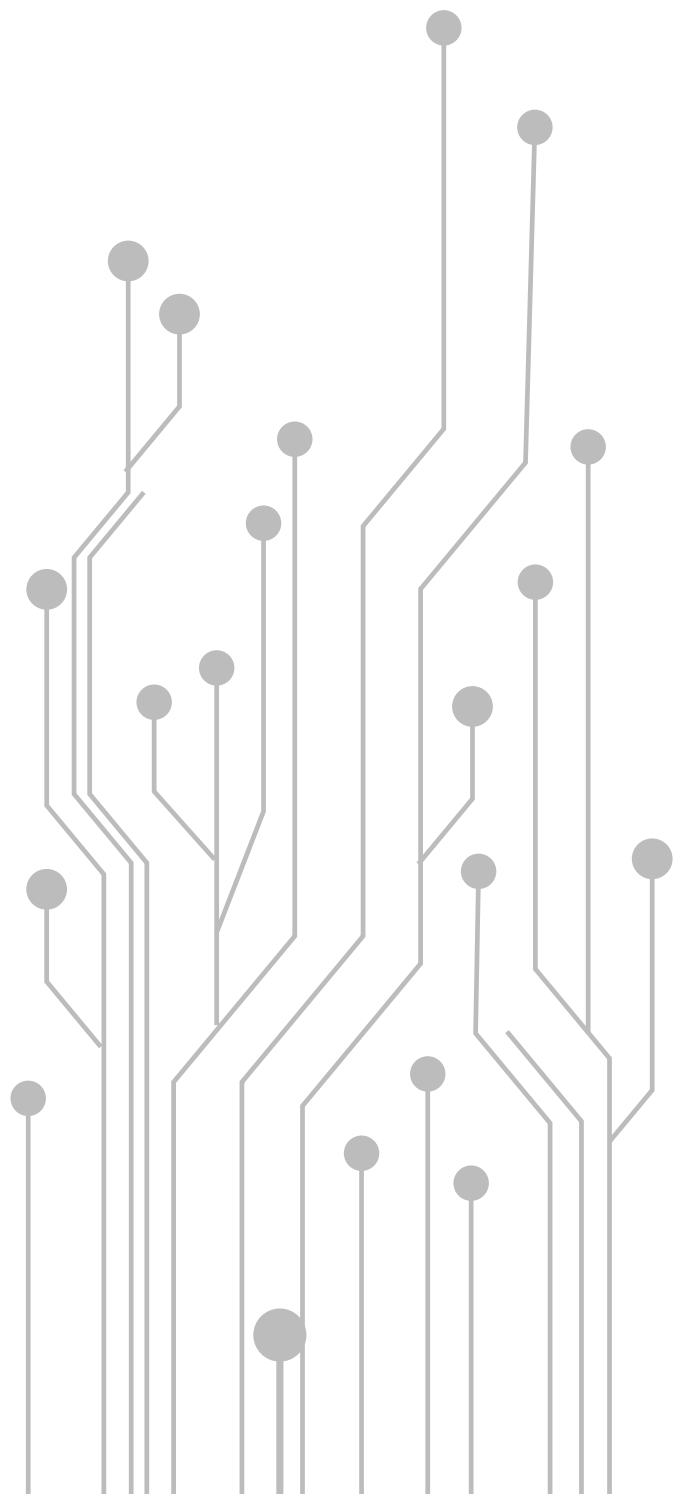
Own channels app/website
- Axio • Neogrowth • Zest
- Money Veiw • Pine Labs
- Paytm

Co - lending

- IIFL finance • Indel Mone
- U GRO Capital • Of business

Market place/ Online advertising
- Bankbazaar.com • Kredx
- Indialends • Indifi
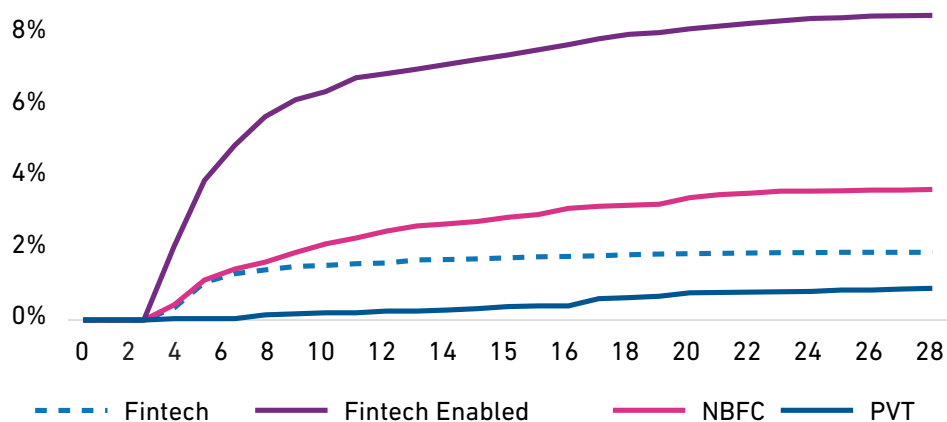- Lendingkart • Paisabazaar.com

FINTECH PORTFOLIO ASSESSMENT:
PROFITABILITY &SCALABILITY

- ASSET PERFORMANCE
- CUSTOMER MANAGEMENT

FY23 sourcing is seen at higher level of risk and hence requires active monitoring

Sourcing - FY'22

Fig 2.1-Personal Loan (90+ Ever) Vintage

Legend: - - - Fintech —— Fintech Enabled —— NBFC —— PVT

- While Fintech registered exponential growth there is some stress observed especially in more recent sourcing.

- There is a need to go for controlled aggression in new sourcing to ensure a sustainable book.

- Major reasons for deterioration in asset quality is the performance on under 35,000 ticket size sub-segment

Sourcing - FY'23

Fig 2.2-Personal Loan (90+ Ever) Vintage

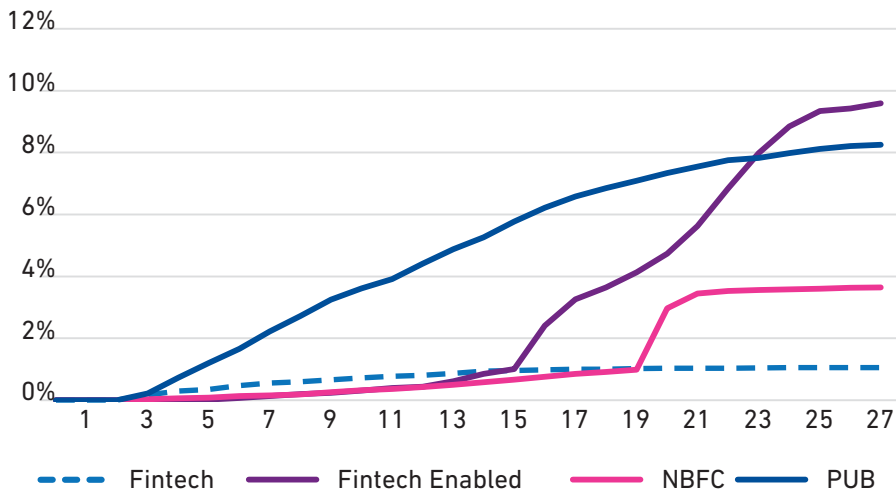Legend: - - - Fintech —— Fintech Enabled —— NBF —— PVT
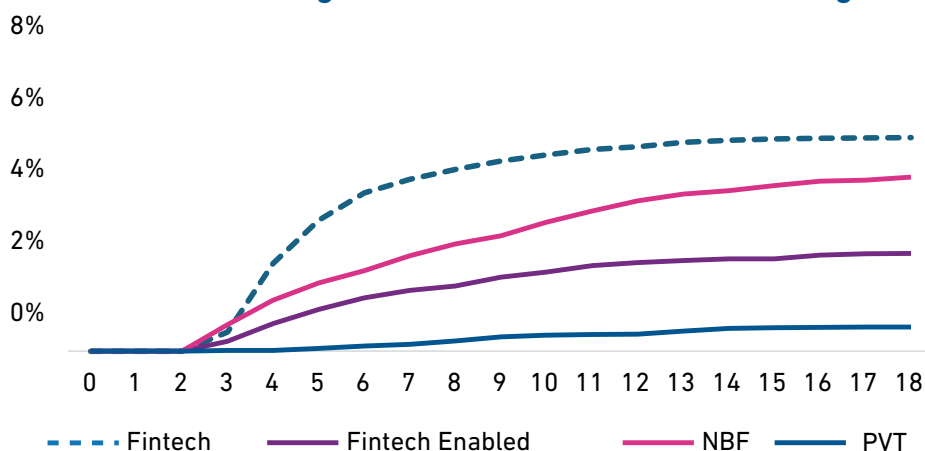
Fintech: NBFC with strong focus on technology led acquisition
Fintech Enabled: Loans originating from one lender but aided by Partnership with another Fintech are tagged as Fintech Enabled Loan.
These loans are of small ticket size (< 1 lacs for PL and < 1 lacs for BL)

The trend on Business Loan performance for fintech is similar as Personal Loan with worsening of sourcing quality in FY23 compared with FY22

Sourcing - FY'22

Fig 2.3-Business Loan 90+ Ever Vintage

Legend: Fintech · Fintech Enabled · NBFC · PUB

Sourcing - FY'23

Fig 2.4-Business Loan 90+ Ever Vintage

Legend: Fintech · Fintech Enabled · NBFC · PUB

- Fintech forayed into Business Loan segment and achieved deep market penetration.

- However, new sourcing is not in sync with other lending segments in terms of early asset performance.

- Major reasons for deterioration in asset quality is the performance on under 50,000 ticket size sub-segment
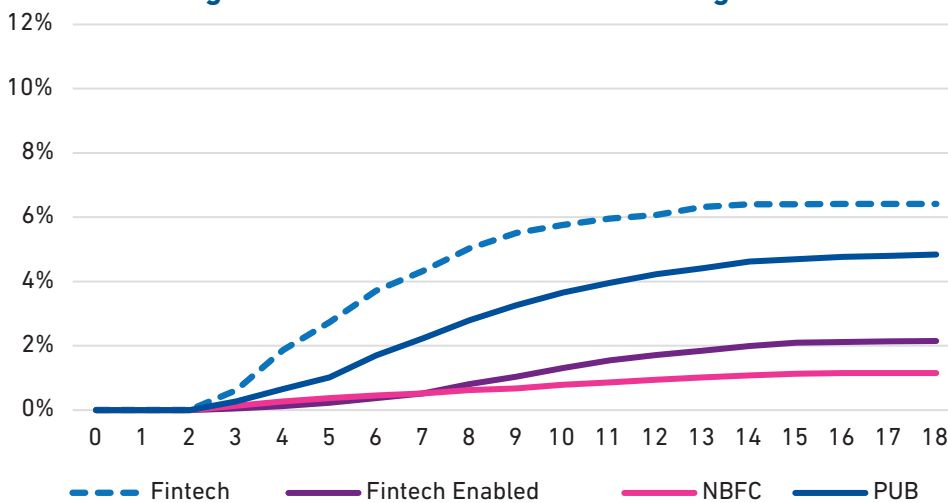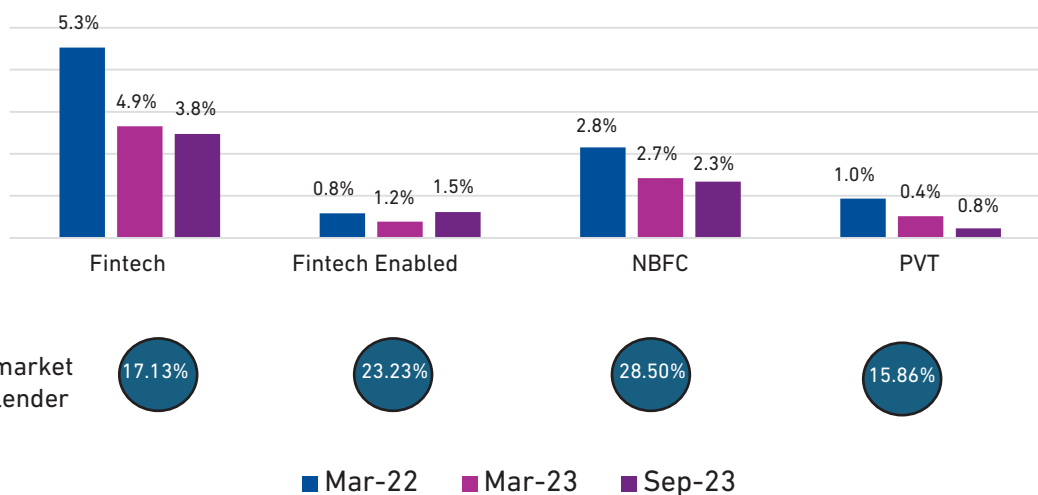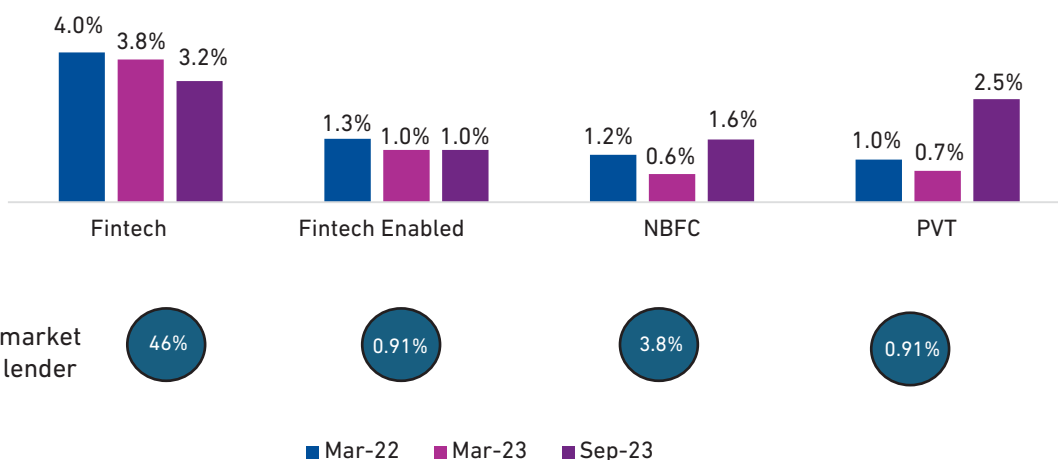
Fintech asset quality has improved significantly but there is still lot of catching up to do with peers

Fig.2.5-Net 90+% delinquency by lender category - PL

Fintech: 5.3% (Mar-22), 4.9% (Mar-23), 3.8% (Sep-23)
Fintech Enabled: 0.8% (Mar-22), 1.2% (Mar-23), 1.5% (Sep-23)
NBFC: 2.8% (Mar-22), 2.7% (Mar-23), 2.3% (Sep-23)
PVT: 1.0% (Mar-22), 0.4% (Mar-23), 0.8% (Sep-23)

Sep 23 – market share by lender
Fintech: 17.13%
Fintech Enabled: 23.23%
NBFC: 28.50%
PVT: 15.86%

■ Mar-22   ■ Mar-23   ■ Sep-23

- Coincidental delinquency on PL for fintech has consistently improved over the years.

- However, it still lags peer s in terms of net 90+ delinquency.

- Higher net delinquency for fintech was mainly on account of sub-par performance in sub-50 K ticket size
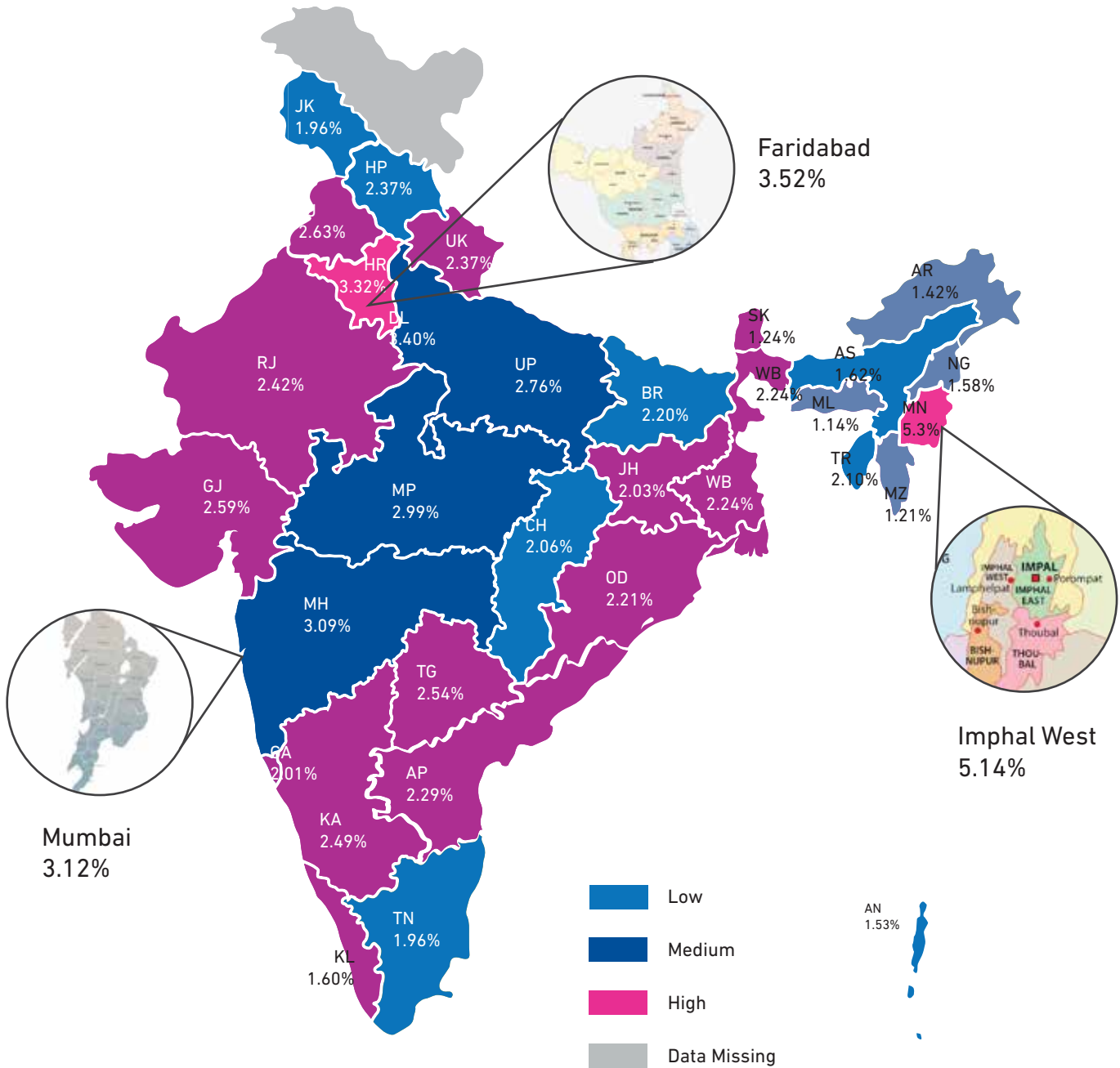
Fig 2.6-Net 90+% delinquency by lender category - BL

Fintech: 4.0% (Mar-22), 3.8% (Mar-23), 3.2% (Sep-23)
Fintech Enabled: 1.3% (Mar-22), 1.0% (Mar-23), 1.0% (Sep-23)
NBFC: 1.2% (Mar-22), 0.6% (Mar-23), 1.6% (Sep-23)
PVT: 1.0% (Mar-22), 0.7% (Mar-23), 2.5% (Sep-23)

Sep 23 – market share by lender
Fintech: 46%
Fintech Enabled: 0.91%
NBFC: 3.8%
PVT: 0.91%

■ Mar-22   ■ Mar-23   ■ Sep-23

- Business loan, as a product segment, has superior asset quality compared to Personal Loan.

- Business Loan, as a product category, will also help expand credit access to self-employed segment.
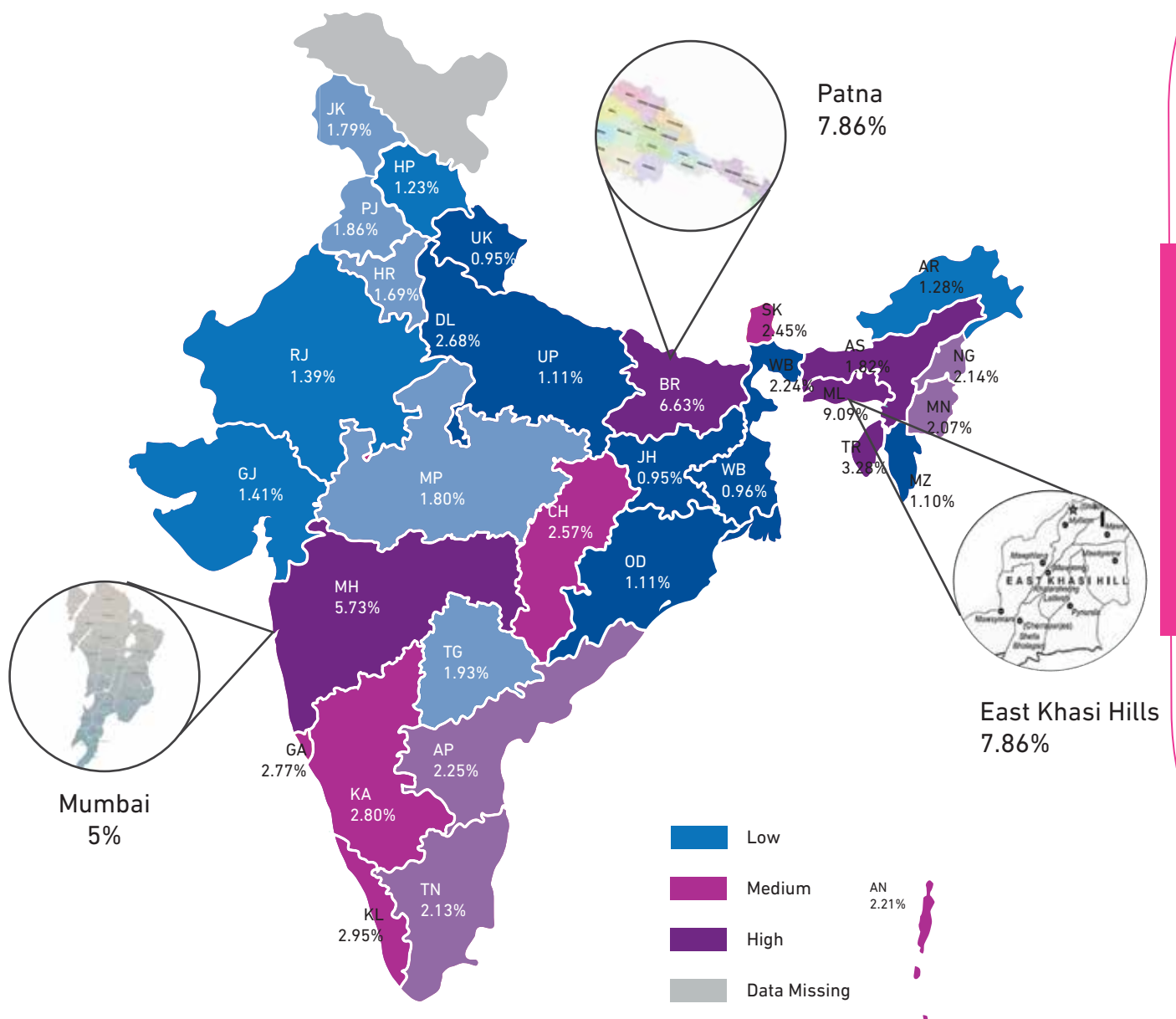
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Asset quality varies across different geographies-important for fintech players to factor in localized risk and grow accordingly

Fig 2.7-90+ delinquency – Personal Loan

JK
1.96%

HP
2.37%

2.63%

UK
2.37%

HR
3.32%

DL
3.40%

RJ
2.42%

UP
2.76%

BR
2.20%

Faridabad
3.52%

AR
1.42%

SK
1.24%

AS
1.62%

NG
1.58%

WB
2.24%

ML
1.14%

MN
5.3%

GJ
2.59%

MP
2.99%

JH
2.03%

WB
2.24%

TR
2.10%

MZ
1.21%

CH
2.06%

OD
2.21%

MH
3.09%

TG
2.54%

Imphal West
5.14%

Mumbai
3.12%

GA
2.01%

AP
2.29%

KA
2.49%

TN
1.96%

KL
1.60%

AN
1.53%

Legend:
- Low
- Medium
- High
- Data Missing

Portfolio till September -2023
Delinquency by Amount

Asset quality varies across different geographies-important for fintech players to factor in localized risk and grow accordingly
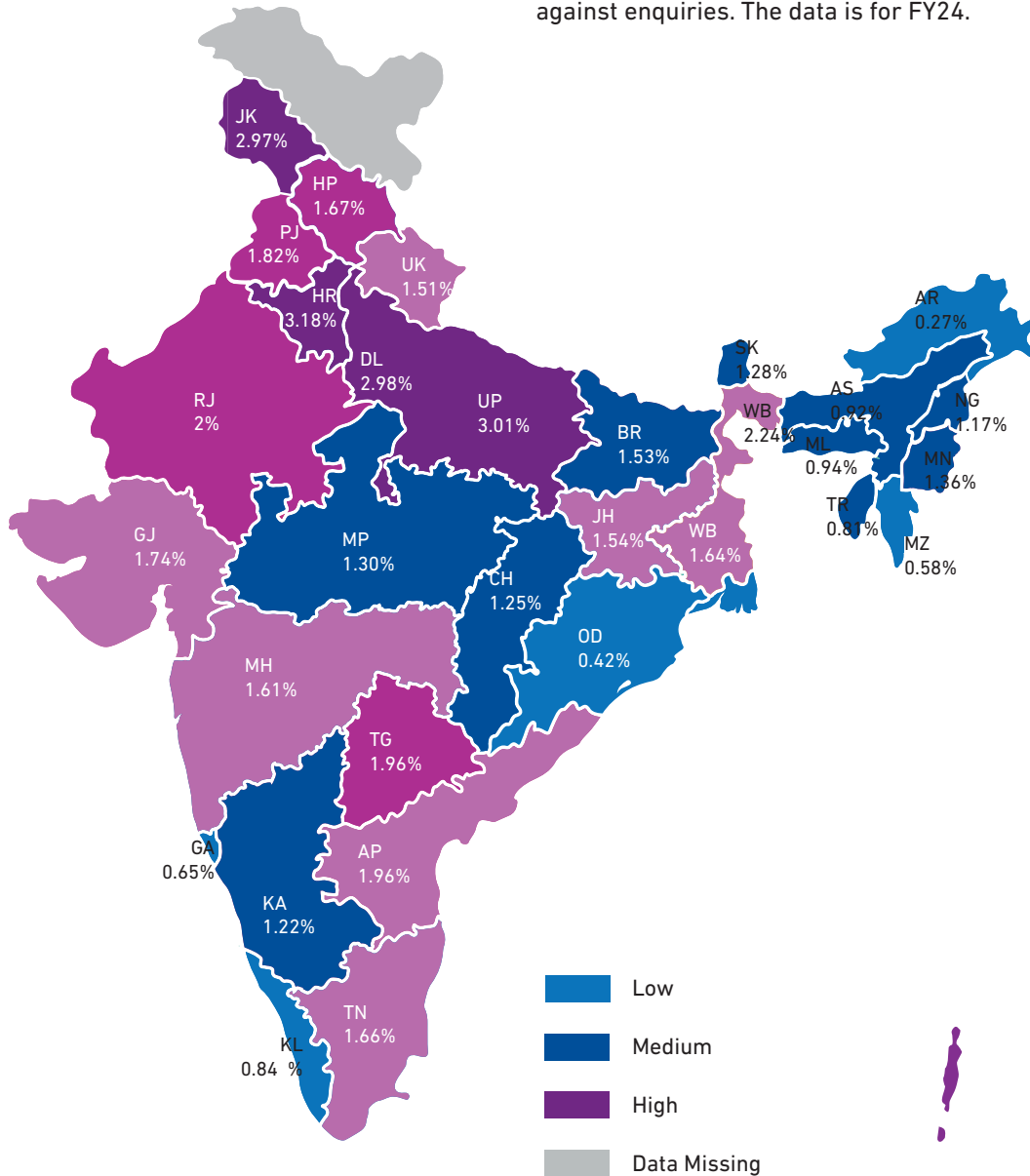
Fig 2.8-90+ Delinquency – Business Loan

Patna
7.86%

East Khasi Hills
7.86%

Mumbai
5%

JK 1.79%	
HP 1.23%	
PJ 1.86%	
UK 0.95%	
HR 1.69%	
DL 2.68%	
RJ 1.39%	
UP 1.11%	
BR 6.63%	
SK 2.45%	
AR 1.28%	
WB 2.24%	
AS 1.82%	
NG 2.14%	
ML 9.09%	
MN 2.07%	
GJ 1.41%	
MP 1.80%	
JH 0.95%	
WB 0.96%	
TR 3.25%	
MZ 1.10%	
CH 2.57%	
OD 1.11%	
MH 5.73%	
TG 1.93%	
GA 2.77%	
AP 2.25%	
KA 2.80%	
TN 2.13%	
KL 2.95%	
AN 2.21%	

Legend:
- Low
- Medium
- High
- Data Missing

Core product segment of fintech also prone to fraud at application stage and the tools to combat this is fundamentally different with that of managing credit risk
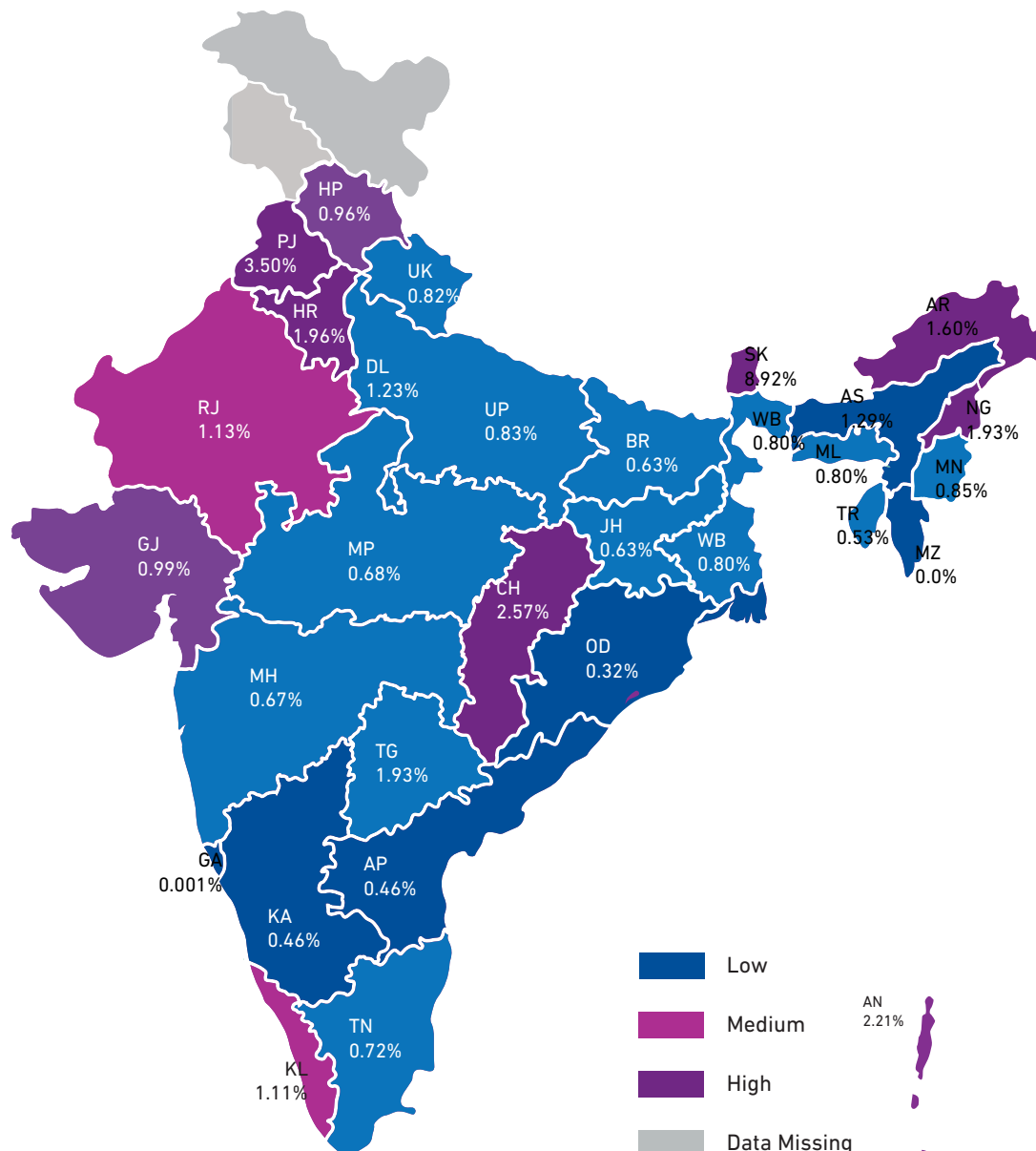
Fig 2.9-Fraud rate – Personal Loan

Fraud rate is computed using data from 'Experian Hunter Data Asset". Hunter database comprises of application fraud tagged by Hunter Closed User Group lenders against enquiries. The data is for FY24.

Map of India showing fraud rates by state:

- JK 2.97%
- HP 1.67%
- PJ 1.82%
- HR 3.18%
- UK 1.51%
- DL 2.98%
- RJ 2%
- UP 3.01%
- AR 0.27%
- SK 1.28%
- AS 0.82%
- NG 1.17%
- WB 2.24%
- ML 0.94%
- MN 1.36%
- TR 0.87%
- MZ 0.58%
- BR 1.53%
- GJ 1.74%
- MP 1.30%
- JH 1.54%
- WB 1.64%
- CH 1.25%
- OD 0.42%
- MH 1.61%
- TG 1.96%
- GA 0.65%
- AP 1.96%
- KA 1.22%
- TN 1.66%
- KL 0.84 %

Legend:
- Low
- Medium
- High
- Data Missing

There are locations with high propensity for application-level fraud and additional mitigation measures need to be factored in over and above credit risk mitigation.

Core product segment of fintech also prone to fraud at application stage and the tools to combat this is fundamentally different with that of managing credit risk

Fig 2.10-Fraud rate – Business Loan
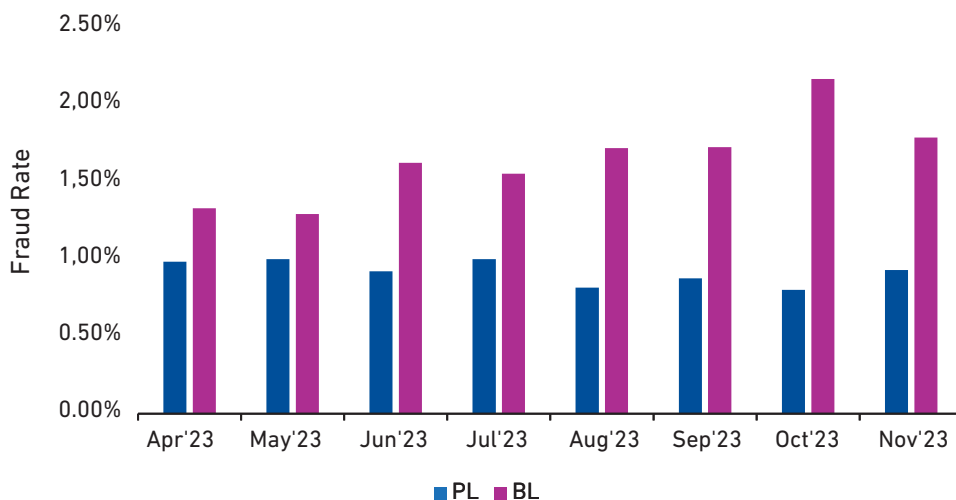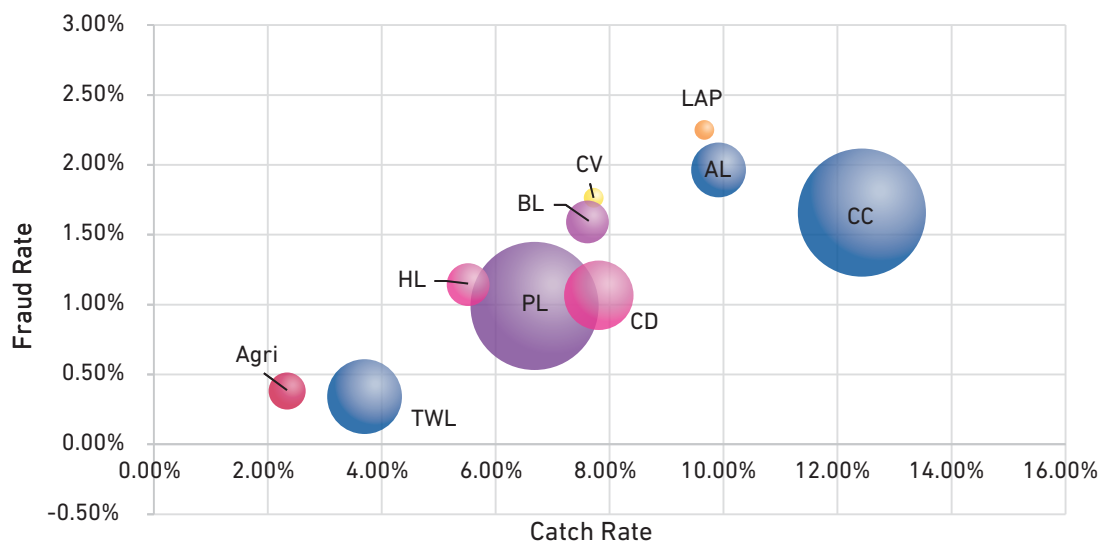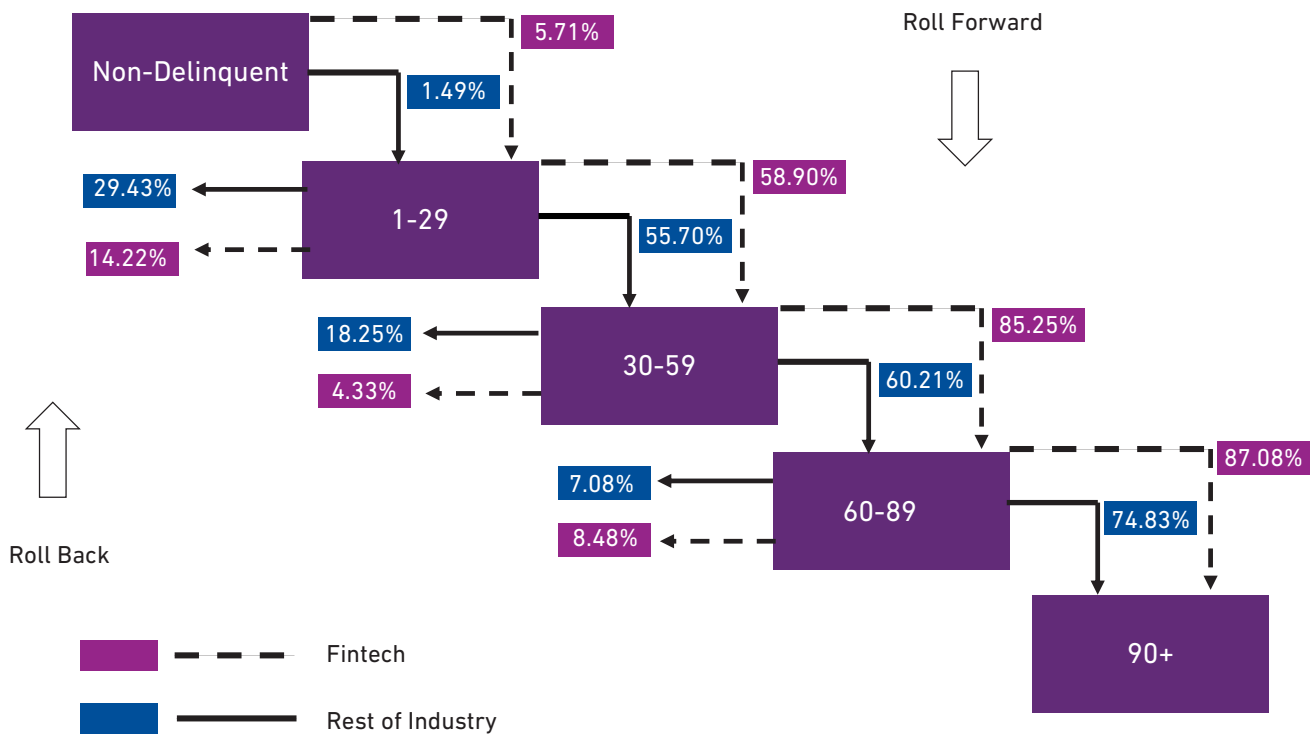

HP
0.96%

PJ
3.50%

UK
0.82%

HR
1.96%

AR
1.60%

DL
1.23%

SK
8.92%

AS
1.29%

RJ
1.13%

UP
0.83%

WB
0.80%

NG
1.93%

BR
0.63%

ML
0.80%

MN
0.85%

GJ
0.99%

JH
0.63%

WB
0.80%

TR
0.53%

MP
0.68%

CH
2.57%

MZ
0.0%

OD
0.32%

MH
0.67%

TG
1.93%

GA
0.001%

AP
0.46%

KA
0.46%

TN
0.72%

KL
1.11%

Low

Medium

AN
2.21%

High

Data Missing

There are locations with high propensity for application-level fraud and additional mitigation measures need to be factored in over and above credit risk mitigation.

Empirical findings on relationship between Fraud Risk and Credit Risk establish they are often independent of each other

Bureau Score

900

800

700

600

500

<700   700-800   801-900   901-1000   1000+
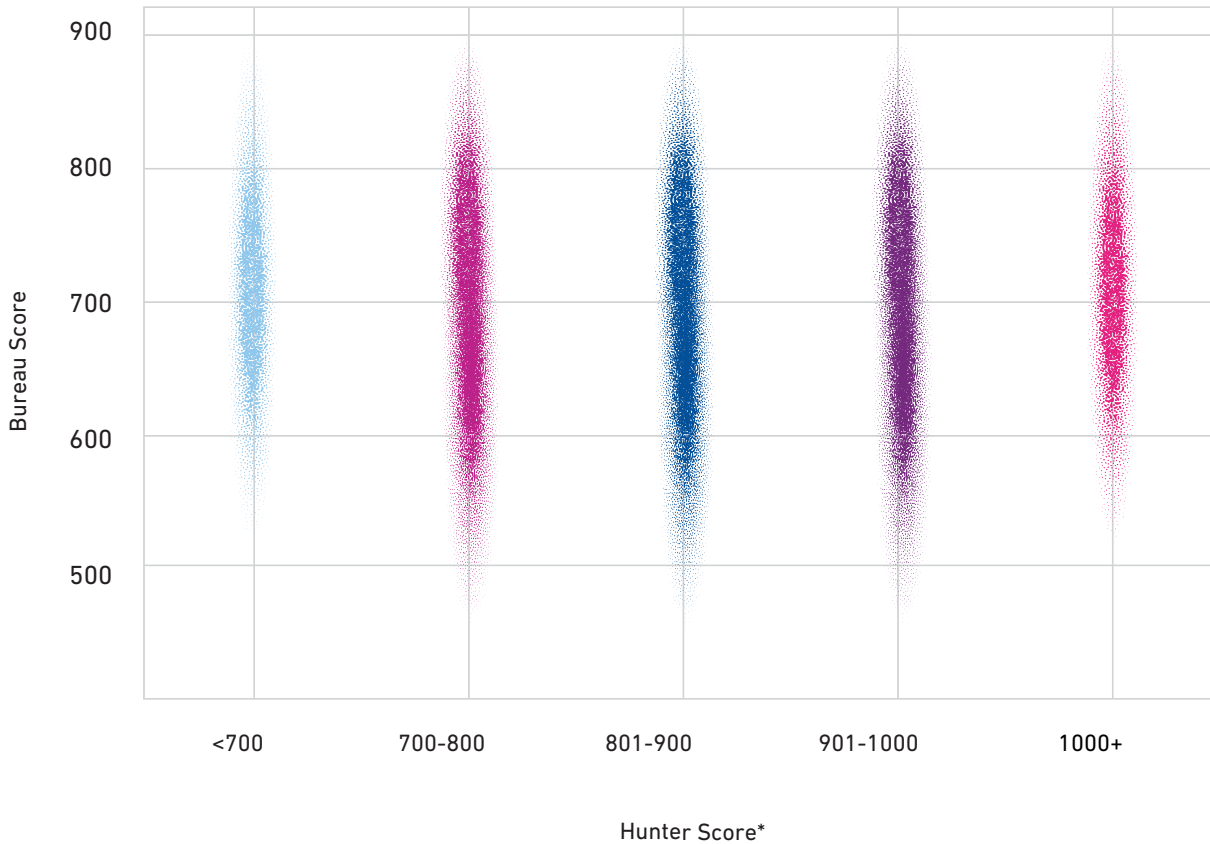
Hunter Score*

- Fintech need to ensure risk mitigation strategy to address fraud at application stage.

- Addressing credit risk alone will not suffice given they are orthogonal risk dimensions

*Hunter Score, developed by Experian, provides Fraud propensity at application level

Core product segment of fintech also prone to fraud at application stage and the tools to combat this is fundamentally different with that of managing credit risk

Fig 2.12-Business and Personal Loan

Fig 2.13

PL: Personal Loans
CD: Consumer Durable Loans
TWL: Two-Wheeler Loans
HL: Home Loans
CC: Credit Cards
BL: Business Loans
CV: Commercial Vehicle
LAP: Loan Against Property

• Business Loan is at higher risk of application fraud compared to Personal Loan.

• This is in sharp contrast to the empirical findings on credit risk where we found Personal Loan risk to be higher compared to Business Loan.

experian.

Fig 2.14

Roll Forward

Non-Delinquent	5.71%
	1.49%

29.43%
14.22%
1-29
58.90%
55.70%

18.25%
4.33%
30-59
85.25%
60.21%

7.08%
8.48%
60-89
87.08%
74.83%

90+

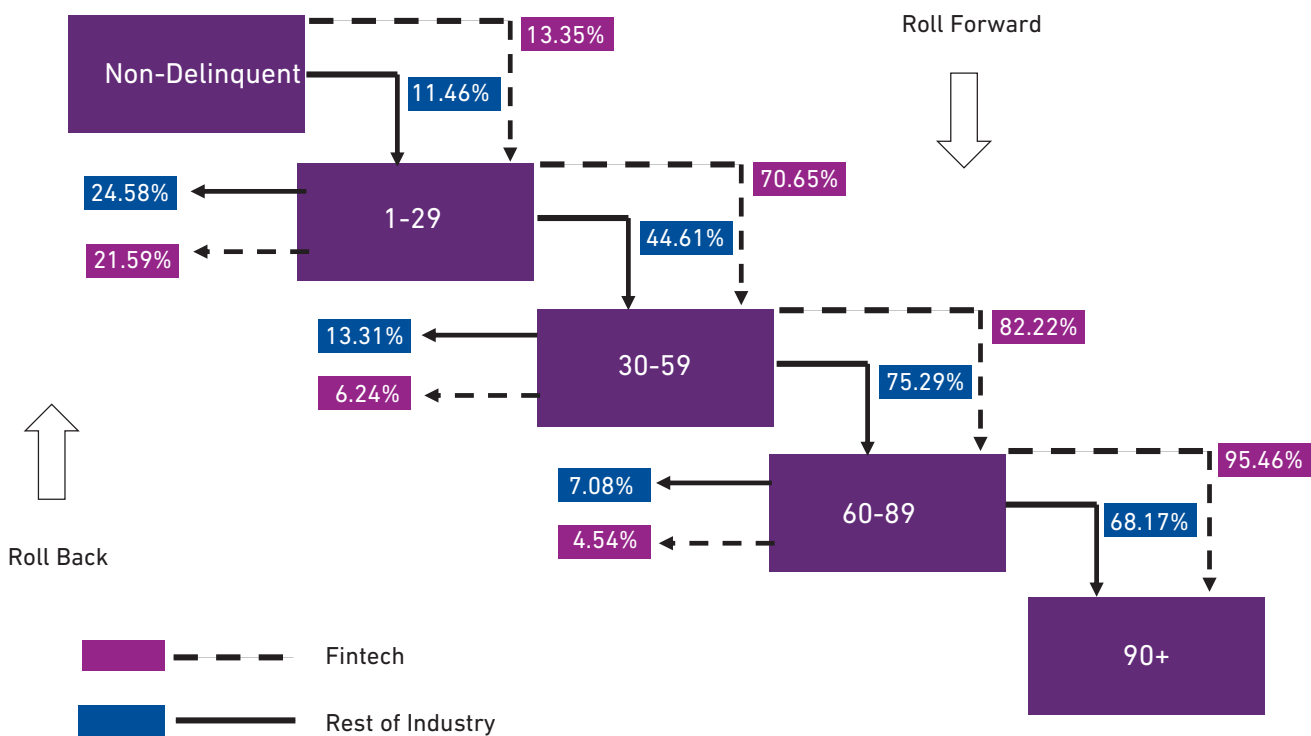Roll Back

Fintech
Rest of Industry

FY23'Q2 - PL

- Absence of strong collection workforce on the ground for fintech hurt them.

- Fintech need to work on unit economies e.g., syndicate approach to get desired ROI on collection investment.

Collection performance for fintech lags with that of rest of industry. Collections inherently is a high touch function especially in deep delinquency buckets. This is one area fintech need to further build capacity.

Fig 2.15

Roll Forward

Non-Delinquent
13.35%
11.46%

24.58%
21.59%
1-29
70.65%
44.61%

13.31%
6.24%
30-59
82.22%
75.29%

Roll Back

7.08%
4.54%
60-89
95.46%
68.17%

90+

■ --- --- Fintech

■ ———— Rest of Industry

FY23'Q2 - BL

- Fintech especially face challenges in collections in deep buckets.

- Deep buckets require physical touchpoint (channel) which fintech have not yet invested in a significant way.

Slippages for fintech has reduced in FY23 and it's a good sign. Recovery rates for fintech is also higher compared to rest of industry.
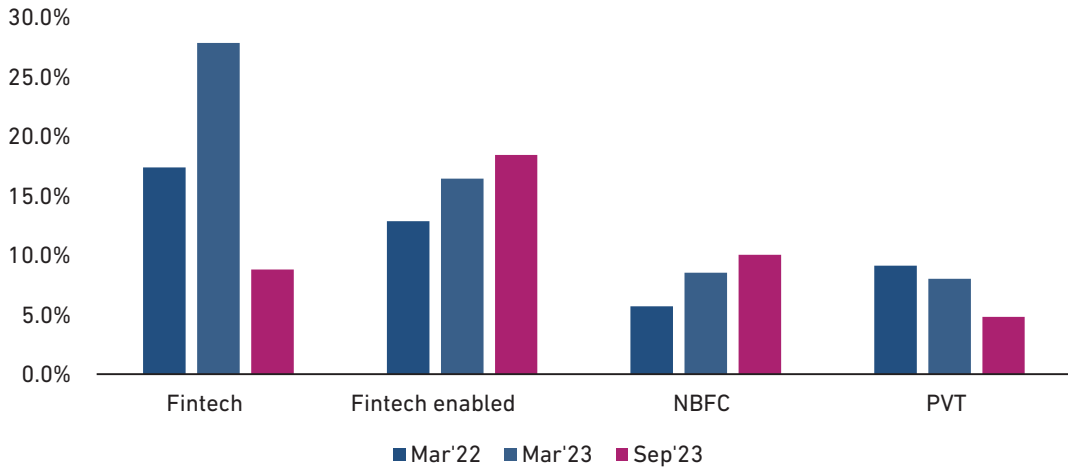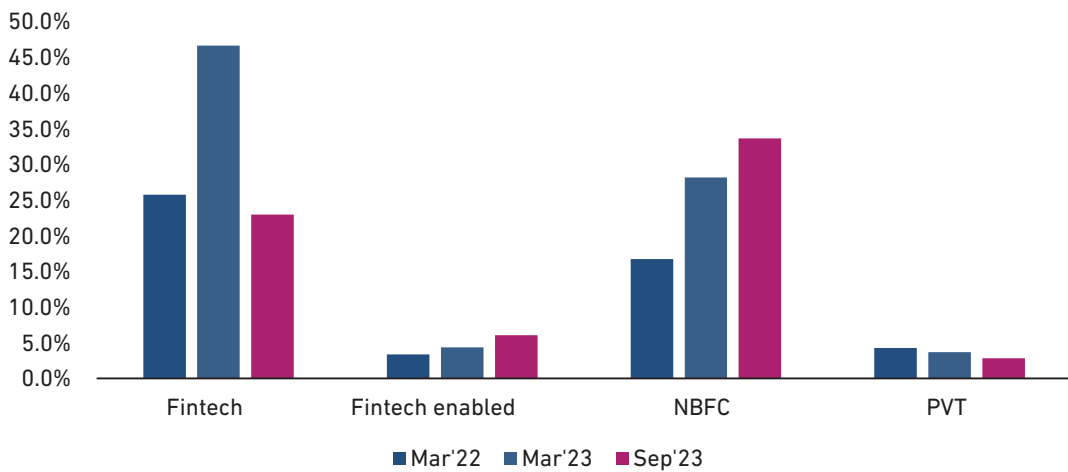
Fig 2.16-Slippages Ratio

■ Mar'22 ■ Mar'23 ■ Sep'23

Fig 2.17-Recovery Ratio
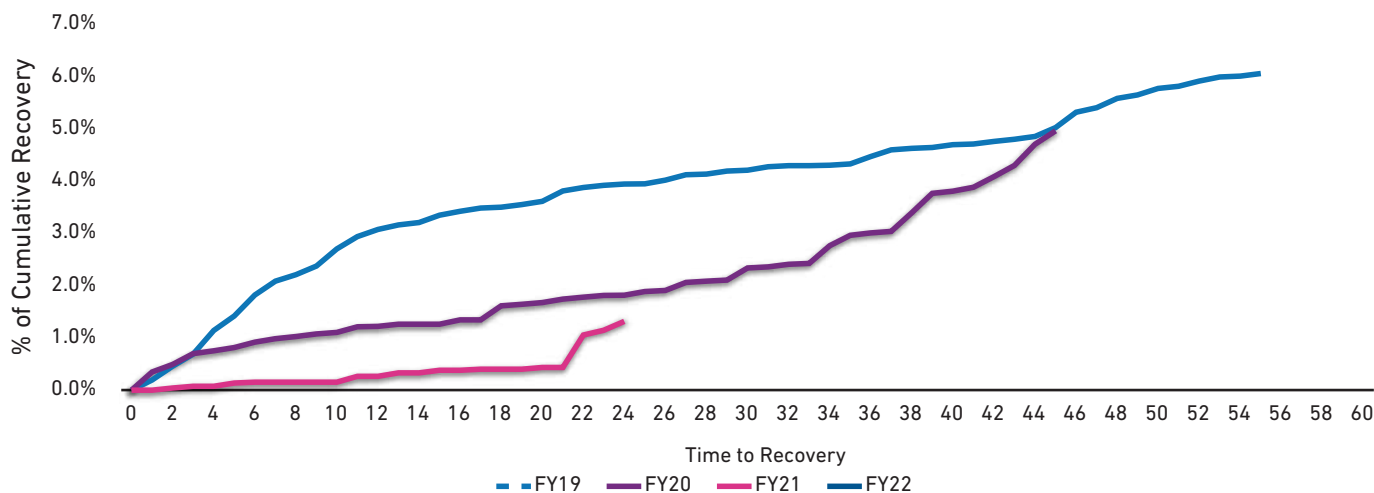

■ Mar'22 ■ Mar'23 ■ Sep'23

- Fintech has controlled the slippages over the period, and this augurs well for the sector

Slippages = Fresh accretion of NPAs during the year / Total standard assets at the beginning of the year

Recovery = % of NPA Recovery over NPA.

There is however still room for improvement on increasing recoveries as fintech performed even better in pre-covid time

Fig 2.18 –Recovery Post NPA

Legend: FY19, FY20, FY21, FY22

X-axis: Time to Recovery (0 to 60)
Y-axis: % of Cumulative Recovery (0.0% to 7.0%)

- Recovery is subdued for accounts that moved into NPA in recent times.

- Overall, we expect recovery rate to be in single digits even after long recovery period.

Fintech have been able to create greater stickiness despite absence of a physical touchpoint in the on boarding journey

Traditional Lender

39% of customers opt for next Personal Loan in next 18 months with Fintech Enabled Bank

~6% of customers opt for next Consumer Durable Loan in next 18 months with Fintech Enabled Bank

40% of the PL base is retained, whereas 54% go to outside for subsequent PL Product funding

Fintech

>50% of customers opt for next Personal Loan in next 18 months with the same Fintech

10% of customers opt for Consumer Durable Loan within next 18 months

65% of the PLbase is retained, whereas 15% go for outside for next PL Loan

THE NEW FINTECH
LENDING PLAYBOOK

- CURRENT STATE SUMMARY
- CHARTING NEW HORIZONS

Existing fintech lending market is showing signs of overheating

Fig 3.1

Customer Cohort	Likely debet leverage	Segment Size		How does it impact(>90dpd in 6mob)	
		Fintech	Industry	Fintech	Industry
Upto 7 PL and No CL	Medium	39%	23%	6%	3%
Upto 7 PL and atleast 1 CL	Medium	29%	18%	7%	3%
More than 7 PL and atleast 1 CL	Very High	14%	0%	9%	11%
More than 7 PL and no CL	High	9%	0%	8%	11%
No PLand CL	Very Low	5%	41%	10%	2%
No PL and atleast 1 CL	Low	4%	17%	11%	3%

• Fintech borrowers tend to have a higher number of Personal Loans.

• Higher leverage often results in subsequent delinquency and hence important to control it.

• Fintech borrowers tend to take subsequent Personal Loan Faster.

Fig 3.2

Fig 3.2 Fintech customer Share and time taken for consecutive Personal Loans(<1L)
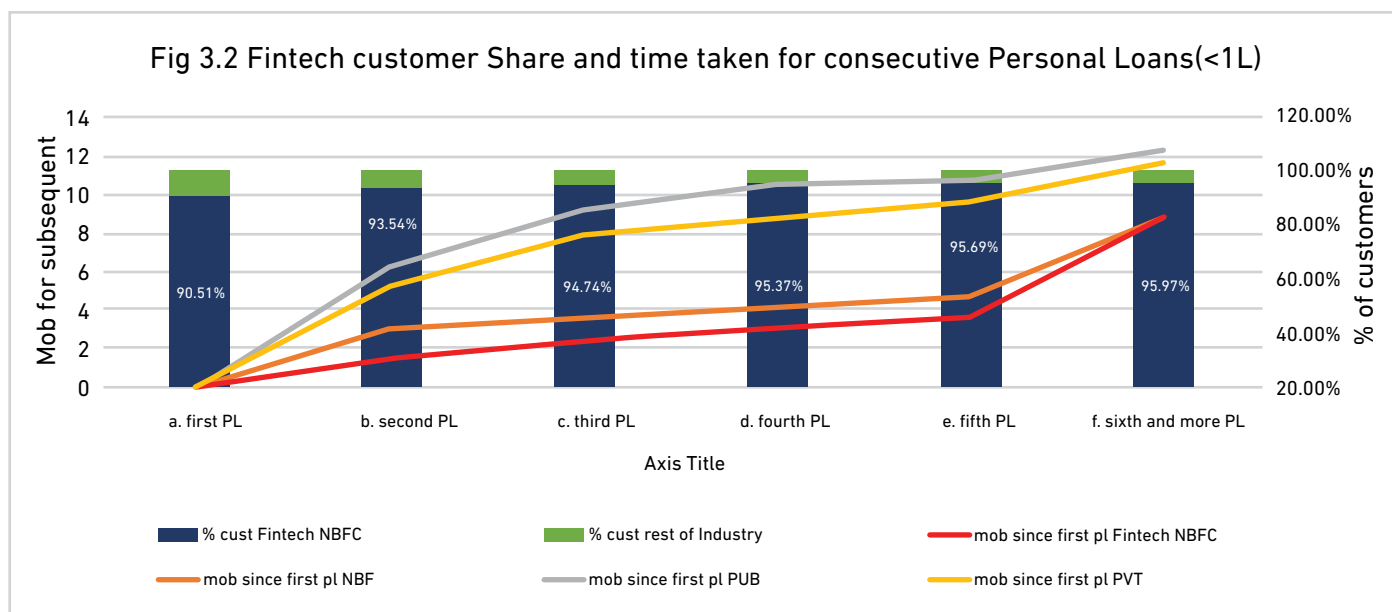
Fintech customer leverage statistics-Comparison with Private Lenders (Fintech vs Private Lender)

Fintech NBFC

64%	**82%**	**11%**
Customers with greater than or equal to 10 Personal Loans	Customers have most recent personal loan only 4 months or less months ago	Customers with current Utilization on all unsecured less than 5%

NUMBER OF PERSONAL LOANS IN LAST 36 MONTHS	MONTHS SINCE LAST PERSONAL LOAN TAKEN	CURRENT UTILIZATION ON ALL UNSECURED PRODUCTS

Customers with greater than or equal to 10 Personal Loans	Customers have most recent personal loan only 4 months or less months ago	Customers with current Utilization on all unsecured less than 5%
37%	**21%**	**21%**

Private

Protect the identified 'blue oceans'

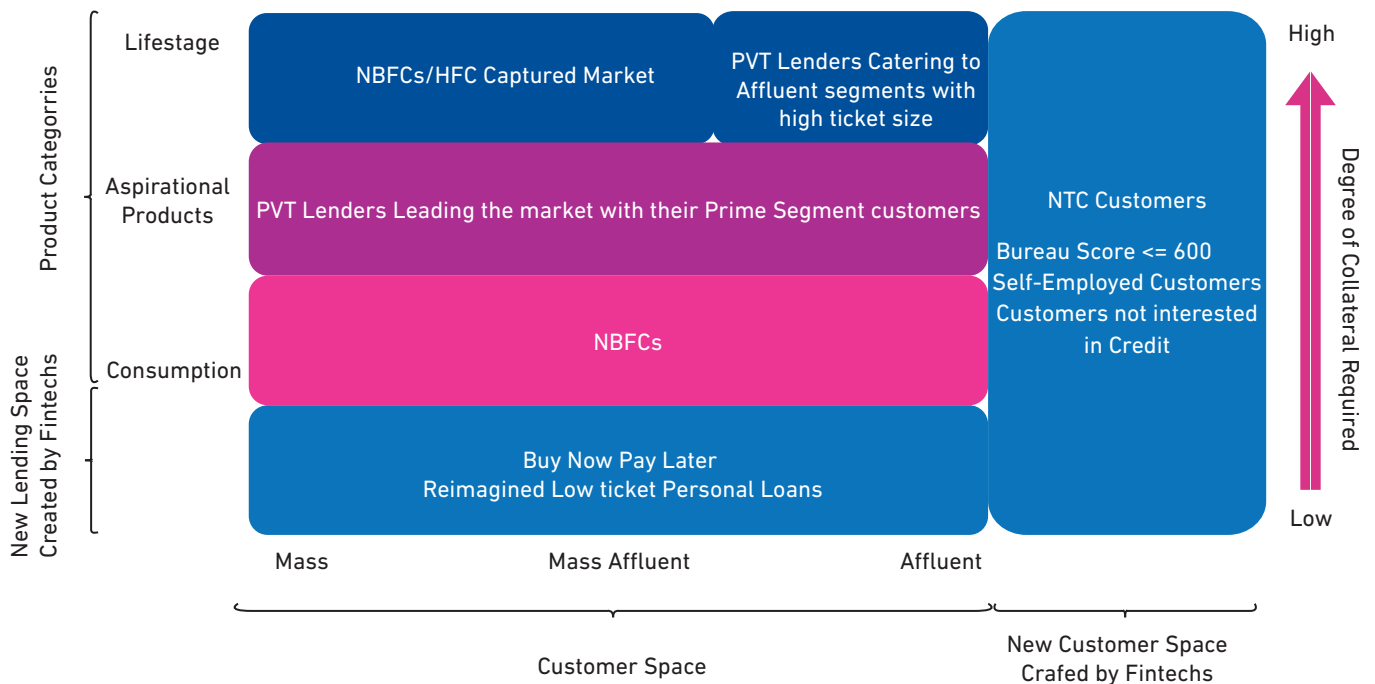From origination champs to a full stack player

Grow to adjacent segments

Leverage core strength to make the most of positive externalities

Be at the forefront in adoption of exponential technologies

Fintech created and nurtured Blue Oceans (Metaphor for New Markets)

- Traditional market spaces had gaps in the market which can be divided into the following categories:

  - Unserved Market
  - Underserved Market
  - Not inclined to take credit

- Consumption based products include Small Ticket PL.

- Aspirational products consists of Credit Cards, Auto Loans, Two-wheeler Loans.

- Life stage products are Home Loan, Loan Against Property.

Further, achieving scale given current asset performance will be difficult as interest rates have already peaked
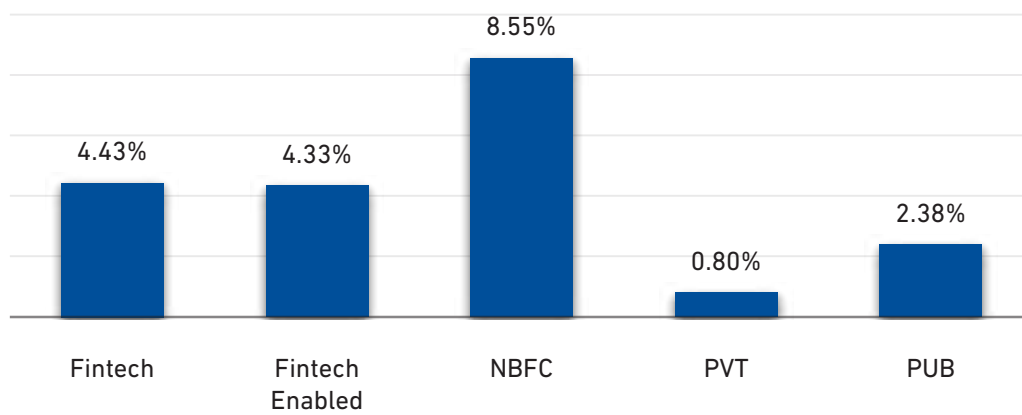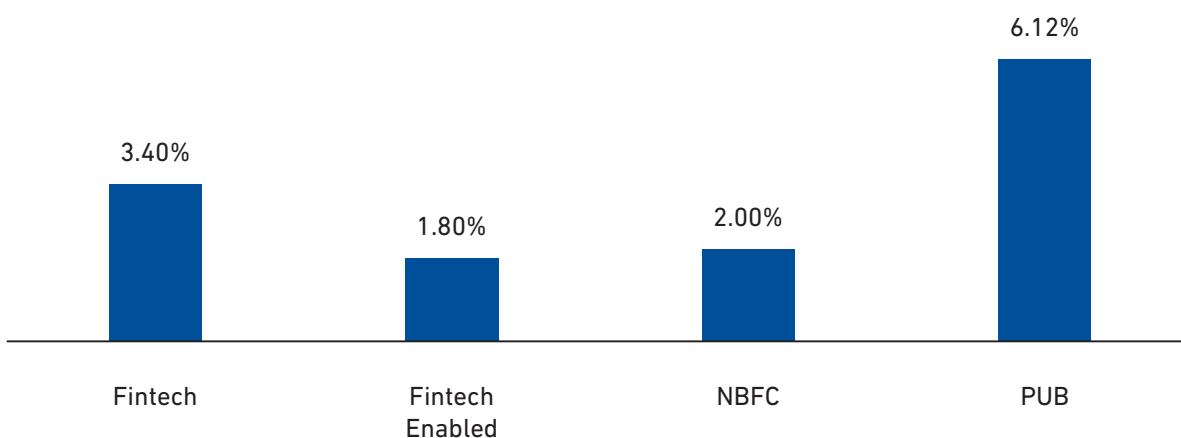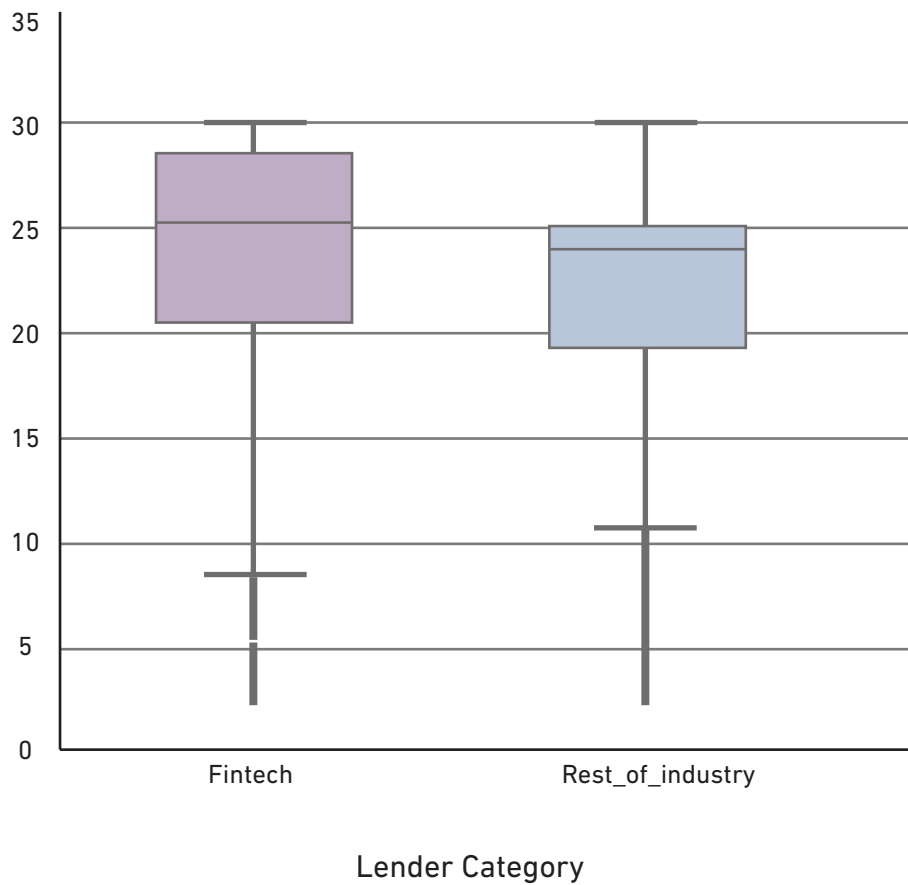
Fig.3.3-ECL PL < 1 Lakh

Fintech	Fintech Enabled	NBFC	PVT	PUB
4.43%	4.33%	8.55%	0.80%	2.38%

Fig. 3.4-ECL BL < 1 Lakh

Fintech	Fintech Enabled	NBFC	PUB
3.40%	1.80%	2.00%	6.12%

ECL (Expected Credit Loss = Probability of Default Exposure at Default * Loss Given Default
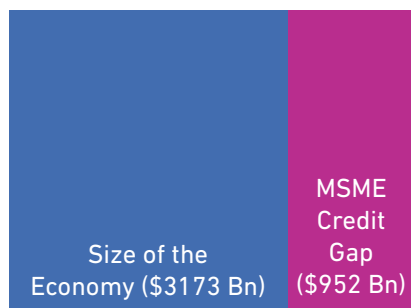
Fig 3.5-Interest rate distribution across lender category

Lender Category

- Fintech have so far been able to manage margins despite higher credit   cost

- It is important for fintech's to continue finding new markets to scale up their value proposition

CREDIT GAP - RELATIVE TO GDP

Size of the Economy ($3173 Bn)	MSME Credit Gap ($952 Bn)

India ranks significantly lower than other economies in terms of credit penetration . This meant that non-salaried individuals, such as small business owners find it difficult to get access to formal credit.

With India's GDP being poised to grow at 6.3% for next 5 years and GOI launching many helpful schemes to help small businesses, need for small and medium sized Business loans, which is already on the rise, is expected to reach new unprecedented levels of disbursements in next few years

- In last 5 years, states like Bihar, West Bengal, Orrisa, Jharkhand and UP have shown high growth in disbursements of Unsecured business loans with ticket size <5 lakh
- States like Bihar and West Bengal has especially shown high level of growth, where customers have increased 57x and 40x respectively (58% share of Fintech In Bihar and 71% share of Fintech in WB

		Share of fintech	
		High	Low
Market Potential	High	Sustain and protect	Expand
	Low	Monitor	–

Best performing districts

Deoghar	Murshidabad	Jamui	Jalpaiguri
Banka	Bhagalpur	East Midnapore	Saran
East Champaran	Samastipur	Saharsa	Cuttack

Discovering new green shoots
(Rising Small business Sectors)
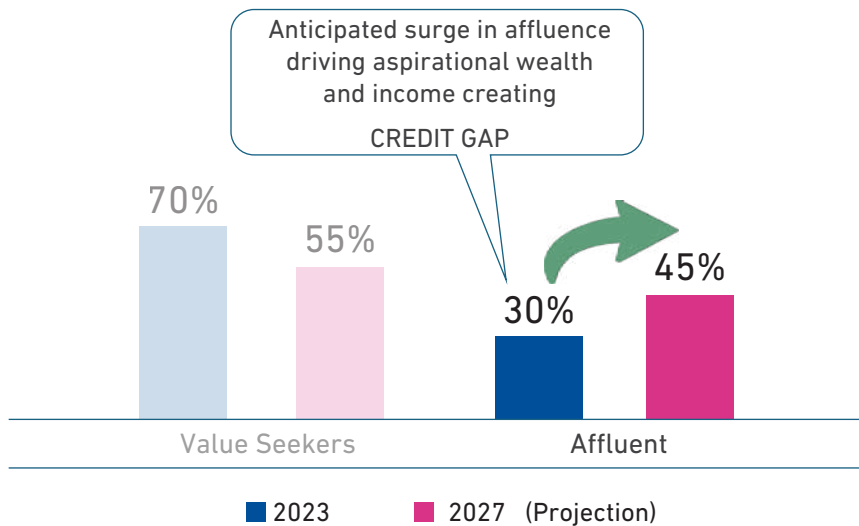
Growth Projection:

Currently 'affluent' people (annual income > US$ 10,000) constitute about 4.1% of the population. Estimated to rise to 100 million in next 4 years.

Strength

Fintech can leverage their advanced data analysis skills to vastly improve sourcing, marketing and upselling to potential consumers.

Weakness

Fintech have most resources and book skewed towards small ticket personal Loan and this may impact scalability.

Anticipated surge in affluence driving aspirational wealth and income creating

CREDIT GAP

70%

55%

30%

45%

Value Seekers

Affluent

■ 2023   ■ 2027   (Projection)

Share of population by income segment (2023–2027E)

Market Impact

Increased affluent populace to fuel demand for high-end consumer goods.

Opportunities

Projected credit need arising out of gap between current income and aspirations.

Threats

Ensuring asset quality on 'new segments' can be tricky owing to lack of credit experience in these.

Fintech ecosystem is likely to face tailwinds spurring growth due to positive externalities
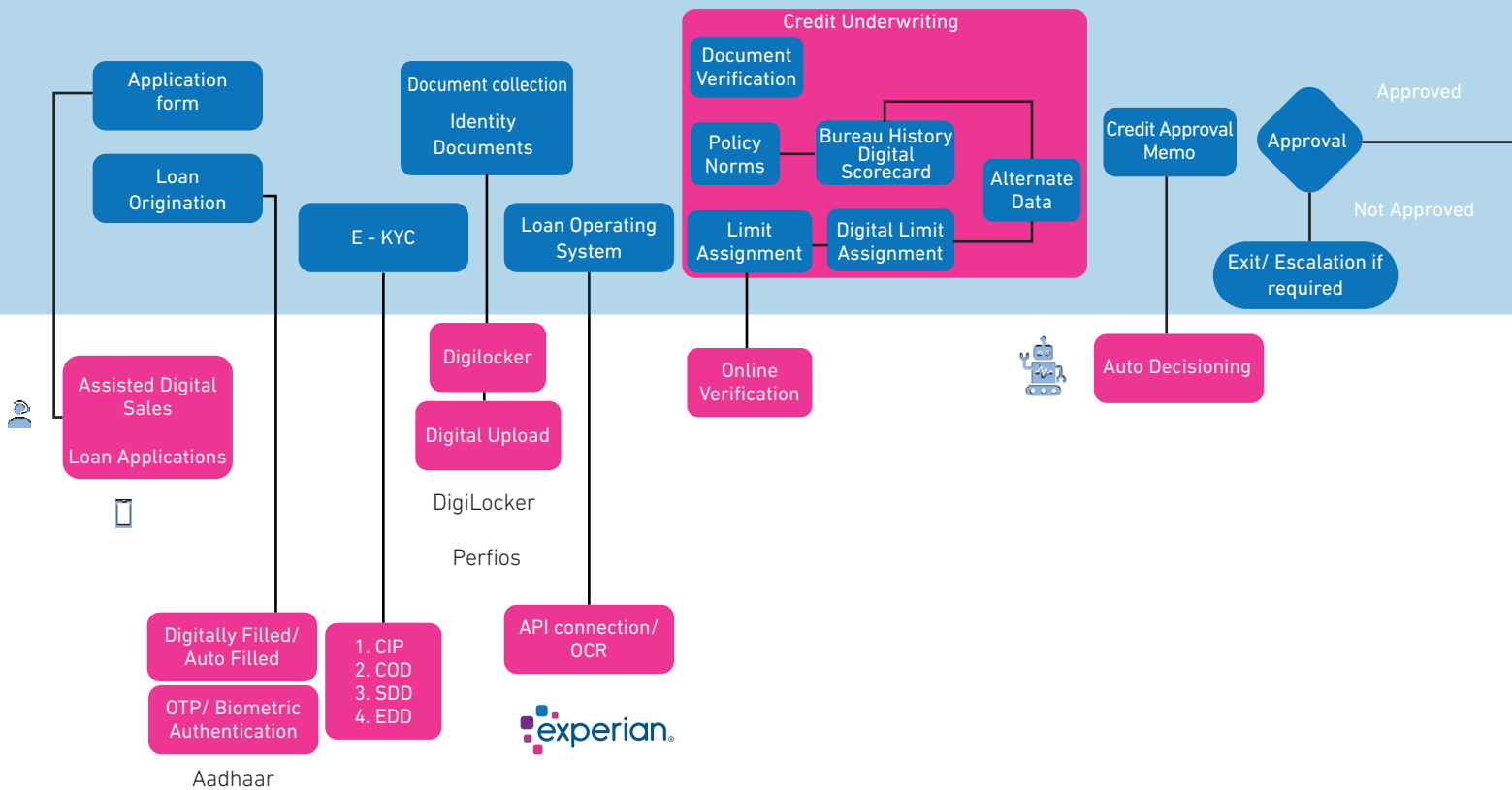
Key Externalities

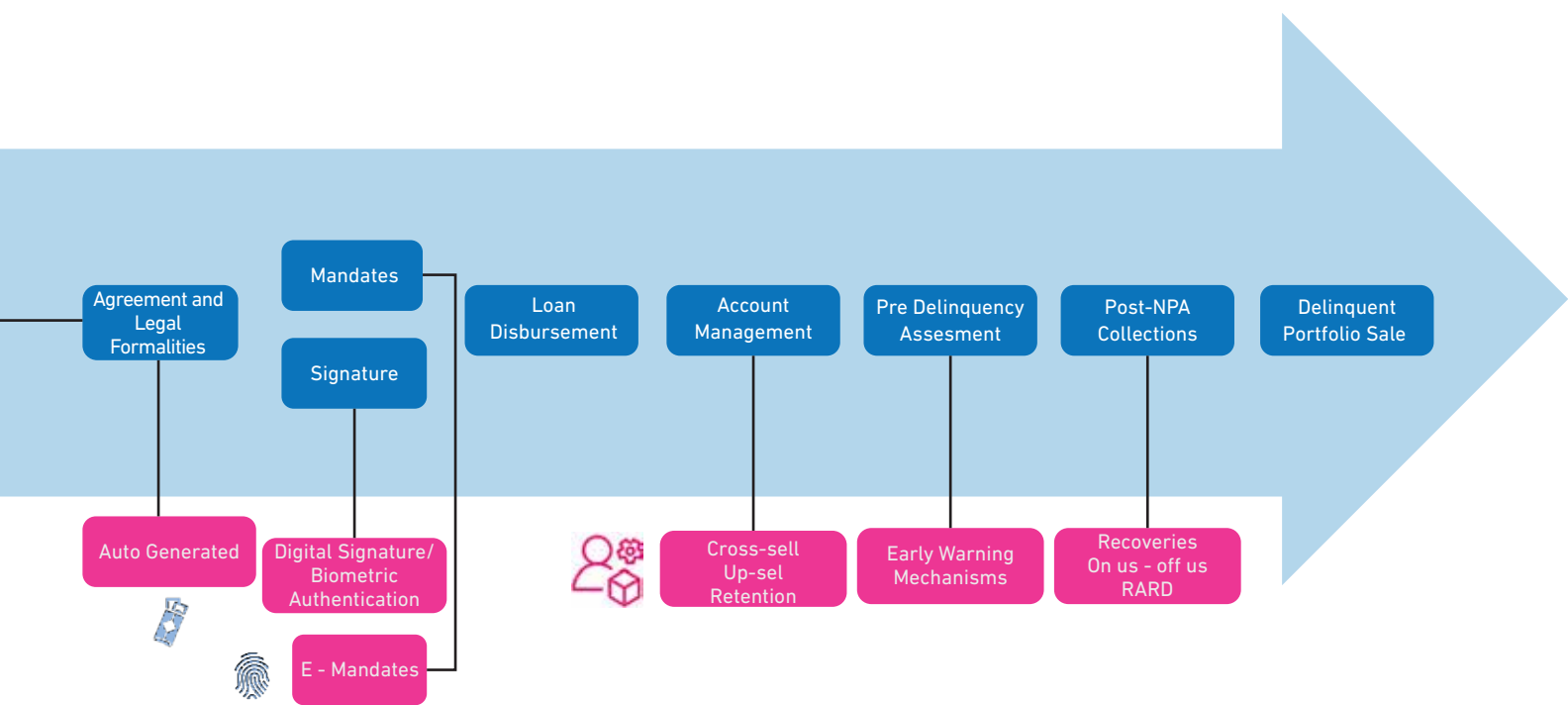| Self - Regulatory Organisation | Exponential Technologies | Government | Economy |
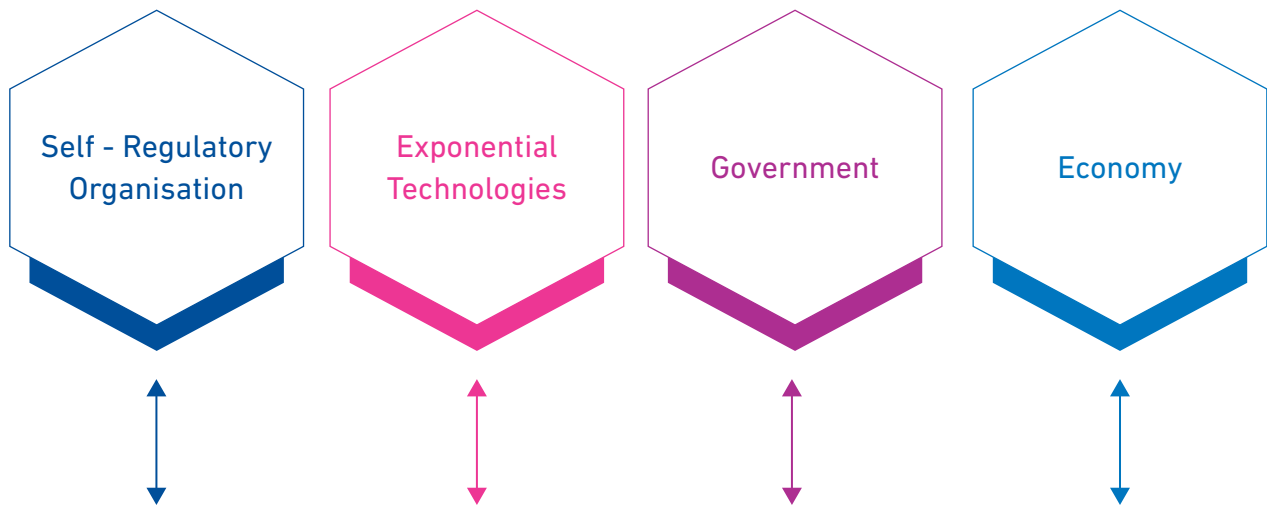
Fintech Ecosystem

Key Developments

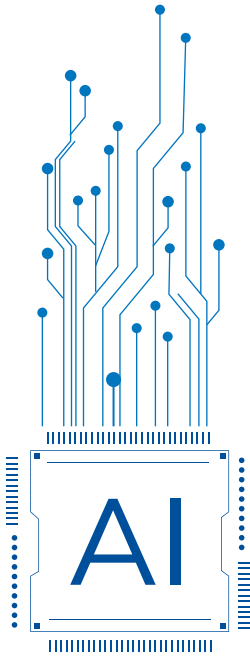| Clarity on FLDG	Enhance customer experience by Gen. AI	Digital Data Protection Legislation	Demographic dividend
Creating assets like Regulatory Sandbox	Cloud to bring down capex	OCEN	Generate higher credit demand

Fintech made the most of thriving digital infrastructure to reduce cost of customer onboarding at scale

Fintech led credit life cycle

Application form

Loan Origination

Assisted Digital Sales

Loan Applications

Digitally Filled/ Auto Filled

OTP/ Biometric Authentication

Aadhaar

Document collection

Identity Documents

E - KYC

Loan Operating System

Digilocker

Digital Upload

DigiLocker

Perfios

1. CIP
2. COD
3. SDD
4. EDD

API connection/ OCR

experian.

Credit Underwriting

Document Verification

Policy Norms

Bureau History Digital Scorecard

Alternate Data

Limit Assignment

Digital Limit Assignment

Online Verification

Credit Approval Memo

Auto Decisioning

Approval

Approved

Not Approved

Exit/ Escalation if required

Agreement and Legal Formalities

Mandates

Signature

Loan Disbursement

Account Management

Pre Delinquency Assesment

Post-NPA Collections

Delinquent Portfolio Sale

Auto Generated

Digital Signature/ Biometric Authentication

E – Mandates

Cross-sell Up-sel Retention

Early Warning Mechanisms

Recoveries On us – off us RARD

Enhancing models with new data sources

With new data sources emerging all the time, Gen AI is one of the technologies that will most likely accelerate the opportunity for businesses to incorporate them into models. Lenders could include sources such as social network data into their models by using LLMs. This unstructured data, including customer emotions and behaviour son social networks, would be treated as an additional variable in the models

Detecting and preventing fraud

Gen AI can play a crucial role in fraud detection by analyzing patterns and anomalies in vast datasets. By leveraging machine learning techniques, Gen AI models can proactively identify potentially fraudulent activities and mitigate risks. The ability to detect fraud in real-time improves the overall security of lending operations and helps protect lenders and borrowers from financial losses.

Personalized customer experience

Leverage customer data to generate personalised product recommendations, and repayment plans. This helps lenders improve customer satisfaction and loyalty, leading to increased customer retention and revenue growth

Operational efficiencies

Gen AI can help bring operational efficiencies to customer journeys across the entire lifecycle, offering lenders the ability to automate and streamline various processes, resulting in improved productivity, cost savings, and enhanced customer experiences.
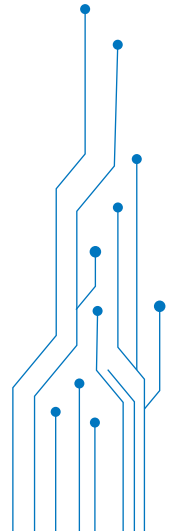
Summary and Recommendations

1

Time for fintech to pivot from topline focused strategy to building a sustainable portfolio. Fintech have achieved scale in the small ticket segment. However, this segment is inherently high risk. While risk-based pricing addresses this, it will affect scalability as borrowers may find credit unattractive in high interest rate regime.

We found Expected Credit Loss (ECL) for Fintech to be ~2% higher compared to their private counterpart. Fintech offset this by positioning their products at higher interest rate. However, Fintech have higher cost of fund and need new revenue lines to maintain margin. Given Fintech operate in a narrow product basket they can collaborate with other lenders on non-compete products to assure themselves a new revenue stream. This is in fact already happening today but needs to scale up further.

Fintech have difficulties in collections as they have limited physical collection shop. Digital collection method can help in targeting situational defaulters who tend to cure or normalize on simple but contextual nudges. To get improved margin there is a need to focus on Customer life-time value through cross-sell and up-sell.

Overall, Fintech need to continue with their leadership on technology adoption as this is what makes up their DNA. Data ecosystem is likely to explode with the proliferation of Open data, but this needs to be harnessed well. Industrialized use of Analytics is an imperative.

2

Fintech lending has come of age in the small ticket unsecured lending market through identification and nurturing of "BlueOceans" (metaphor for new markets). However, there is a need to diversify to new product segments as also foray into new customer segments to achieve further scale.

Fintech have had a strong growth so far in the unsecured small ticket space. Their growth outpaced that of other lender categories like private and public sector banks. Not only this, fintech also enabled other lenders on digital acquisition. Hence, we have a new class of lending which we are calling as "Fintech enabled". The full impact of Fintech, we believe, is not just on what they source but also what they enable.

Presence of Fintech today is largely restricted to small ticket and bite size products. Traditional lenders have a near monopoly on asset backed products. With further inroads into digitization this segment too may become accessible to Fintech. Fintech with greater agility would make up a significant lending pie.

Product segments like Two Wheelers, Used Car financing can be the next big foray for fintech as these have similar Customer characteristics and experience expectations. Further, segments such as newly affluents hold lot of potential in terms of growth.

3

Collaboration with traditional lenders will reach a high degree of maturity, with co-lending expected to be a dominant business model. It is expected that the trend on loan origination outside the core lender will continue with embedded lending. Fintech value proposition in partnership with incumbent will be on how they enhance customer experience in acquisition journey.

Fintech have pioneered experience or context-based lending as against traditional approach based on products and services. However, this is currently focused on consumption-based financing which has a natural pull. This approach needs to extend to unaddressed needs such as home & vehicle purchase, financing for creation of fixed assets etc.

Traditional lenders are also leaning towards "the fintech way" by embarking on digital transformation journey and hence point of differentiation fintech have will diminish. Hence, fintech need to build new competencies which enable enhanced onboarding experience, customer stickiness and robust risk management.

In addition, fintech also need to safeguard against application fraud as this impacts bottom line in a direct way. The product and customer segment fintech cater to are also prone to higher degree of fraud.

4

Regulatory clarity, government investment in digital public good, adoption of exponential technologies and positive outlook on economy provide tailwinds to the growth of the sector and Fintech would especially be the primary beneficiary of these.

Regulatory oversight will increase as market share of fintech increases over the next decade. While this will help increase customer trust, it will also entail greater compliance investments for measures such as cybersecurity, customer data protection, and more.

Recent developments like the passage of Digital Personal Data Protection and now becoming an Act is a move in the right direction.

Digital lending guideline by Reserve Bank of India has brought about clarity on schemes such FLDG (First Loan Default Guarantee). Overall, this will bring greater ownership by the risk bearing regulated entity leading to improvement in asset quality in the long run.

Government initiatives such as OCEN will further help in increasing access to credit at favorable terms to a large segment. Fintech can leverage such frameworks to their advantage.

Finally, as India races to become the third largest economy in this decade itself she will offer tremendous opportunity for everyone to grow. Rising aspiration class and millennials will be significant contributor in the lending pie and these being core to the Fintech they will surely benefit from the India story.

Disclaimer

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Glossary

1. Product Acronyms: -

- PL: – Personal Loans

- STPL: – Short Term Personal Loans

- CDL: – Consumer Durable Loans

- TWL: – Two-Wheeler Loans

- CVL: – Commercial Vehicle Loans

- CC: – Credit Cards

- LAP: – Loan Against Property

- BL: – Business Loan

2. Lender Peer Definition:-

- NBF: – Non-Banking Finance

- PVT: – Private Banks

- PUB: – Public Banks

3. Lexicons:-

- SLIPPAGE RATIO: – Fresh accretion of NPAs during the year /Total standard assets at the beginning of the year.

- DPD: – Days Past Due

- ROLL FORWARD: – Percentage of customers moving to higher dpd bucket from lower dpd bucket.

- ROLL BACKWARD: – Percentage of customers moving to lower dpd bucket from higher dpd bucket.

- OCEN: – Open Credit Enablement Network

- FLDG: First Loss Default Guarantee

- ECL: Expected Credit Loss (PD*EAD*LGD)

- PD: Probability of Default

- EAD: Exposure at Default

- LGD: Loss Given Default

- Hunter Score: Experian proprietary Application Fraud Score

4.Score Ranges:

Score Classification	Experian Consumer Bureau Score
Super Prime	>801
Prime	726-800
Near Prime	651-725
Sub Prime	<650
New To Credit	Customers with no credit history

5. Loan Categorized as Fintech Enabled: Conditions used for identified lenders

Product	City Tier	Ticket Size
Personal Loan	1	<1L
Personal Loan	2,3,4	<1L
Business Loan	1	<10L
Business Loan	2,3,4	<6L