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“From strangers to lenders: - Financial Disruption, p2p in India”

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Abstract:

This research paper aims to analyse the concept of peer to peer lending. The paper revolves around the mechanism of peer to peer lending in India along with understanding the prospects and challenges of p2p lending in India. Peer to peer lending (P2P) is a platform where individuals can lend and borrow money through online platforms regulated by law. It's a virtual base where various lenders and borrowers meet. Presence of social media is one of the principle features, First P2P online platform was started in 2005 with “Zopa”. The paper concludes that p2p lending will soon flourish in India.

Key Words:

p2p lending, financial disruption, peer to peer lending.

Introduction:

With the consultation paper released by RBI in 2016, P2P laid its roots in India. There are around 15 entities that have the licence to operate p2p platforms. Peer to peer lending (p2p) lending enables individuals to borrow and lend money through online platforms that match lenders with borrowers, and was expected to disrupt the consumer lending business, like what digital transactions have done to consumer payment. P2P lending service providers have been in business in India since early 2014, but until 2016, there was no regulation around it. In September 2017, RBI notified that these will be registered as non-banking financial companies (NBFCs) and came out with guidelines for P2P lending platforms a month later. The size of the Indian P2P lending market is around ₹ 200 crore, said Rajat Gandhi, founder and CEO of P2P platform Fair cent, owned by Fair assets Technologies Pvt. Ltd, one of the first P2P lenders in India that got RBI registration. The interest rates are usually determined by the platform, sometimes the rates are set as per mutual agreement between the lender and the borrower. Peer - to - peer lending companies are for - profit organisations that generate revenue from fees paid by borrowers and lenders.it is for both depositing money and lending money. Any Indian resident, above 18 years of age, with a valid bank account and PAN can lend on the platform. Any non-banking financial company listed by RBI or companies formed under the Indian Companies Act can also apply as lenders.

Literature Review

Vinod Kumar (2016) extol their paper titled “credit risk analysis in peer to peer lending” has analysed the credit risk involved in p2p lending system of “lending club” company. the paper concludes by coining a model system for peer to peer lending that how company can acquire good credits and identify potential defaults for minimizing risk.

“Why peer to peer lending is struggling to take off in India” by Pratik bhakta talks about various struggles of p2p in India , The problems that plague the sector are various, from the profile of the borrower to the restrictions that the central bank has put on the business to prevent it from creating any systemic risk to the economy. While Indians typically stay away from any risky business, which P2P lending is, those who are ready to take the bet face regulatory restrictions, like a cap on the money they can lend.

Alexander Bachmann in his paper, “Journal of internet banking and commerce” investigates various determinants that play a very important role in the process of funding. It also focuses on variables that influence funding success and interest rates of loan request. paper gives brief overview of p2p lending market operating online.

“Peer to peer lending: An Empirical study”, written by Robert h. smith provides important information on how social networks provide important credit information about borrowers. It studies whether and how network metrics affect the outcome of financial transaction in the market and whether such credit worthiness is supported ex post through loan performance data.

“Lessons for p2p lending in India” article written by S.Z. Saleem focuses on working of p2p market in china and how India can learn from it. The P2P lending industry in China has 50 million registered users and \$192 billion of outstanding loans, according to the Bloomberg report. Other estimates put the size of outstanding loans through P2P lending platforms in China at \$430 billion. We are talking about China? That’s because a P2P lending market is slowly developing in India too. However, investors, who become lenders in P2P lending, looking to make money through the interest they earn by loaning an amount need to be careful.

Observations drawn from review of literature:

The researcher has done extensive review of literature. The available literature hardly comments upon the mechanism and prospects and challenges of p2p lending, hence it provides a research gap therefore the current research paper is an attempt to study the concept, mechanism, and prospects and challenges of p2p lending in Indian context.

Objectives:

- 1 To understand the concept of Peer to Peer Lending
- 2 To study the Mechanism of Peer to Peer Lending
- 3 To identify the Prospects and Challenges of Peer to Peer lending in India.

Research Methodology:

Research Design:

Research design opted is exploratory in nature. The researcher has done extensive review of literature.

Secondary Data:

The secondary data was collected through Scholarly articles from various online journals Research Papers, Magazine Articles, Newspapers etc. Mainly Google Scholar articles.

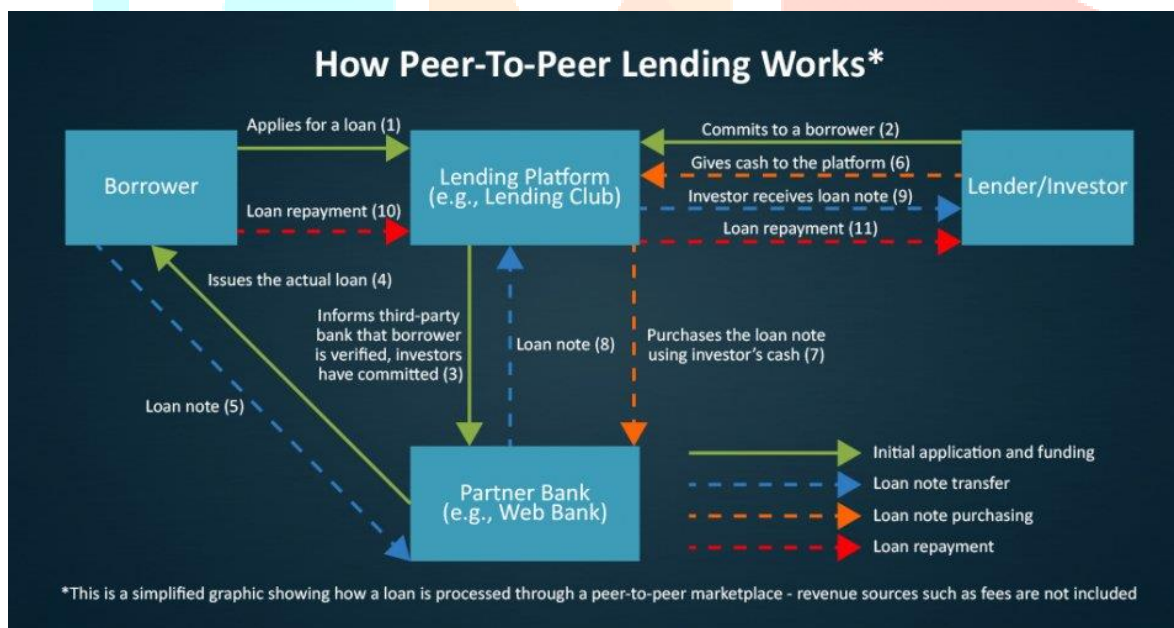
Data Analysis:

The secondary data so obtained is analysed and presented in a systematic manner such as : First Part represents Mechanism of p2p lending, second part covers features and last part covers prospects and challenges of p2p lending.

Mechanism of p2p lending:

“The main process of lending mechanism is almost the same across different online peer-to-peer lending platforms. Potential users, including borrowers and lenders first have to register with personal information, such as ID card number, bank account, personal information in a third-part credit institution, etc. Based on this information, credit rating of users is calculated. The lending procedure is initiated by borrowers. Borrowers indicate the amount they want to borrow and the maximum rate they are willing to offer, and to provide some other optional information, such as loan purpose, repayment period, listing auction format, etc. Lenders provide certain amount of money and choose a lending pattern. Currently, there are two patterns. One pattern is the lender chooses a borrower on the platform, and borrows the money to him/her. Another pattern is the lender puts money in a pool of funds. The P2P lending company dispatches the money to different borrowers. In this pattern, a lender doesn't know the borrower's information.

When a borrower's requirement is fully funded, the related transactions are sent to the lending intermediary for further review before becoming a loan. In this stage, some additional documents may be asked for to demonstrate their credibility. Once a listing is materialized into a loan, money will be transferred from the accounts of listing lenders to the accounts of listing borrowers”. ---taken from springer open



P2p process is more convenient than bank loans here interest rates can be negotiated between borrower and lender. Process of taking background information is much different here p2p majorly depends on the techniques of data mining for scanning background information and there is much risk involved in p2p as compared to bank loans.

Features of p2p lending in India:

The features are explained as below for the lenders and for the borrowers

For lenders

- 1) Age criteria- Any Indian resident, above 18 years of age, with a valid bank account and PAN can lend on the platform. Any non-banking financial company listed by RBI or companies formed under the Indian Companies Act can also apply as lenders.
- 2) Lender becomes Investor- become an investor, you can sign up and fill in the basic details about yourself and pay the registration fees through debit/credit card, net banking, etc. Your registration will be verified within 12-24 hrs. Once approved, you can log on to your account online and start lending.
- 3) Maximum amount and duration of lending- One can start with a minimum amount of Rs 750 per loan. Borrowers are registered for a period between six and 36 months. You can choose the borrower according to the loan duration suitable to you.
- 4) Expected rate of return- Lenders can expect returns in the range of 12-28 per cent, depending on how you spread your investment. Returns also depend on the ongoing demand for lenders on the platform.
- 5) Maximum amount investment- an individual lender can invest up to 20 per cent, high net worth individuals can invest up to 50 per cent, and institutional lenders up to 100 per cent of the total loan amount requested by an individual borrower.
- 6) Action taken for non-payment- In case of any default, additional penal interest will be applied to the due amount for the duration of delay which borrower(s) will be liable to pay directly to their lender(s).

Features of borrowers

- 1) Age criteria- Any Indian resident, above 18 years of age, with a valid bank account and PAN can borrow on the platform.
- 2) Registration- You can sign up and start the registration process. You must fill in the basic information, pay the registration fees and upload the required documents. Once your identity is verified and credit profile checked by the platform, you will be qualified to borrow. Once your registration as a borrower is approved, you can apply for a loan on the platform.
- 3) Documentation- Apart from the CIBIL score, other parameters like repayment ability, income stability, past performance and intention of the borrowers, and documents like salary slips, bank statements, ITRs, among others, would be required while applying for a loan.
- 4) Maximum amount for borrowing- If it is for personal use, loan amount can vary from Rs 30,000 to Rs 5 lakh. For business purposes, you can apply for a loan of up to Rs 10 lakh.
- 5) Loan tenure- Loan tenures can vary from a minimum six months to maximum 36 months

- 6) Repayment of loan- You can close the loan three months after the disbursement without any additional charges. Pre-closure before three months can be done after paying balance interest due to lenders for

a period of three months from the date of disbursement. This is payable directly to lenders. P2P platform may charge one-time non-refundable pre-payment fee

7) Expected rate of interest-Interest rates are calculated by an automated credit appraisal system that uses the personal and financial information provided by borrowers. The interest rate ranges from 12 per cent to 28 per cent. Unrated borrowers may be registered at higher interest rate.

Leading Peer-To-Peer Lending Platforms

	Faircent.com	ILend.in	Lendbox	Loanmeet
Number of lenders	5,000	1,300	900	670
Number of borrowers	20,000	3,500	2,000	1,500
Hit rate (possibility of getting funded)	1/10 applications	3/10 applications	6/10 applications go through	1/20 applications
Commission	1% from lender; 2-6% from borrower depending on creditworthiness	1% from lender; 3% from borrower	2-6% from borrower	2-5% from borrower
Registration fee	₹1,500 (refundable if funds not raised)	₹500	Nil	₹1,000, 50% returned if funds not raised
Total disbursement	₹2 crore	₹90 lakh	₹75 lakh	₹61 lakh
Lenders' mandate	₹10 lakh of investible funds; above 25 years of age. Investments in stocks & possession of immovable property	Annual income of ₹8 lakh, PAN card, "only graduates"	PAN card, ID proof, one cheque leaf	Insist co-investing
Borrowers' mandate	Salaried borrowers, SME owners with cash flows	Salaried borrowers (₹25,000 per month, 6 months continuous employment)	No salary/income limits, three security cheques	Pan, Aadhar & bank statements, 1 banking transaction from borrower's account favouring Loanmeet.

Prospects of Peer-to-Peer Lending:

The prospects of Peer to Peer Lending is elaborated as below for lenders and borrowers separately

For lenders:

- 1) Potentially, higher returns than savings and mutual funds
- 2) Receive monthly payments with interest
- 3) Diversify your risk across many different loans rather than making a single loan or investing only in stocks.

For borrowers:

- 1) Lower interest rates and lack of collateral requirement for a loan.
- 2) online and potential application
- 3) fixed monthly payments
- 4) Credit requirements may be less strict than at a bank
- 5) No prepayment charges
- 6) p2p lenders may be more inclined to invest in business ideas than banks would

Challenges in peer to peer lending

- 1) Higher risk for both principle and interest amount.
- 2) Prevalence of conservative culture in India.
- 3) Lower security than a bank.
- 4) No uniformity when it comes to requirements, changes from lender to lender.
- 5) Risk of losing your money if borrowers default.
- 6) Less liquidity than stocks or bonds because of long time horizons (three to five years).
- 7) Lesser protection or regulation to prevent fund, delinquency.

Findings:

- 1) p2p is in its initial stage in India , there is a saying that, “There is a perception that one who cannot get loans anywhere else can get so from a P2P start-up, this needs to go,” said Achal Mittal, cofounder of Liquiloans.
- 2) Due to strict RBI regulations and conservatism culture in India. P2p is struggling to take off in India, it’s an easy and most convenient form of loan exchange which will soon flourish.
- 3) P2p modelling needs to be restructured to minimize the risk for both borrowers and lenders.
- 4) Conservative nature of the investors also restricts them to be away from p2p lending
- 5) It is found that Maximum amount is Rs 10 lakh which is very small for large pocket investor.

Conclusion:

P2p is one of those platforms which engage future of lending in it. from simplified online process to flexibility in the interest rates p2p is most easy and convenient form of lending system, with the increasing rate of online users and connecting it to lending system makes it handy for use but it also suffers with many problems. With convenience comes high risk, procedure needs to be modelled so the risk becomes low which will lead to increase in confidence of people. RBI can take initiative towards restructuring the p2p lending which will encourage the layman to take benefits of p2p lending. needs to make some changes as to increase highest amount invested so that heavy pocket investors can also invest.

Thus, the current paper concludes with the entire discussion on the pros and cons of p2p lending, mechanism of p2p lending in detail.

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