MONEY MANAGEMENT INDIA

Peer-2-Peer lending in India

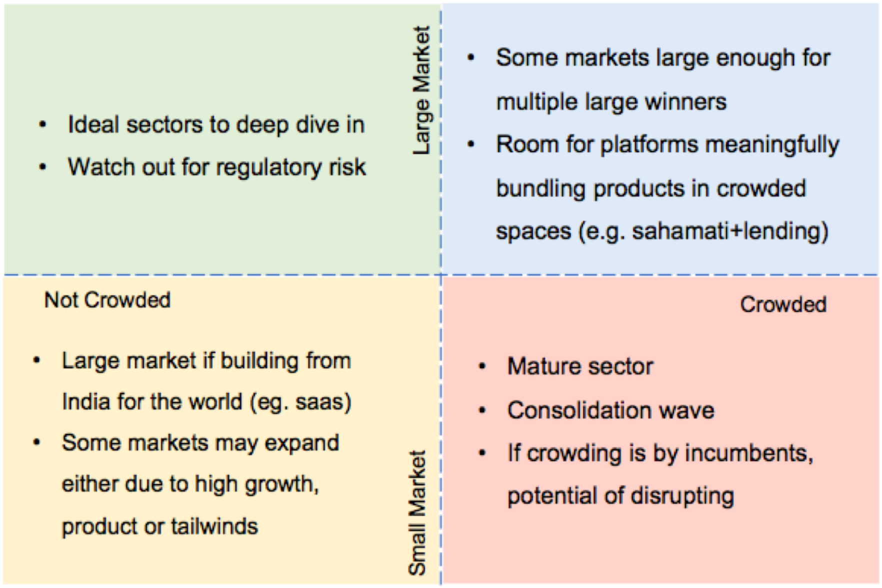
Applied, January 2022

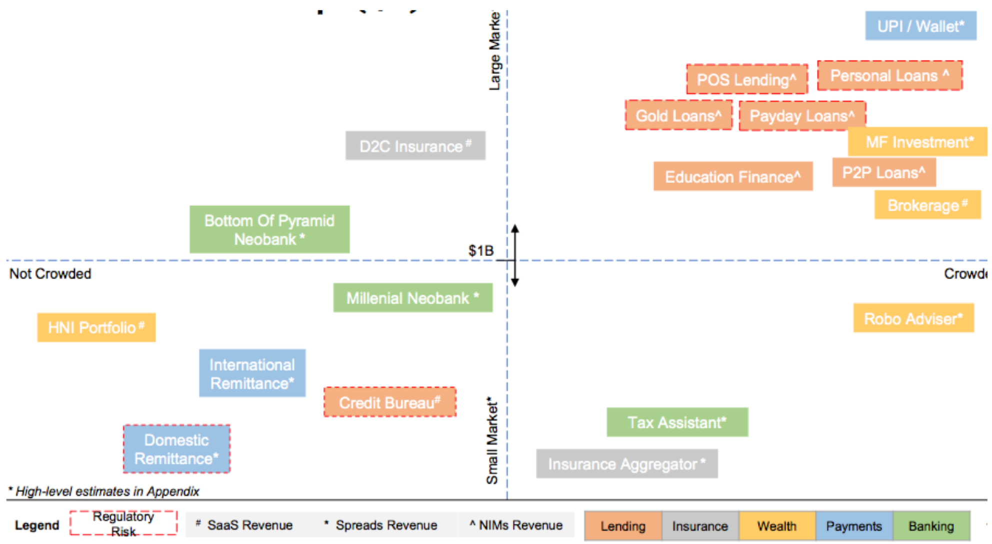
India's P2P lending market overview

- Peer to Peer (P2P) lending service providers have been in business in India since early 2014, but until 2017, 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
- P2P lending platforms now have to hold licenses as **Non-Banking Financial Companies (NBFC-P2P as per RBI directive 2017)**
- As per the economic survey, traditional banks disbursed only 5% of the loans to MSEs. The shortage of funds can be filled by the P2P lending industry leading to the popularity of this sector among the small scale enterprises.
- According to a report by PwC, India's P2P lending is expected to be USD 4 billion in next five years (2026) which is very low as compared to China's current P2P lending which is USD 100 billion.

Source: livemint.in, pwc.org.in

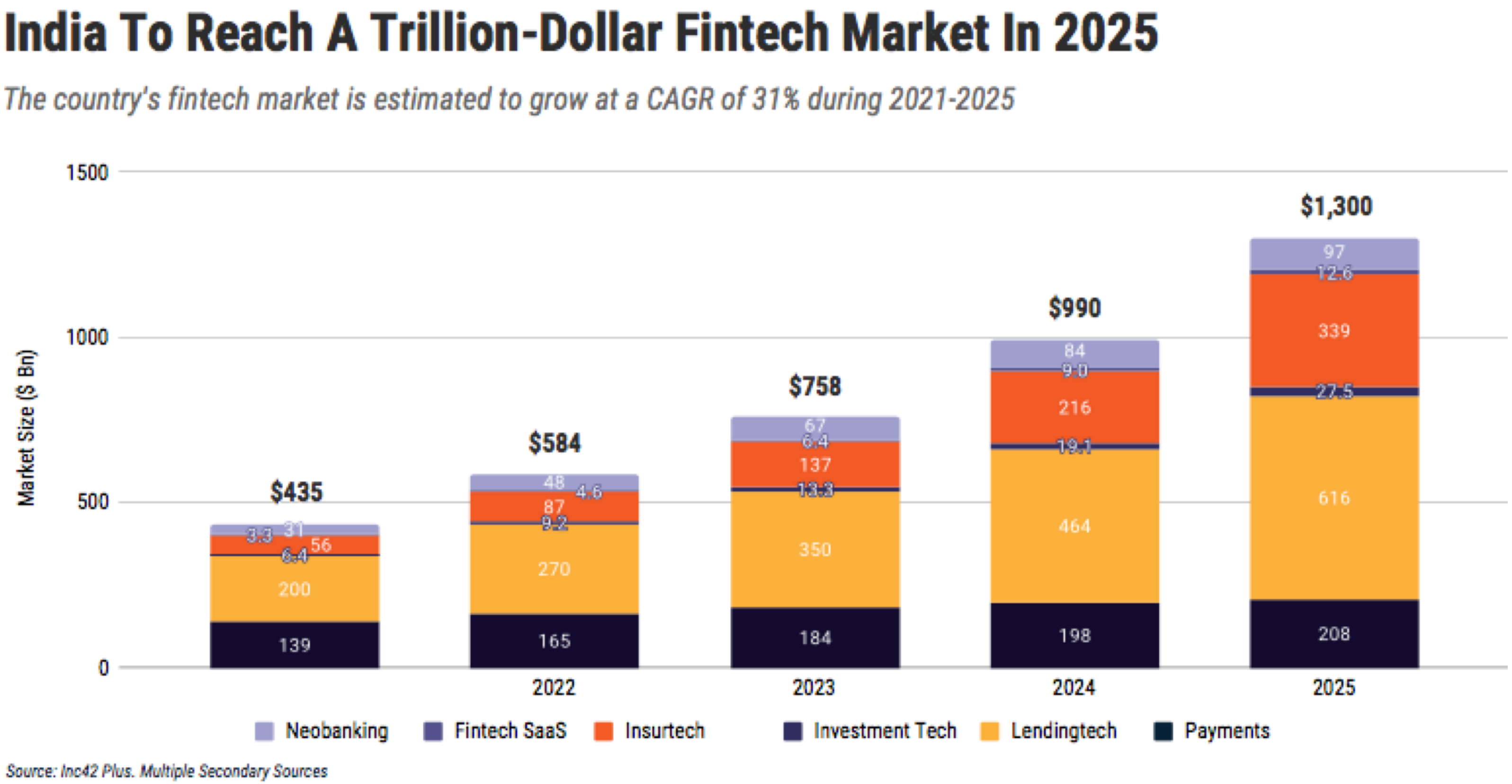
P2P is part of lucrative lending market





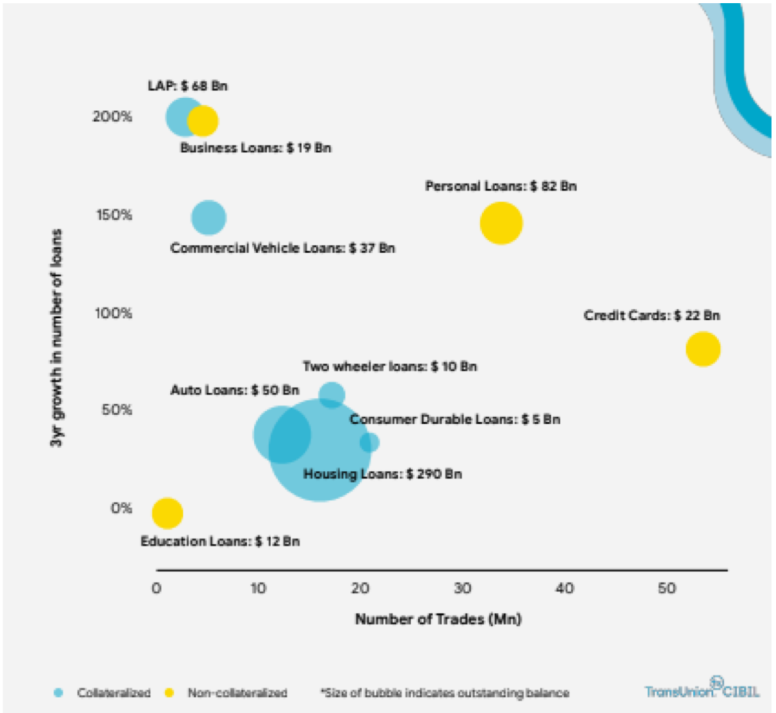
Source – Blume Fintech Report

Lending is biggest segment



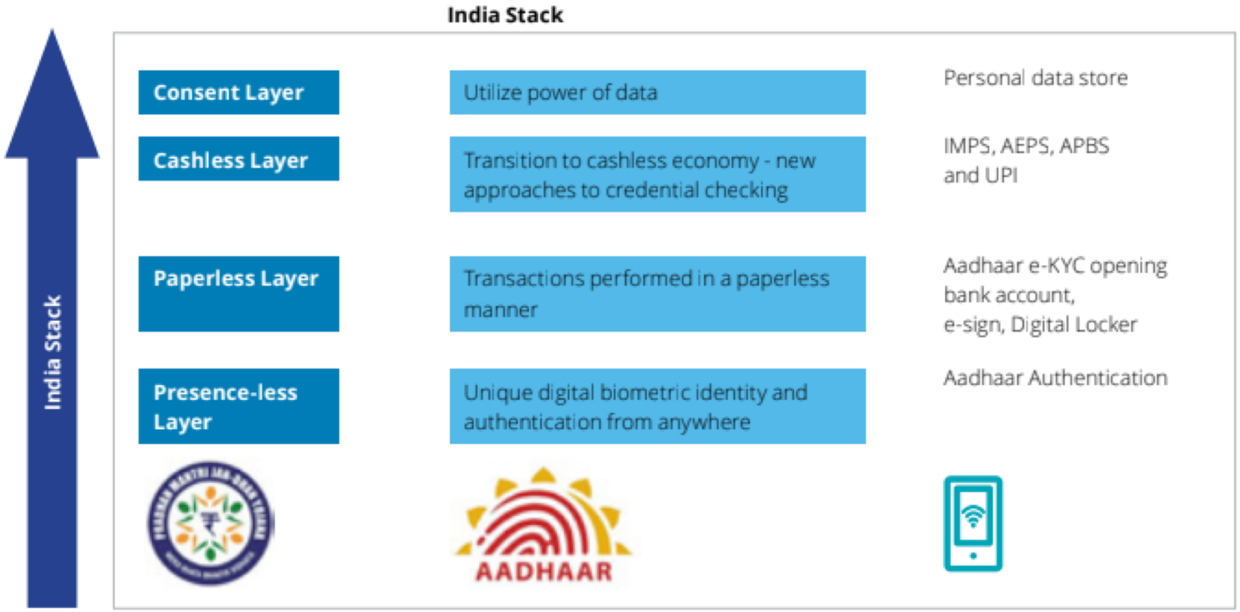
Source – Inc42 State of Fintech Q1 2022

P2P are small un-collaterised personal loans - showing one of the fastest growth rates



Source – Transunion CIBIL/Google

India Stack has enabled fintech...



Source: Credit Suisse reports, News articles, Deloitte analysis

...and P2P is poised for break-out

Areas	Fintech Segments	Creating new value propositions	Designing new business model	Shaping long term customer behavior	Expanding market	Fostering collaboration and working within regulatory purview	Eliminating legacy constraints	Leveraging data and analytics
A. Credit	01. Peer-to-Peer Lending	Medium	High	High	Low	High	High	Medium
	02. Crowd Funding	High	High	High	Low	Medium	Low	Medium
	03. Market Place for Loans	High	Medium	Low	Medium	High	High	High
	04. Online Lenders – NBFCs using own capital	Medium	Low	Medium	Low	Medium	Medium	High
	05. Credit Scoring Platforms	Low	High	High	High	Low	Low	High

Likelihood of Breakout High Medium Low

Source: Deloitte Analysis based on interaction with Industry participants

Regulatory framework

Eligibility to become a NBFC P2P

To obtain the NBFC license for P2P lending and a certificate of registration (CoR) from RBI, the applicant needs to -

- Be registered as a company in India, under the Companies Act.
- Have a **net owned fund (NOF) of not lesser than INR 2 crores**, or more, as stipulated by RBI.
- On the application, RBI would verify and may grant the NBFC certificate of registration for providing P2P lending.
- All P2Ps are to be registered with the RBI as an NBFC. However, an existing NBFC is not entitled to operate as an NBFC P2P.

Source: nbfclicenseindia.com, rbi.org.in

RBI regulations

- RBI defines **NBFC P2P** as a non – banking institution involved in the business of a peer – to – peer lending platform.
- The Reserve Bank of India (RBI) has regulated P2P lending to **protect the interest of lenders and borrowers**.
- As per its provisions, an NBFC-P2P is to become a member of **all CICs (Credit Information Companies)** and submit the data at regular intervals. So that all payments can be monitored and recorded.

Presently, there are 4 CICs in India —

1. Credit Information Bureau (India) Limited (CIBIL),
2. Equifax Credit Information Services Private Limited (ECIS),
3. Experian Credit Information Company of India Private Limited, and
4. CRIF High Mark Credit Information Services Private Limited.

Source: nbfclicenseindia.com, rbi.org.in

Role of credit information companies (CICs)

1. NBFC P2P has to become a **member of ALL CICs** and submit all previous data.
2. The **credit information of the borrower should be maintained and updated regularly**, either monthly or at shorter intervals, as the mutual understanding between NBFC P2P and CIC.

- Appropriate measures must be taken to ensure that the credit information of borrowers is **up-to-date, accurate, and complete**.
- Necessary declarations should be placed in the agreements with the participants that they have consented to provide the required credit information.

Source: nbfclicenseindia.com, rbi.org.in

Compulsory disclosures

Borrowers

1. Personal Identity
2. Required amount
3. Interest rate sought
4. Credit score as arrived by the P2P platform
5. Terms & Conditions of the loan
6. Return
7. Fees & Taxes

Lenders

1. Proposed Amount
2. Interest rate offered

Personal identity and contact details of the lender are not to be disclosed.

On Website

1. Method of credit scoring and factors considered.
2. Usage and protection of data.
3. Mechanism of grievance redressal.
4. Portfolio performance including the proportion of non-performing assets.
5. Broad business model.

Source: nbfclicenseindia.com, rbi.org.in

Prudential requirements

- At any specific point in time, a lender is not allowed to invest more than **INR 50 lakhs** across platform.
- A lender is allowed to invest only up to a maximum of **INR 50,000** for one borrower.
- The total loan amount taken by the borrower at a certain point in time **s**hould not be more than **INR 10 lakhs.**
- NBFC-P2P is to maintain a **leverage Ratio** of not more than **2**.(Outside Liabilities /Owned Funds)
- The company is responsible to **conduct due diligence** on all parties.
- The maturity duration of the loans should not be more than **36 months**.

Source: nbfclicenseindia.com, rbi.org.in

Operational requirements

- NBFC P2P must have a **Board approved policy** in place –
  - Setting out the e**ligibility criteria** for participants.
  - Determining the **charges** on the services provided by it.
  - Setting out the **rules** for matching lenders with borrowers equitably and impartially.
- No amount shall be transferred unless the individual lender/s have approved the individual recipient/s of the loan and all concerned parties have signed the **loan contract**.
- **Cash transactions are strictly forbidden**. All fund transfers shall be through and from bank accounts.

Source: nbfclicenseindia.com, rbi.org.in

Reporting requirements

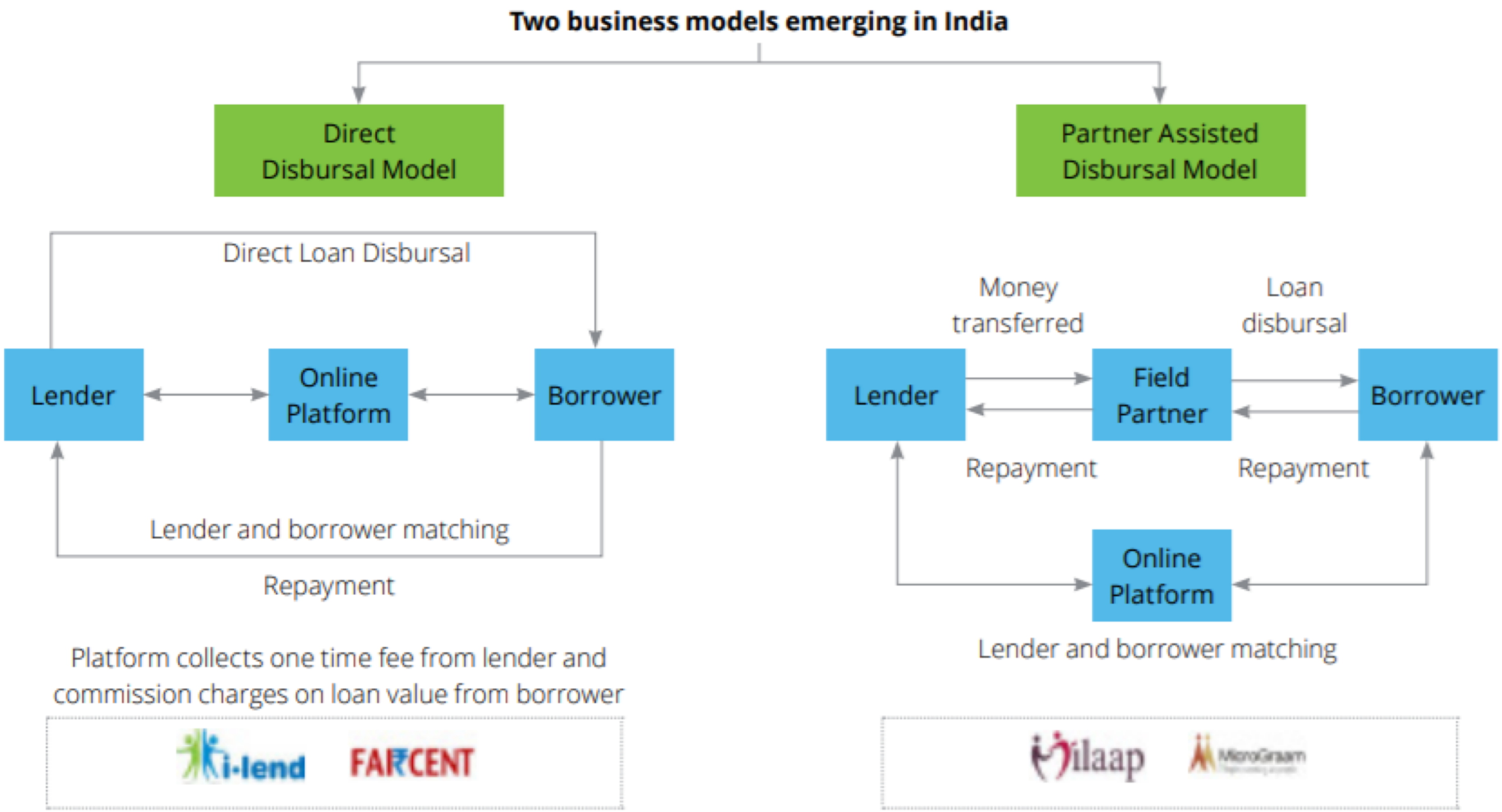
As per the NBFC Act, the P2P platform must submit a quarterly statement to RBI within 15 days after the end of such a quarter. The statement must contain –

- Number and amount of loans disbursed during the quarter, closed during the quarter, outstanding at the beginning and the end of the quarter along with the number of lenders and borrowers at the end of such quarter.
- The amount held in both Escrow Accounts, with separate details of the amount received from lenders and borrowers.
- The number of complaints received. Bifurcated as received from lenders and borrowers pending at the beginning and end of the quarter and disposed-off during this quarter.

Source: nbfclicenseindia.com, rbi.org.in

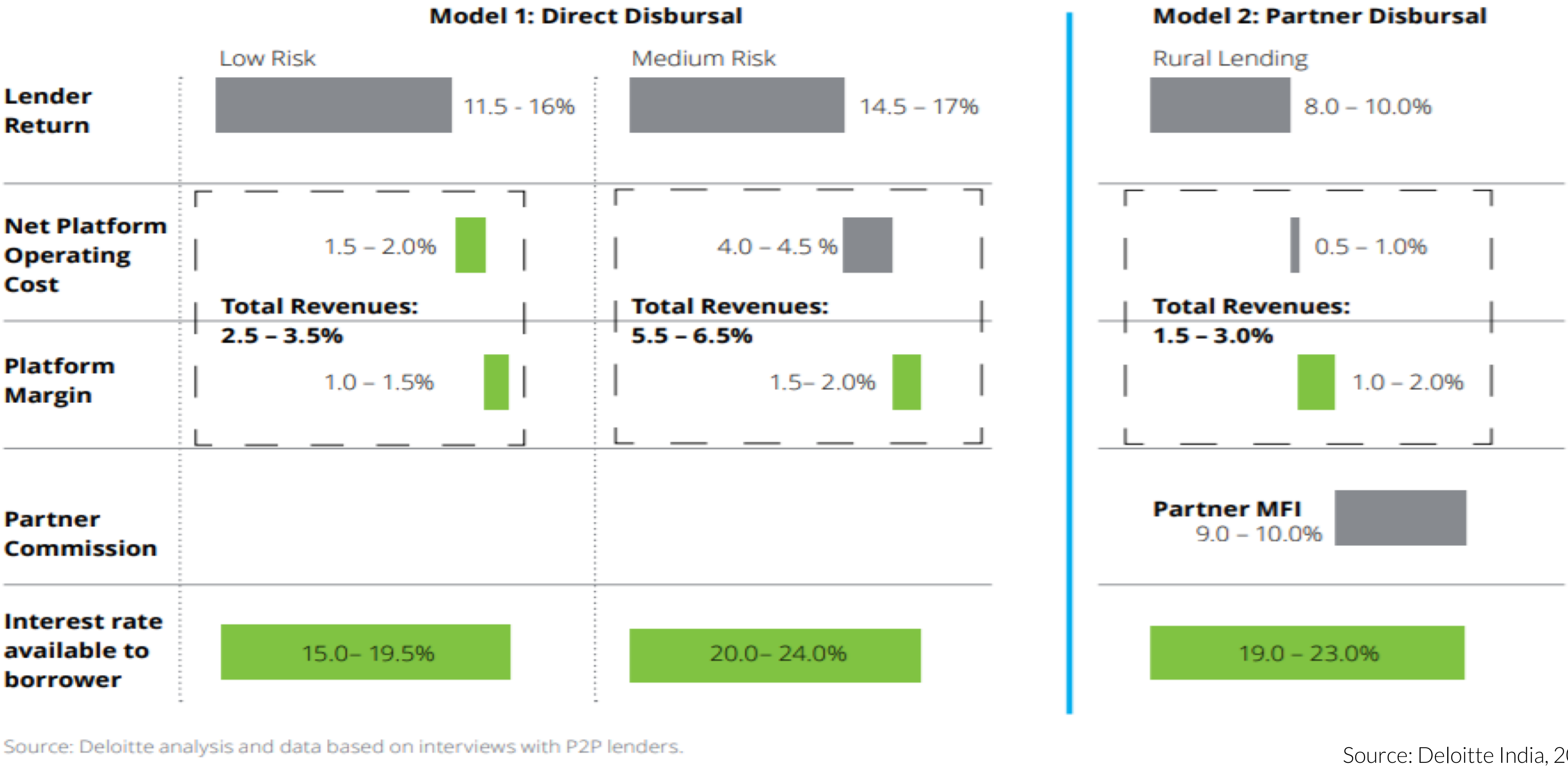
Business models

P2P operating models – direct and partnerships



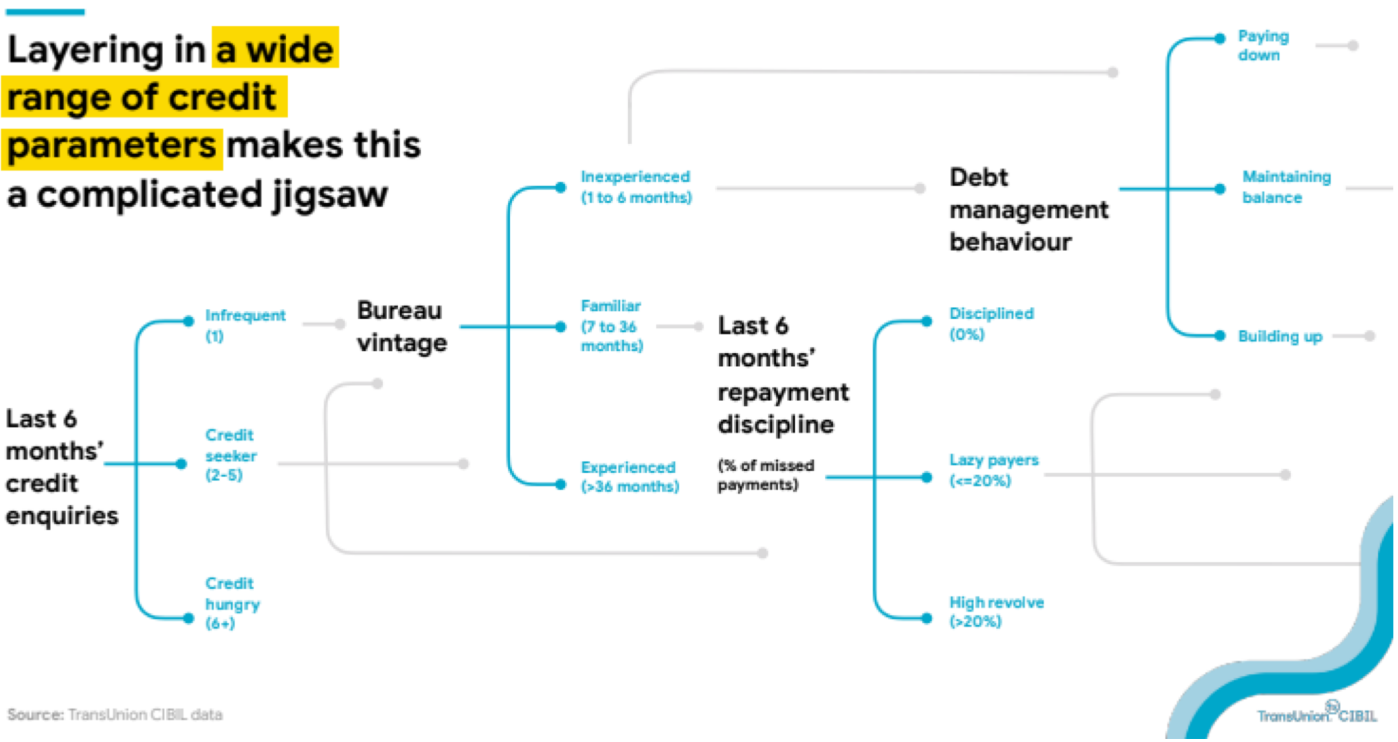
Source: Deloitte India, 2017

P2P operating models – partners help in rural



Source: Deloitte India, 2017

Apart from business models, lenders are using range of credit parameters



Source – Transunion CIBIL/Google

Risks

- Poor executed business model of P2P lending platform can **lead to bankruptcy.**
- Absence of a trust account can lead to **misappropriation of funds** from platform firm.
- Possibility of **data leakage** if data privacy is breached through platform's website
- If AML and KYC are breached, the platform firms could be used to **money launder and fund illegal businesses.**
- Absence of adequate recovery and resolution process **(RRP)** could lead to lender's money at stake.
- Absence of robust back to end IT framework could result in **errors and breaches of RBI guidelines.**
- Lack of cyber security in the platform could lead to hackers accessing confidential data which in turn can be **siphoned for money**.

Source: pwc.org.in

Future scope of P2P

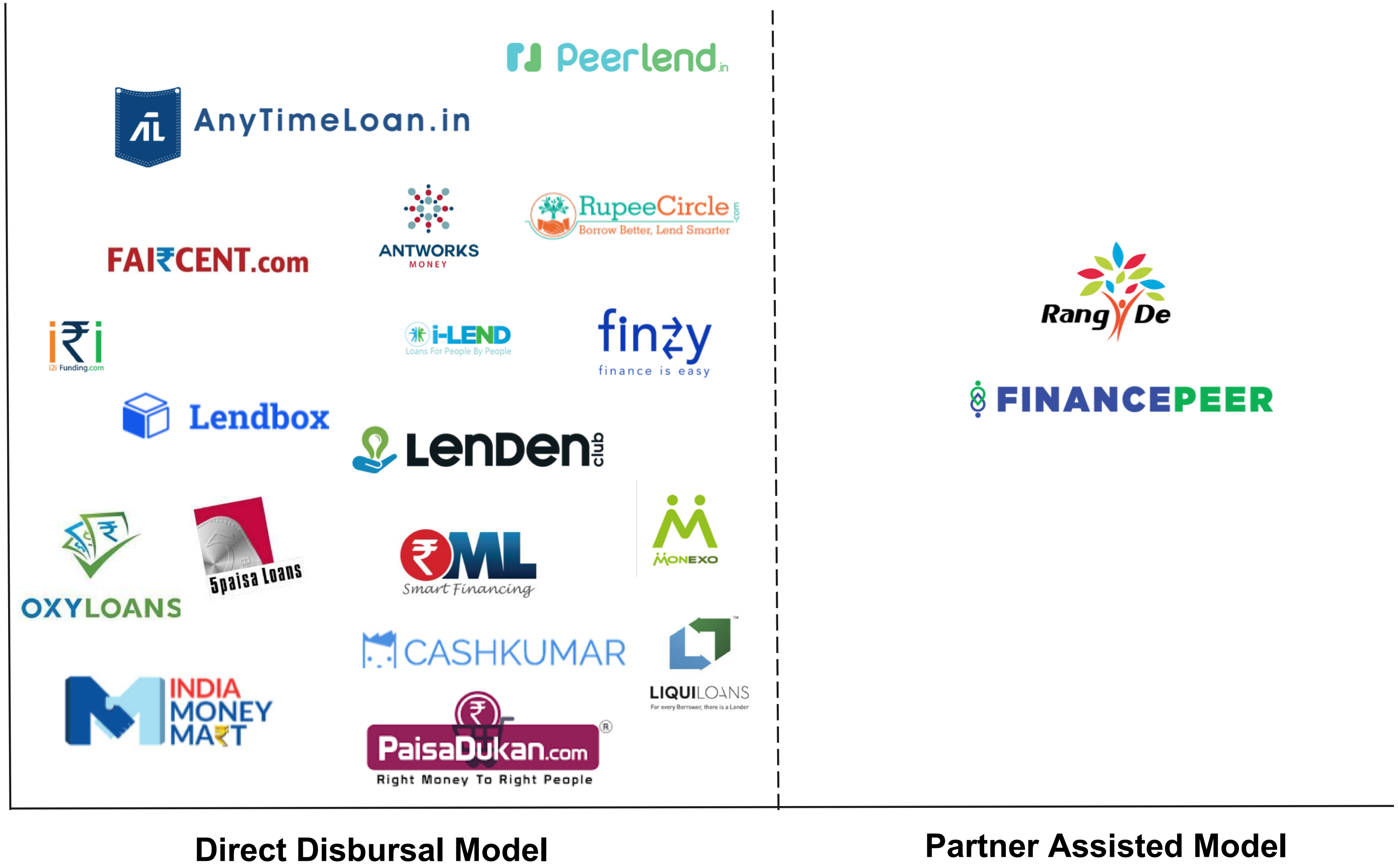
Above mentioned RBI regulations are expected to impact the P2P lending space as follows:

- The market for peer-to-peer lending in India is **expected to reach $10.5 billion by 2026**, rising at a CAGR of 21.6% in the forecast period of 2021-2026. (IndustryARC)
- A major chunk of the **currently underserved market will be covered** under the financial umbrella.
- People that are currently opting for banks to fulfil their financial needs, would migrate to P2P lending platforms as the **P2P loan application processes are very efficient.** (like in US & UK)
- For the lenders on these P2P platforms, the **returns are very lucrative** which will continue to be the case along with **more checks and processes introduced** by P2P platforms in order to keep NPAs in check.

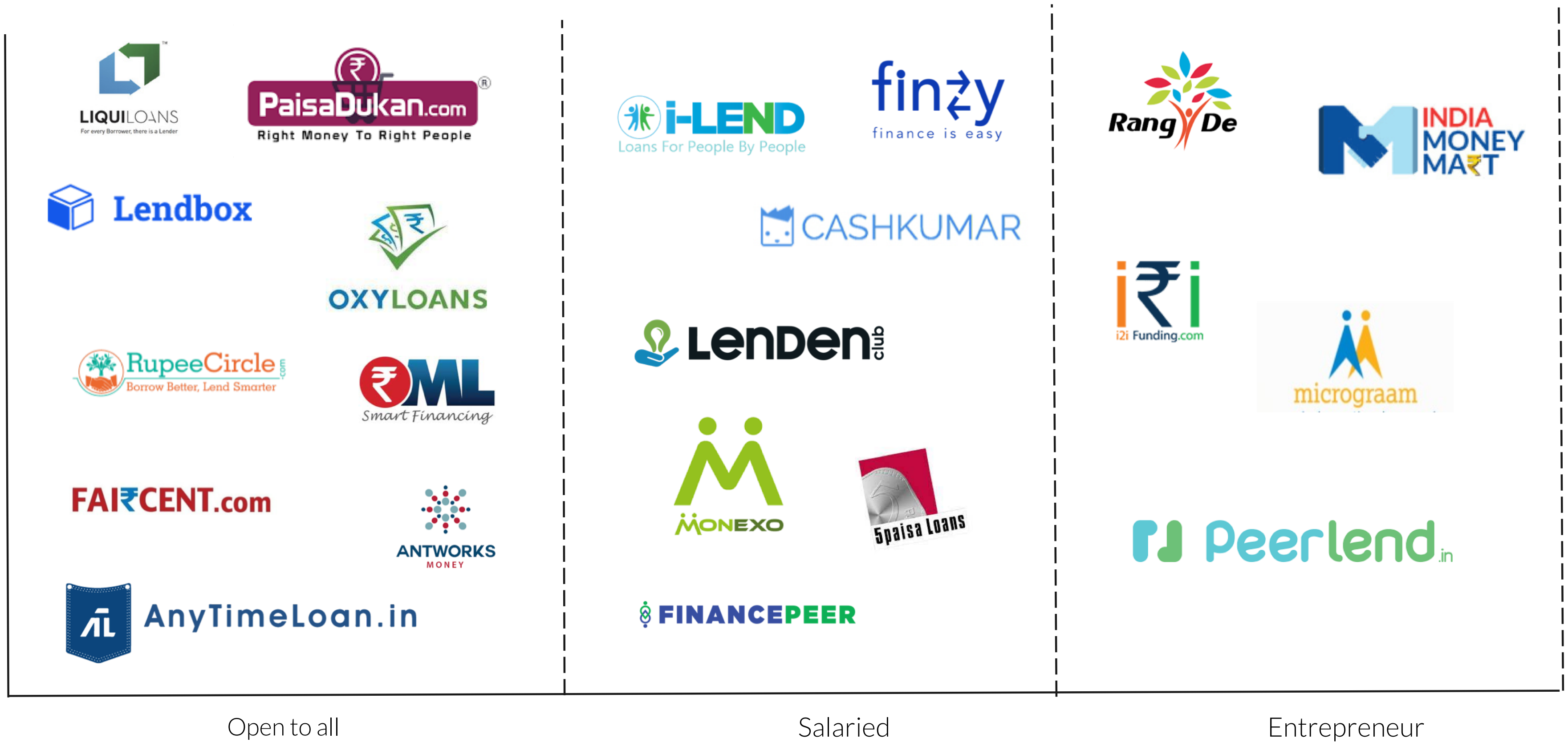
Source: nbfclicenseindia.com

Indian landscape

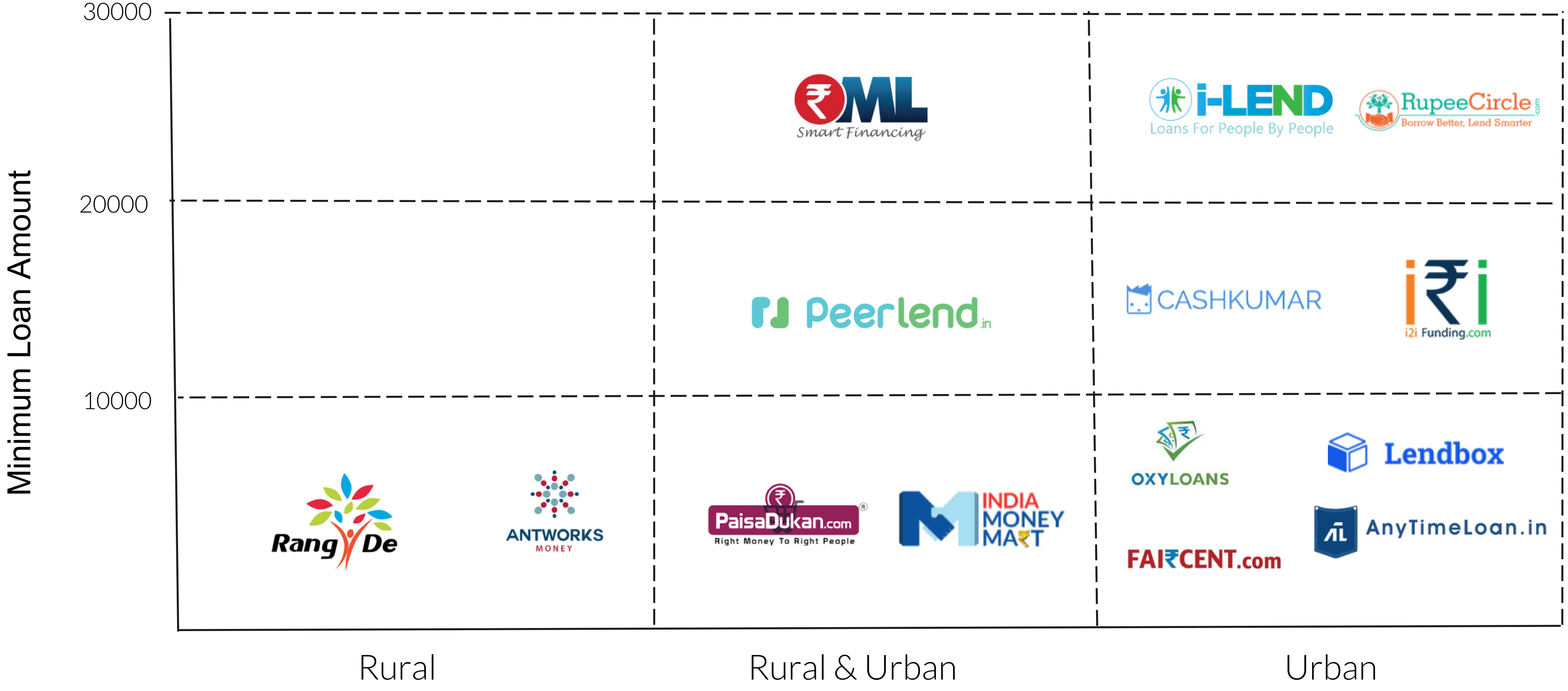
Business model



Customer segmentation



Minimum loan amount vs target segment for entrepreneurs

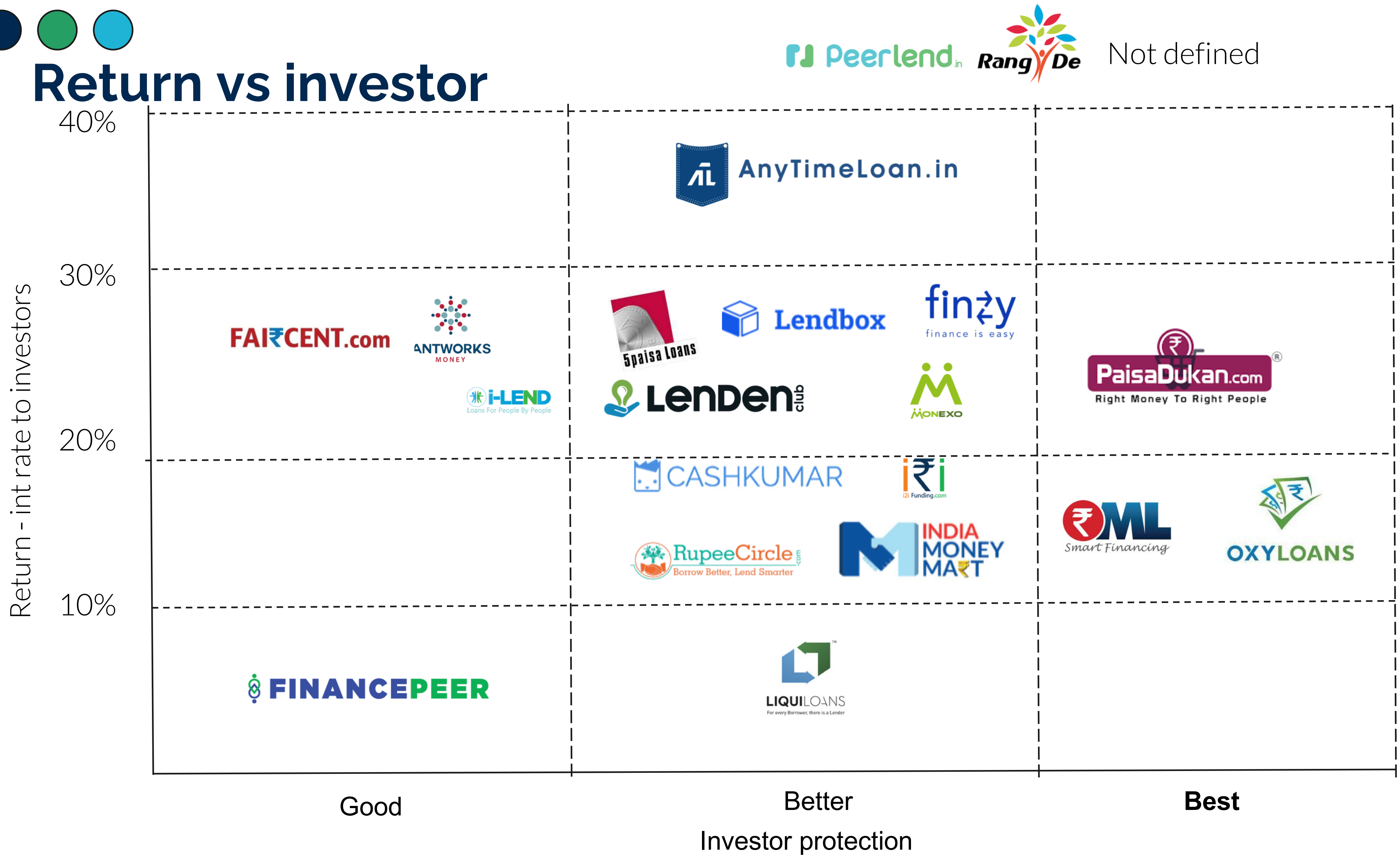


Return vs investor

We decided to grade platforms on ‘investor protection’ during non-repayments, on the basis of -

- Good - provides legal assistance only
- Better - provides legal assistance and aid from debt collection agency
- Best - asks for other securities from borrowers (ie; PDC, Insurance, loan buybacks)

Return vs investor



Conclusions

Indian landscape

Based on a high level study of 20-odd licensed P2P platforms in India, we note -

- The average loan tenure is between **3 - 36 months**.
- Some of the lowest interest rates paid by borrower is offered by Rang de at **0-8%pa** that targets rural entrepreneurs to provide loans. The highest interest rate given to lender is offered by PeerLend and OxyLoans at **14-36%pa**, that caters to both self employed and salaried individuals to provide loans.
- The platform **revenue** is commission-based or membership-based, and depends on the percentage or fixed amount levied as **registration/listing fees, processing fees and repayment collected (EMI)**.
- As part of credit assessment each P2P platform have their own proprietary credit algorithms which also looks into CIBIL score, repayment history, cash flow, document verification, ITR filing, physical verification, ability to pay and intent to pay.
- At the time of non-payment, the borrower is entitled to pay back the loan amount and the **p2p platform is not the sole responsible entity for non-repayment.** The platform will provide assistance through providing legal service or aid from third party.

P2P lending an alternative asset

- Peer-to-peer (P2P) lending gives investors a chance to earn competitive annual returns by investing in unsecured personal loans to other consumers through various p2p platforms.

- P2P lending can be considered as part of an allocation to high risk/high return alternative investments, which can provide diversification benefits.

- Investing through a P2P platform can work well if risks are managed -
  - Investments are not liquid (one must wait for the borrower to repay the loan before the entire principal amount is returned).
  - A future economic recession could lead to widespread loan defaults leading to diminished returns and/or a loss of principal.

Picking P2P platforms for investment

Investors may want to -

- Favour loans to borrowers with history of timely repayment
- Look into the non-performing asset ratio of platforms (if available)
- Favour loans where the borrower has greater employment stability
- Review and opt for platforms that offer upstanding investor protection from borrowers (e.g. platforms asking for post dated cheques, insurance & loan buybacks from borrowers)
- Diversified across several platforms and loans

Disclaimer

- This study is subject to the accuracy of the data sourced from third-party sites and tools.
- This is an internship project designed for freshers to learn, discuss and debate investment observations. It is possible to have mistakes.
- Past performance does not necessarily indicate future results.
- Mutual funds are subject to markets risks.
- This study is not an invitation to invest in equity markets, mutual funds or p2p platforms.

- Prepared by – Anjana Nambiar and Dheeraj Dhole during an internship in November - December 2021.