Peer to Peer Lending Platforms in India: Regulations and Response

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The paper examines Peer to Peer (P2P) lending in India, its growth and the way lending platforms have fared following the introduction of regulations by Reserve Bank of India. The paper analyses the transaction practices of these lending platforms, their margins and makes a comparison with the micro finance model of lending.

The paper observes that there was an increase in the number of platform-based lending entities from 2010 to 2017. Subsequently, the growth of peer to peer lending platforms has been subdued following regulations introduced by the RBI. The paper finds that their operations belies their claim of being transparent. The desired lower cost to borrowers is yet to be witnessed in this novel segment of lending.

Keywords: P2P, Peer to Peer Lending Platforms, RBI Regulations, Fin-tech, Financial Inclusion

JEL Classification: G29, G28, G38, O14

In the fast-changing landscape of Fin-tech¹, Peer to Peer (P2P) lending platforms has become a subject of interest because of the unique characteristics of this method of intermediation. P2P lending is a form of crowd funding where loans are sought through the medium of platforms from people willing to lend. P2P lending platforms act as a market place for borrowers and lenders in the internet world. This novel way of lending caters to individuals and petty businesses by finding lenders within a time frame, without the need to provide collateral for obtaining loans. Self-employed persons, contract employees, persons with no regular jobs and borrowers with some black marks in their credit history may well be able to find lenders in the peer to peer lending

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1. FinTech stands for financial technology and describes technologically enabled financial innovations. From ‘start-ups’ to ‘big-techs’ to established financial institutions, all the key players are harnessing this technological edge along the financial services' value chain to provide agile, efficient and differentiated experiences to the end-user(Das, 2019a).
space. Most of these loan seekers find it difficult to get loans from banks. These platforms also nudge consumers in the personal loan segment and small businesses to borrow loans through them.

Globally, P2P lending has grown with the largest market being in China, followed by USA and UK. In China, the trading volume reached USD 67 billion in 2015, which was about four times bigger than that of the US and ten times that of the UK. In China there was a total of 2388 P2P platforms in 2017. The platforms are mainly operated by small and medium-sized firms in China. In contrast, the online lending markets in USA and UK are dominated by a few firms. In the US, Lending Club and Prosper together have 98 per cent of the online lending market share, and similarly in the UK up to 88.5 per cent of the British online lending market is in the hands of Zopa and Fundingcircle. In China, online lending primarily provides credit to start-ups and SMEs with bank credit directed towards state-owned enterprises. In comparison, the online lending market in the US serves the needs of personal consumption, such as credit card and housing mortgage payments. In the United Kingdom, consumer lending accounts for a greater proportion of the online lending market than business lending (Huang, 2018). In China, following the swindling of investors by a few platforms, registration requirements, custodian requirements, information disclosure requirements and lending limits were introduced in 2017 (Huang, 2018). Online lending has been considered similar to the banking business in China and falls within the jurisdiction of the China Banking and Insurance Regulatory Commission (CBIRC). In the US, there are two levels of regulation; federal regulation through the Securities and Exchange Commission (SEC) and state-level regulation. In the UK, the Financial Control Authority (FCA) regulates loan based crowd funding.

Crowdfunding platforms including peer to peer platforms in India emerged around 2010. The number of P2P lending platforms grew without much regulatory oversight, encouraged also, by the general growth of the digital economy. In 2017, the number of online platforms was estimated to be close to 50 and the outstanding loans sanctioned through P2P platforms was estimated to have reached 60 crore rupees (Care Ratings, 2017). The central bank, Reserve Bank of India (RBI) was designated as the regulator and has approved the registration of only 11 entities to operate peer to peer lending platforms. There is an expectation among policymakers that this mode of lending will further the cause of financial inclusion which is not the anticipation in other countries. The growth trajectory in India has therefore, been somewhat different from that seen in other countries.

This paper analyses the process of P2P lending in India. It examines the growth of the sector to see whether the claims of the peer to peer lending platforms in

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2. Four kinds of crowdfunding models exist - reward based, peer to peer (debt), equity and donation based.
terms of their assertions of low-interest rates and transparency have been actually realized.

The examination can provide insights useful to regulators, financial sector intermediaries, academics and the general public.

The Policy Environment

The Government of India has, in recent years, attempted to promote and accelerate the pace of growth of digital payments. As a matter of fact, one of the justifications given (albeit ex-post), for the demonetization of currency notes with denominations of Rs 500 and Rs 1000 in November, 2016 was to give a big boost to the digitalization of payments to make India a less-cash economy (GOI, 2017). The Government of India's campaign for Digital India along with easy availability of smart phones and affordable mobile data packages enabled the growth of Fintech in India.

When peer to peer lending began to grow in India, there was some ambivalence as to whether the business model would fall under the jurisdiction of Securities Exchange Board of India (SEBI) or of the Reserve Bank of India (RBI). The consultation paper on crowd funding in India issued by SEBI in 2014, placed the subject of peer to peer lending in the domain of RBI (SEBI, 2014: p.30). RBI issued a consultation paper on P2P lending in April 2016 and invited comments from the public. Peer to Peer lending has been defined in the consultation paper as the use of an online platform that matches lenders with borrowers in order to provide unsecured loans. The paper noted that P2P lending promotes alternative forms of finance, where formal finance is unable to reach, it also has the potential to soften the lending rates as they have lower operational costs and enhance competition with the traditional lending channels. The consultation paper posed several questions and asked for comments on the nature of regulation required (RBI, 2016a). RBI issued a Gazette Notification and followed it up with directions in 2017(RBI, 2017a; RBI, 2017b). The RBI in the Gazette notification declared that peer to peer platforms fall under the jurisdiction of RBI and that the platforms would need to be Non-Banking Financial Companies (NBFCs). The notification defined the business of a peer to peer lending platform to mean the business of providing under a contract, the service of loan facilitation, via online medium or otherwise, to the participants who have entered into an arrangement with that platform to lend on it or to avail of loan facilitation services provided by it.

Subsequently, the RBI brought out detailed directions in October 2017. The directions of RBI require companies carrying out the business of peer to peer lending platform to be incorporated in India. The directions cover registration requirements as Non-Banking Financial Companies and the manner peer to peer lending platforms need to function. The RBI has prescribed minimum

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3. "Leverage Ratio" means the Total Outside Liabilities divided by Owned Funds, of the NBFC-P2P.
capital requirements, limits on leverage and that the promoters and directors need to be fit and proper. A minimum capital requirement of Rs 20 million was prescribed. NBFC-P2Ps are required to maintain a leverage ratio of not exceeding 2. The aggregate loans taken by a borrower at any point of time, from various NBFC-P2Ps, has been subjected to a cap of one million rupees. The exposure of a single lender to the same borrower, across all NBFC-P2Ps, has been limited to 50,000 rupees. The aggregate exposure cap of a lender to all borrowers at any point of time, across all NBFC-P2Ps, has been prescribed at one million rupees. The maximum tenure of loans has been fixed at 36 months (RBI, 2017b).

The fund transfer on the peer to peer lending platform from the lender to the borrower and vice versa is required to take place through escrow accounts which would be operated by a trustee. Two escrow accounts, one for funds received from lenders and pending disbursal, and the other for collections from borrowers, are to be maintained. The trustee has to be mandatorily promoted by the bank maintaining the escrow accounts. The funds have to necessarily move from the lenders' bank account to the borrower's bank account so as to prevent the possibility of money laundering. Besides, cash transactions have been prohibited. RBI has specified P2P platforms need to have alternative arrangements in place to ensure that loan agreements on the platform would need to be managed and administered by other third-party servicers in accordance with the contract terms, if the NBFC-P2P ceases to carry on the P2P activity.

The directions of RBI issued in October 2017 have been updated twice since then. In the first instance, they were updated in November 2017 with the requirement for NBFCs to put in place a process for the management of risks and to follow a code of conduct in the outsourcing of financial services by them. Later, in February 2018, the platforms were brought under the purview of the Ombudsman scheme for Non-Banking Financial Companies which was applied to other NBFCs as well. Besides, the direction of RBI on the requirement on data localization for digital payments which was introduced for peer to peer lending platforms was later extended to cover other entities also (RBI, 2018c).

RBI has prescribed certain Do's and Don'ts for conducting the business of P2P platforms. Do's include:-

(i) ensure adherence to legal requirements applicable to participants as prescribed under relevant laws;

(ii) store and process all data relating to its activities and participants on hardware located within India;

(iii) undertake due diligence of the participants;
undertake credit assessment and risk profiling of borrowers and disclose the same to prospective lenders;

(v) acquire prior and explicit consent of participants to access credit information;

(vi) undertake documentation of loan agreements and other related documents;

(vii) provide assistance in disbursement and repayments of loan amount;

(viii) provide services for recovery of loans originated on the platform;

(ix) submission of data to credit information companies.

The restrictions placed on peer-to-peer lending portals include:

(i) A NBFC-P2P platform cannot lend on its own;

(ii) cannot provide or arrange any credit enhancement or a credit guarantee;

(iii) cannot facilitate or permit any secured lending linked to its platform; i.e. only clean loans will be permitted;

(iv) cannot hold, on its own balance sheet, funds received from lenders for lending, or funds received from borrowers for servicing loans. It cannot cross-sell any product except for loan specific insurance products;

(v) cannot permit international flow of funds.

RBI has also issued clarifications in the form of frequently asked questions. The clarifications inform that both lender and borrower can be natural persons or artificial bodies. Apart from banks, NBFCs or All India Financial Institutions (AIFIs), all the other retail lenders who lend through platforms will have to register separately as NBFC-P2Ps (RBI, 2018a).

**Implications of Regulations**

With the introduction of regulations, participants and platforms have acquired legal standing. The RBI regulations imply that all lenders who make use of platforms to lend to retail customers will need to be registered as NBFC-P2Ps. This may also impact lenders in the micro finance category who make use of platforms to lend to retail customers. They will now need to register as NBFC-P2Ps.

The exposure of a lender to a single borrower has been limited to Rs. 50,000. Hence a borrower who requires Rs. 1 million, which is the maximum amount permissible, would need to borrow from at least 20 lenders and may be required to sign several contracts to reach the target amount which is cumbersome.
Some readjustment for individual lenders within the ceiling of the loan may be called for.

NBFCs have been allowed to access both equity and debt funds. Therefore, the platforms themselves can be a class of investment for the rich and wealthy. The ticket size and conditions imposed by RBI make platforms relatively unattractive for persons with large surplus funds to lend through them.

RBI directions forbid the international transfer of funds on peer to peer platforms. However, fintech companies have been classified under "other financial services" and are been permitted 100 per cent Foreign Direct Investment (FDI) through the automatic route by the Government of India and the Reserve Bank of India (GOI 2016, RBI 2016c). This implies that while transactions take place within India, the company itself may be fully foreign-owned. At present, some of the platforms have received foreign funding as part of their equity. This can in future has implications in terms of repatriation of profits and royalty.

**Comparison with MFI**

The loans taken through platforms have certain characteristics which are similar to loans arranged by microfinance institutions (MFIs). Some scholars have considered online P2P lending as a digitized and somewhat modified version of traditional microfinance programs. Like peer-to-peer lending, microfinance is typically collateral-free and carry with them similar information asymmetry problems (Lin, Viswanathan and Prabhala, 2009). Lin *et al.* suggest that P2P markets should incorporate functionalities that promote interaction among members which help to broker better deals. This suggestion has been made in the context of the USA, and it may not be workable in the Indian situation where the borrower and lender belong to different economic and social strata. Another similarity of both methods is that the loan amounts are higher than the disbursed amounts. The amount provided to the borrower is less than the borrowed amount at the commencement of the loan itself. The principal and interest calculations for repayment are made on the loan amount and not on the disbursed amount.

The drafting of directives on peer to peer lending by RBI was carried out with hindsight of the bitter experience from the debt crisis emanating from Micro Finance Institutions (MFIs) loans in Andhra Pradesh. In Andhra Pradesh, borrowing from MFIs at high costs pushed many borrowers into a debt trap leading to a law and order problem in 2010. Initially, the state government and later the RBI intervened to put in place some controls on MFI lending. The RBI set up the Malegam Committee and based on their recommendation brought in rules governing MFI lending. Limits on loan size, tenure, interest margins and overall indebtedness were set (Gandhi, 2016). With hindsight from this experience, RBI has fixed limits on the size of loan and tenure in the case of
P2P loans at the initial stage itself so to obviate some of the problems encountered with MFI loans.

The Reserve Bank has treated P2P lending through platforms as a means which facilitates direct interaction between small lenders and small borrowers and hence a method which could further financial inclusion (Gandhi, 2016). The amount fixed in the case of P2P platforms has been more liberal than for NBFC-MFI. RBI has placed a ceiling on the amount of loan at 100,000 rupees for NBFC-MFIs\(^4\) as compared to 1 million rupees for peer to peer platforms which is ten times higher. The loan limit at Rs. 1 million for peer to peer platforms is set at par with loans extended to small and micro enterprises without collateral. Such SME loans are included by RBI in the computation of financial inclusion\(^5\).

The limits for P2P platforms have been set at a slightly more liberal level than for MFI lending. In the case of peer to peer platforms, the borrower cannot take loans exceeding one million rupees from all platforms taken together. For MFI, in comparison the borrower cannot have an overall debt exceeding Rs. 1,00,000 excluding the loans taken for medical and educational purposes for rural areas. The maximum tenure of the loan is 36 months in the case of P2P platforms and 24 months in case of MFIs.

Both MFIs and peer to peer lending platforms cater to providing credit to groups who generally require the loan urgently and do not have much choice. The prospective borrower usually has an inelastic demand curve for the loan. Peer to peer lending platforms arranges to lend for purposes for which mainstream players may be reluctant to lend. The requirements may be medical emergency, hospitalization, tuition fees of private coaching classes, or roll over of debt. Both modes of lending try and treat each customer differently and attempt to extract maximum consumer surplus from each borrower individually.

RBI has notified similar provisions for peer to peer lending platforms applicable to MFI loans for dealing with recovery procedures. Peer to peer lending platforms has been forbidden from resorting to harassment such as persistently bothering the borrowers at odd hours and using coercion for recovery of loans.

MFIs directly lends to borrowers and can reschedule loans. There is little option for rescheduling loans arranged by platforms, because of the nature of the contract. The lending platform can be used for personal loans where the borrower feels certain of getting funds before the payment of an instalment is due to tide over a temporary financial problem. This model is however, not

\(^4\) Education and medical expenses are excluded in the calculation of debt.

\(^5\) The upper limit of Rs 10 lakhs is similar to the ceiling placed for lending by commercial banks to micro and small enterprises. In the case of commercial banks, RBI has mandated that they should not accept collateral security in the case of loans up to Rs. 10 lakh extended to units in the micro and small enterprises (RBI, 2013).
suited for project loans which are long term as the task of appraisal and evaluation is beyond the capability of platforms. Here there is little option for rescheduling loans when faced with an uncertain environment.

**Growth of Peer to Peer Lending**
The policy environment and regulatory framework have an important role in determining growth and in shaping the relative size of segments within the financial sector. They influence the behaviour of participants also. Prior to the introduction of regulations, there had been a spurt in the growth of peer to peer lending platforms and there were reported to have been 50 platforms operating in the country (Care, 2017). The scenario has drastically changed since then. Following the regulations introduced in 2017, this category of lending entities has shrunk in number. By the end of March 2019, which marked the completion of one and half years of the period of regulatory oversight, there were only a modest number of 11 NBFCs who were registered with RBI for undertaking P2P lending operations. In comparison, there were 9,353 non-deposit taking on systematically important NBFCs and 95 NBFC-MFIs registered with RBI in the country.

**Transaction Practices of P2P**
An examination of the loans advertised and listed on the websites of peer to peer lending platforms show that the loans are predominantly personal loans. P2P lending platforms generally require borrowers to make over post-dated cheques to them so that they get a legal standing in the loan. In case of default in payment, the platform would attempt to encash the cheque in their possession and initiate action for recovery.

RBI regulations require platforms to display the rate of interest in annualized percentage terms. The following table shows the interest rates and method of appraisal of loans followed by the peer to peer platforms (Table 1).
Table 1

Indicative Interest Rates Charged To Borrowers & Scoring Used

<table>
<thead>
<tr>
<th>Platform</th>
<th>Office</th>
<th>Interest Rate per cent</th>
<th>Score Type</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cashkumar.com</td>
<td>Bengaluru</td>
<td>18 to 30.0</td>
<td>grades borrowers according to their risk bucket</td>
</tr>
<tr>
<td>Monexo</td>
<td>Chennai</td>
<td>12 to 30.0</td>
<td>Monexo proprietary screening M1 to M8</td>
</tr>
<tr>
<td>Faircent</td>
<td>New Delhi</td>
<td>6 to 36.0</td>
<td>Faircent rule engine, an in-house algorithm; parameters: stability, ability, intention, habit</td>
</tr>
<tr>
<td>Peerlend</td>
<td>Hyderabad</td>
<td>14 to 36</td>
<td>rate range for lenders and borrowers to negotiate</td>
</tr>
<tr>
<td>Anytimeloan.in</td>
<td>Hyderabad</td>
<td>36.0</td>
<td>proprietary algorithm with robot using artificial intelligence and data science</td>
</tr>
<tr>
<td>itoi</td>
<td>Lucknow</td>
<td>23.35</td>
<td>A to F, CIBIL score with 40 parameters</td>
</tr>
<tr>
<td>om lp2p.com</td>
<td>Mumbai</td>
<td>10.99 to 36.0</td>
<td>CrIF score &amp; 7 risk grades for personal (P1 to P7) and business (B1 to B7) based on standard appraisal</td>
</tr>
<tr>
<td>Finzy.com</td>
<td>Mumbai</td>
<td>10.99 to 27.99</td>
<td>Finzy credit algorithm; 130 parameters, Equifax report for history</td>
</tr>
<tr>
<td>Paisadukan.com</td>
<td>Mumbai</td>
<td>12 to 24.0</td>
<td>proprietary credit score salary pan card aadhar card/capacity capital character</td>
</tr>
<tr>
<td>Lendenclub.com</td>
<td>Mumbai</td>
<td>12 to 28.0</td>
<td>Lenden credit score: 100 data points, 5 step screening mechanism where borrower’s personal, professional and financial information</td>
</tr>
<tr>
<td>LiquiLoans</td>
<td>Mumbai</td>
<td>12 to 25.0</td>
<td>proprietary credit score</td>
</tr>
</tbody>
</table>

Source: Data obtained from respective websites mentioned above as on 25/4/2019

The Table indicates the range in interest rates from 6 to 36 per cent. The interest rate charged for subprime borrowers at the upper end in the case of platforms is higher than that charged by MFIs and about thrice the rate charged by banks. The RBI has notified the formula for MFIs to fix interest rates and it has hovered in the vicinity of 26 per cent. The softening of interest rates on lending platforms expected by RBI has not taken place so far.

The borrower is slotted into a risk category with a credit score calculated by the platform for listing the loan. To calculate the score, the platform collects various data points and personal particulars. The personal particulars go much beyond the information that banks collect for KYC (Know Your Customer).

P2P lending platforms slot the clients into risk categories through algorithms prior to making their profiles available on platforms. The score is computed by applying an algorithm but this does not necessarily make the number

6. The average base rate of the five largest commercial banks by assets multiplied by 2.75 is the ceiling and is advised by the Reserve Bank on quarterly basis (RBI, 2015).
generated scientific and beyond reproach. The lending platforms claim to be transparent in their working. Their operations, however, belie the claim.

The existing directions of RBI require the platforms to disclose an overview of credit assessment, score methodology and factors considered. In view of the need to understand the score, the RBI should make it necessary to share the detailed calculation on the score as well as various charges to borrowers for clarity.

The nature and application of algorithm pricing have been a matter of debate and discussion in other sectors as well. The pricing of fares by cab aggregators and airline ticket pricing have been looked by Competition Commission of India for the possibility of unfair pricing. The Commission has observed that pricing algorithms allow room for coordination among competitors (CCI, 2017). In the case of peer to peer platforms, the behaviour of platforms in the market players may need to be monitored so as to ensure fair play in the economy.

**Margins of Peer to Peer Platforms**

Banks earn revenue from the spread in interest rate between the borrower loans and lenders deposits. P2P platforms in contrast, charge fees and commissions from both lenders and borrowers. The P2P platforms generally take registration fees for boarding onto the platform from both borrowers and lenders. They also charge a commission on the loan amount from both parties. From borrowers, platforms charge fees for credit scoring and listing. On finding a loan match they charge a commission on the loan amount before allowing for its disbursal. They most often charge for monitoring payments made of the principal and interest amounts. Their earning depends on the loan amount and the number of transactions. The charges levied as given on the websites by platforms are presented in Table 2.
Table 2
Charges Levied for Participating on Platforms

<table>
<thead>
<tr>
<th>Platform</th>
<th>Charges on Lenders *</th>
<th>Charges on Borrowers *</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cashkumar.com</td>
<td>Not given</td>
<td>Not given</td>
</tr>
<tr>
<td>Monexo</td>
<td>2.5 per cent of loan</td>
<td>2 to 4 per cent</td>
</tr>
<tr>
<td>Faircent</td>
<td>1 per cent from individuals</td>
<td>Rs 500 + 3 to 5.5 per cent of loan</td>
</tr>
<tr>
<td></td>
<td>2 per cent from institution of loan</td>
<td></td>
</tr>
<tr>
<td>Peerlend</td>
<td>2 per cent of loan + Rs 1898 CIBIL Report</td>
<td>3.5 per cent of amount + Rs 1898 for CIBIL Report</td>
</tr>
<tr>
<td>Anytimeloan.in</td>
<td>1.5 per cent of loan amount</td>
<td>Rs 800 or 0.1 per cent of loan</td>
</tr>
<tr>
<td>itoi</td>
<td>Not given</td>
<td>Rs 1100</td>
</tr>
<tr>
<td>omlp2p.com</td>
<td>1 per cent of commitment amount</td>
<td>200 + 1 to 10 per cent of amount</td>
</tr>
<tr>
<td>Finzy.com</td>
<td>Small fee on returns</td>
<td>1 to 5 per cent of amount</td>
</tr>
<tr>
<td>Paisadukan.com</td>
<td>Rs 500</td>
<td>Rs 300 + 3 to 5 per cent processing fee + insurance</td>
</tr>
<tr>
<td>Lendencub.com</td>
<td>Rs 500 + 1 to 3 per cent on emi</td>
<td>Not given</td>
</tr>
<tr>
<td>LiquiLoans</td>
<td>Not given</td>
<td>Not given</td>
</tr>
</tbody>
</table>

Note: * Excludes Goods and Services taxes.
Source: Data obtained from respective websites mentioned above as on 25/4/2019.

Table 2 shows that the cost of intermediation is in the vicinity of 10 per cent of the loan amount. The components of cost are not uniform across platforms. RBI has not notified the admissible charges on loans nor issued advisories regarding fees and commission charged by the peer to peer platforms. In comparison, RBI has fixed margin caps as defined by the Malegam Committee for MFI loans. For MFI loans, the margin may not exceed 10 per cent for large MFIs (loans portfolios exceeding Rs.100 crore) and 12 per cent for the others. Processing charges will not be more than 1 per cent of the gross loan amount. There will be only three components in the pricing of the loan viz. the interest charge, the processing charge and the insurance premium (which includes the administrative charges in respect thereof (RBI, 2016). Guidelines on similar pattern for loans arranged by platforms seem to be required.

In terms of financial health, the level of Non-Performing Asset (NPA) has been modest. NPAs for the company Faircent stood at 4.4 per cent and for cashkumar at 3.64 per cent in June 2019. The remaining platforms have not made the data available to enable a comparison.

The number of functioning platforms has come down from 50 to 11 after the introduction of directions by RBI. From this it would appear that the conditions...
placed by RBI have not found favour with potential platform operators. In addition, RBI has also been strict in granting licenses for undertaking this activity.

The platforms have been operating under a regulatory framework for two years. The time framework is too short to evaluate the performance of peer to peer lending objectively. The testimonies and anecdotes given by borrowers and lenders of their experience on websites of platforms present a rosy picture of their experience. These are in the nature of advertisements and, therefore, difficult to accept at face value.

Some of the registered peer to peer NBFCs run similar and other related business in the digital space, and use the experience garnered to offer a bouquet of products to consumers. A few companies operating peer to peer lending platforms also offer to arrange for personal loans from banks and NBFCs. Cashkumar provides assistance in getting personal loans from private sector banks like IndusInd Bank, HDFC, etc., and also NBFCs. Paisadukan.com has an agreement with a company called bookmyparts to help in providing credit to buy machine spare parts for its users. Liquiloans has been promoted by the promoters of the rental platform Rentomojo.

**Peer to Peer as Shadow Banking and Regulation**

The overall size of the shadow banking sector including peer to peer platforms has been growing. The Report of the Working Group on Fintech and Digital Banking was of the view that the risk of contagion may be less in case of the failure of P2P platform than for banks because they do not have the same network of credit interlinkages (RBI, 2017). There are other aspects which need to be considered for stronger regulation of platforms.

The tangible investment required for setting up Fintech platforms is less than for banks as the work is carried out mostly in the digital space through the application use of technology. Peer to peer lending competes with other methods of lending and finance which are governed by rules. To avoid regulatory arbitrage, platforms need to be covered in similar directions. RBI has been cautious and put ceilings on the amount of loans provided by lenders because they are unsecured. The scope for deception in the online space is high and the rules on conduct by platforms are required to reduce the possibility of them operating Ponzi schemes.

An important issue relates to privacy due to the possibility of using personal data for commercial purposes. The particulars of borrowers are required to be sent by platforms to credit information companies. Credit information companies are expected to be the custodians of data by RBI. Rules on data confidentiality, safekeeping and sharing data require to be drafted by RBI. In this context, Report of the Inter-Regulatory Working Group on FinTech and
Digital Banking has also highlighted the requirement for exhaustive stand-alone legislation on data protection in India keeping in mind the innovations in FinTech and risk to personal data which comes to the possession of these entrepreneurs (RBI, 2018b, p 54).

**Peer to Peer, Micro Finance Institutions and Financial Inclusion**

Financial inclusion has conventionally been considered the preserve of institutional lenders like commercial banks, cooperative banks in India. Financial inclusion was stated to be the process of ensuring access to appropriate financial products and services needed by vulnerable groups such as weaker sections and low-income groups at an affordable cost in a fair and transparent manner by mainstream institutional players (Chakrabarty, 2011). The rationale for the Jan Dhan Yojana or National Mission for Financial Inclusion announced by Prime Minister on 28 August 2014 was to ensure affordable access to financial services *viz.* bank accounts, remittance, credit, insurance and pensions. Subsequently, the Committee on medium-term path on financial inclusion set its vision of financial inclusion as ‘convenient’ access to a basket of basic formal financial products and services (Mohanty, 2015). This was reiterated by the Deputy Governor of RBI on financial inclusion as providing access to all sections by mainstream players (Munda, 2016). The emphasis till 2016 was on mainstream players like commercial banks, cooperative banks providing credit to achieve financial inclusion. The underlying understanding was that production sectors need to be supported by institutional lenders.

Since 2016 the definition of priority sector lending has widened to include on-lending to MFIs by commercial banks as part of priority sector lending, if the MFIs, in turn, lends to designated sectors (RBI 2016b). The RBI Governor at the NITI Aayog’s FinTech Conclave, Delhi on March 25, 2019 in his Keynote Address has stated that peer-to-peer lending for which the Reserve Bank has issued Master Direction in October 2017 has the potential to improve access to finance for small and medium enterprises (Das, 2019a). Subsequently at another event, he highlighted that the Reserve Bank is continuously aligning its regulatory and supervisory framework so that the evolution of FinTech can be leveraged to widen and ease the financial access by the excluded population (Das, 2019b). The coverage of private entities like MFIs and to consider peer to peer platforms as possible means to achieve financial inclusion marks a significant change in the outlook of RBI.

**Concluding Observations**

Overall, this paper finds that following the regulations introduced by the RBI, the growth in a number of peer to peer platforms has been subdued with only 11 NBFC – peer to peer lending platforms getting registered. A few of the companies which registered themselves as NBFC-peer to peer lending platforms
are also operating separate platforms as facilitators of loans from banks and NBFCs, indicating thereby that P2P loans are one among the different models of lending services being provided by Fintech Companies.

The costs and margins including interest rates are quite high compared to market rates and interest charged by banks and even by MFIs for some borrowers. When borrowers cannot get loans directly from banks for their stated purpose they turn to peer to peer lending platforms and informal finance to arrange loans for them. Platforms ask for personal history and data to prepare profiles. The RBI as the regulator needs to monitor the kind of information peer to peer lending platforms seek so as to ensure that the data used for profiling borrowers do not end up being used against them including inducing them to over-borrow.

RBI has been veering towards including peer to peer lending platforms and similar entities as modes of lending contributing to financial inclusion. Here it needs to be emphasized that peer to peer lending platforms contribute towards financial inclusion only in a limited sense of providing unsecured loans to those who cannot get it elsewhere. They are not suited to providing developmental and livelihood support due to their inability to appraise projects which is necessary for ensuring sustainable growth.

The emergence of peer to peer lending platforms is a relatively new and interesting development and expectations from technology-driven innovations should be realistic. A careful balance would be needed to ensure that the supervisory and regulatory concerns are addressed even when there may be good reasons for fostering an innovation-friendly environment for Fintechs.

References


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