



STUDENTS' ECONOMIC FORUM

A monthly publication from South Indian Bank

*To kindle interest in economic affairs...
To empower the student community...*

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Theme 295

PEER TO PEER LENDING



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South Indian Bank is a member of BCSBI and is committed to treat customers in a fair, transparent and non-discriminatory manner.

Theme No: 295: PEER TO PEER LENDING

A well informed customer will make the policy makers as well as organization which produce goods and services more responsive to the customer needs. This will also result in healthy competition among organization and improve the quality of goods and services produced. The "SIB Students' Economic forum" is designed to kindle interest in the minds of younger generation. The banking channels mainly cater to the need of organised sector. The informal sector often find it difficult to get funds. The peer to peer lending will act as an effective tool to bridge this gap. This month we will discuss about peer to peer lending.

What is crowd funding?

The crowd funding refers to a method of funding a project or a venture via small amounts of funds. These small amounts of funds are raised from large number of people. A portal will preferably act as a technological platform or as an intermediary for such transaction.

What is peer to peer lending?

It is a form of crowd funding which is used to raise the loans and are paid back with interest. It can be defined as the use of the online platform which matches lenders with borrowers to provide unsecured loans. It works as a marketplace for connecting borrowers and lenders. The borrower either could be an individual or a legal person in need of loan.

What are the major activities of the peer to peer platform?

- The platform provides services of assessing the credit worthiness of the borrower and collecting the loan repayments from the borrower.
- The platform also does the credit scoring of the borrower
- The platform sets the interest rate by mutual agreement between the borrower and lender

What are the revenue earning aspects for the platform?

The borrowers pay an origination fee. This could be either a flat fee or a certain percentage of the loan raised. The lenders will be paying an administration fee and additional fee for the add-on services provided if any.

What is the market size of peer to peer lending (P2P?)

The global size of P2P lending has increased from 2.2 million GBP in 2012 to 4.4 billion GBP in 2015.

What are the various regulatory regimes of peer to peer lending in various countries?

The various regimes of peer to peer lending in some of the countries are listed below

Regulatory regimes	Countries
Unregulated market	China, Ecuador, Egypt, South Korea, Tunisia
Intermediary regulation	Australia, Argentina, Canada (Ontario), New Zealand, United Kingdom
Banking regulation	France, Germany, Italy
US model	USA
Prohibited	Israel, Japan

What is the status of peer to peer lending in India?

There are many online peer to peer lending platforms in India which mainly cater to the micro finance activities and providing credit to small entrepreneurs. Broadly, it is divided into three categories as micro finance, consumer loans and commercial loans. The borrowers often get lower interest rate than the existing money lenders. The lenders will have an higher returns than the traditional investments such as fixed deposits, recurring deposits, cumulative fixed deposits etc.

How is the interest rate charged in peer to peer lending in India?

The interest rate is charged on the following basis

- Flat interest rate
- Dynamic interest rates
- Cost plus model

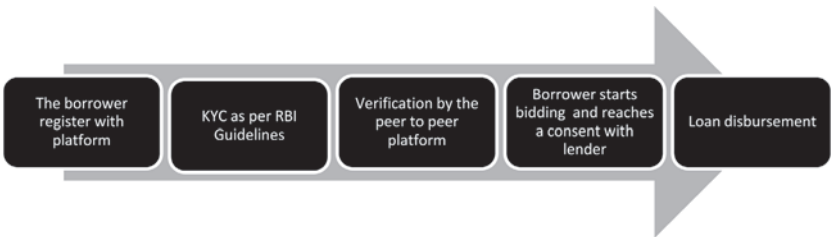
Explain the business model and attributes of peer to peer lending model in India

Nature of the firm	• Mainly technological format registered under companies act
Activity of the platform	• Act as aggregator for lenders and borrowers.
	• Conducts due diligence of the borrower
	• Moderates interaction between borrower and lender

	<ul style="list-style-type: none"> • Facilitate and follow up repayment of loan
Additional Services	<ul style="list-style-type: none"> • Credit assessment, recovery methods
	<ul style="list-style-type: none"> • Reverse auction model (In reverse auction, the sellers compete to obtain business from the buyer and prices will typically decrease as the sellers underbid each other.)

Explain the key processes for loan disbursement in peer to peer lending

The key procedures for a borrower in a peer to peer lending are as follows:



What are the benefits for borrower in peer to peer lending?

The major benefits of peer to peer lending for the borrower are as follows

- Lower interest rates compared to local money lenders
- Simple and fast processing of application
- Low processing fees
- Transparent loan processing

What are the benefits for the lenders in peer to peer lending?

The major benefits of peer to peer lending for the lenders are as follows

- High returns compared to lenders when compared to traditional investments such as fixed deposit, recurring deposit etc.
- Provides diversification of portfolio and mitigating the risk
- Relatively simple product to understand when compared with bonds and stock market
- Get a chance for the lenders to make a social impact
- More option for lenders

What is the significance of peer to peer lending in India?

The peer to peer lending forms an alternative method of financing for the informal sector. This will help more access to finance in a better cost effective manner. The use of technology will reduce the operational cost which could be passed to the end consumer.

What are the effects of unregulation in peer to peer lending?

The lack of regulation in peer to peer lending may result in

- Unhealthy practices in the industry
- Contravention of RBI rules and regulation by the government
- Threat to privacy details of the borrower
- The orderly growth may be at risk

What are the major items in the proposed regulatory framework by RBI for peer to peer lending ?

- The platforms will work with in the permitted activity
- The platforms will have the necessary prudential norms
- Platforms need to have a necessary governance capabilities
- There should be a better risk management framework and business continuity plan
- Transparency in operations and data confidentiality for the borrower
- Better grievance redressal mechanism
- Better reporting system of financial position, loans arrangement, complaints to RBI

What are the permitted activities of peer to peer lending as per the consultation paper of RBI?

- The role of the platform will be only as intermediary and may be prohibited from giving assured return.
- The funds will have to necessarily move directly from the lender's bank account to the borrower's bank account to avoid the threat of money laundering
- The platforms should opine on the suitability of a lender and creditworthiness of a borrower and adequate regulation on advertisement
- The platform should prohibit cross-border transaction relating to residents and non- residents

What are the challenges for peer to peer lending in India?

The major hurdles for the peer to peer lending in India are as follows

- Limited use of digital signature
- Lack of precise regulation for peer to peer lending
- Limited access to credit bureau and also enlisting all the borrowers in credit bureau

The peer to peer lending can act as an alternative method for the financing small amounts. They could act as a precursor for the individuals before venturing into the formal banking channels.

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