P2P LENDING: AN OVERVIEW OF INDIAN P2P LENDING PLATFORMS

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ABSTRACT

In this age of sophisticated technology and rapid economic growth, India still has a largely unbanked and underserved population by the country's financial institutions. With more than 50% of the population with no access to formal funding, the country has largely been reliant on borrowing from friends and family, community, or the private money lenders.(Source: RBI)This is where **Peer-to-Peer (P2P) Lending** comes in rapidly growing Indian economy. P2P platforms provide the same facility with the help of technology thus enabling a much wider network of borrowers and lenders, and a win-win situation as the lenders earn more than the average return on bank deposits while the borrowers get cheaper funds. Present study compared P2P lending practices of 5 out of 36 P2P lending platforms in India and concluded that the adoption and reception of P2P lending in India has been tremendous from the public given the number of borrowers and lenders registered on P2P lending space. The study however found that there is supply demand mismatch as conservative lenders stay away from these platforms due to certain legal issues which need to be addressed by regulatory authorities in India.

OBJECTIVES OF THE STUDY

This study aims:

1. To introduce the concept of P2P lending as an alternative means of funds.
2. To give an account of P2P lending industry in India and brief on various lending practices followed by P2P lending companies in India.

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RESEARCH METHODOLOGY

A sample of 5 companies out of 36 companies in this industry has been taken to understand divergent lending and borrowing practices exercised by these P2P lending platforms. This study reviewed secondary data in form of academic papers and research reports on online P2P lending published between October 2014 and March 2016.The company based information was retrieved from databases of their respective websites. As P2P lending is of recent origin in India, availability of data was the major constraint in carrying out this research.

INTRODUCTION

Microsoft founder Bill Gates once famously said: "Banking is necessary, banks are not." The worlds of technology and finance are increasingly intersecting in such an exciting way that technology has altogether changed the definition of financial transaction. Banks have been transformed from document driven organizations to technology driven organizations. One of the most visible and important effects of technology on finance in recent years has been peer-to-peer (P2P) or marketplace lending. More efficient platform technologies, the ability to make more secure transactions, the potential for more competitive returns and the expansion of virtual communities has fuelled the development of P2P lending worldwide and has made it a disruptive force in the financial services sector. Peer-to-peer lending, sometimes abbreviated P2P lending is the practice of lending money to unrelated individuals, or "peers", without going through a traditional financial intermediary such as a bank or other traditional financial institution. This lending takes place online on peer-to-peer lending companies' websites using various different lending platforms and credit checking tools. Many also use the abbreviation "P2P" when discussing the peer-to-peer lending or investing industries more generally. Peer-to-peer lending can also be known as crowd lending.(https://en.wikipedia.org/wiki/Main_Page)

According to RBI report dated 26 June 2014 titled Financial Sector Regulation and Infrastructure, Peer-to-peer lending (P2P lending), also referred to as 'social investing', 'marketplace lending' or 'direct consumer lending' is the practice of borrowing and lending of money among unrelated individuals and business entities on online platforms without any role for a traditional financial intermediary like a bank or a non-banking financial institution. Crowd funding is a common term where small amounts of money from a large number of individuals/organisations is raised to fund an art work, social cause or start-up venture through web-based platforms. P2P lending is carried out through websites of P2P lending companies, using different lending 'platforms' which charge a relatively small commission for their services. P2P lending companies, apart from finding potential lenders and borrowers, also provide support services like verification of identity and financial details of the borrowers, credit models for pricing of loans and customer service to borrowers. P2P platforms are able to market themselves as modest community operations with an advantage of reduced costs for lending and borrowing.

Table1. Unique characteristics of P2p lending

- Usually conducted for profit
- Lenders and borrowers don't need to have a common bond or a prior relationship
- The P2P company serves as an intermediary, not a lending institution
- Transactions take place online, not in an office
- Lenders may choose which borrowers to invest in
- The loans are unsecured and are not normally protected by government insurance.
- P2P loans can be converted into securities and sold to other lenders

Source: Thomson Reuters

Table 2. Services provided by peer to peer intermediaries

Most peer-to-peer intermediaries provide the following services:

- on-line investment platform to enable borrowers to attract lenders and investors to identify and purchase loans that meet their investment criteria
- development of credit models for loan approvals and pricing
- verifying borrower identity, bank account, employment and income
- performing borrower credit checks and filtering out the unqualified borrowers
- processing payments from borrowers and forwarding those payments to the lenders who invested in the loan
- servicing loans, providing customer service to borrowers and attempting to collect payments from borrowers who are delinquent or in default
- legal compliance and reporting
- finding new lenders and borrowers (marketing)

Source: Wikipedia

ADVANTAGES OF P2P LENDING

Advantages for investors

- **High risk-adjusted returns:** The lenders are able to earn higher rates of interest than they would earn from bank deposits. Agreed it gets a little risky but then the returns are also much higher. While a bank deposit will yield around 8-10% a year, lending directly to a borrower through a peer-to-peer, or, P2P lending platform can get you an average return of 17-19%. (Source: Lending money through P2P platform can give higher return than banks, Chandralekha Mukerji , ET Bureau| Sep 16, 2015). It also allows lenders to choose borrowers as per their risk appetite and desired returns on investments.
- **Diversification**: It is a new type of investments that further diversifies a mixed investment portfolio. Investors can invest small amounts into multiple loan projects forming a sort of hedge and can create a diversified portfolio depending upon his risk appetite. It's like having the features of a large investment for a small one. P2P thus offers the best of both worlds for small investors.

Advantages for borrowers

- **Personalized interest rate.**
- ***Reduced Costs*****:** P2P lending helps borrowers reduce costs as it disintermediates the banks and connects borrowers directly to individual lenders.
- **Flexibility:** Borrowers can make overpayments or settle their loans early at any time, without charge.
- ***Transparency of Rates*****:** It brings in transparency in rates as all interests and fees are clearly presented and available to all site visitors.
- **Simple and fast process:** It is simple and fast for applying and monitoring (borrowers can log in and see status of payments etc.)

RISKS INVOLVED IN P2P LENDING IN INDIA:

- **Risk of default by borrowers:** While thorough fraud and credit-related checks on borrowers are carried out on P2P lending platforms, a few individuals most probably default on their loans. This loss of default by borrowers is borne by the lender and P2P lending platforms have no liability for these defaults.

➢ **All loans are unsecured:** Although, P2P lending platforms collect a range of documents including post-dated cheques from borrowers, the loans made through these platforms are unsecured, i.e. they are not secured by any collateral viz. property, gold, car, etc. Hence, in case of a potential default by the borrower only legal recourse is available to the lender.(Source:IndiaLends.com)

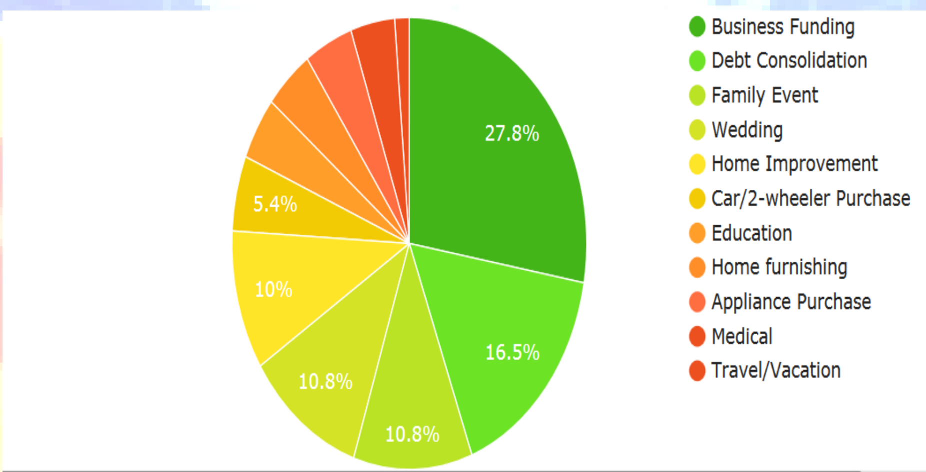
NEED FOR P2P LENDING IN INDIA

The world saw P2P lending emerge about a decade back. A company called Zopa in UK is credited with being the oldest peer-to-peer lending platform, having launched in March 2005. Then the trend came to India. P2P lending is a transformative new technology that would be a boon in a capital-starved country like India. Most Indians do not have access to formal credit. According to a report by international philanthropic investment firm Omidyar Network, Big Data, Small Credit—The Digital Revolution and Its Impact on Emerging Market Consumers, in India, more than 400 million people borrowed money in 2014, but fewer than one in seven were approved for a formal loan. Moreover India doesn't enjoy broad-based equity market culture. To bridge the gap of unavailability of proper formal credit, an aggressive breed of loan providers has emerged in India, called peer-to-peer (P2P) lending. The concept is not new. India had informal systems of moneylending for centuries. In the absence of bank credit Indians have traditionally relied heavily on loans from peers primarily amongst friends, family and the community. It has been till now an unorganised activity with no proper contracting, underwriting or recourse to recovery. P2P lending is an organized activity which is similar to a friend lending to you, but in this case, you have to pay an interest on the loan and the lender is a stranger. In India, technology-enabled P2P lending is at a nascent stage, with pioneering companies such as Kiva.org, Rangde.org, Milaap.org and Faircent.com. entering this arena only in the last few years. A rough estimate would peg the technology-enabled P2P lending market in India at about more than $4 million. India needs about a trillion dollars in investment to ramp up its infrastructure in the next few years. The general population can do a better job of lending and financing each other under a robust system of technology driven P2P lending which potentially frees up funds for nation building.

Current position

- The number of P2P lending companies in the online space has been increasing significantly. For instance, so far in the year 2015-16, close to 20 new online P2P lending companies have been launched, according to data compiled by Tracxn, a data analytics company. As of now, there are about 36 online P2P lending start-ups in India. This is much lower than the numbers in China, where the number of registered P2P companies is reported to have crossed 2,000.
- P2P lending platforms are not regulated by RBI. Market regulator Securities and Exchange Board of India (Sebi) has proposed a framework for crowd funding. It has floated a white paper, but subsequently there has been no movement. Without legal protection both lenders and borrowers are at risk.
- Currently, in India the online P2P lending can be broadly divided into three categories—micro finance, consumer loans and commercial loans. The consumer loans category can be further divided into personal and education loans. Some of the companies in this category are Faircent.com, Loanmeet.com and i-lend.in

Chart 1.Loan Purpose



Source: Faircent.com

Table3. Comparative analysis of P2P lending companies in India

Particulars	**Faircent.com**	**I lend.In**	**Lendbox**	**Loanmeet**	**Lendenclub**
Location/year of formation	Gurgaon/2014	Hyderabad, 2013	Delhi/2015	Bangalore/2015	Mumbai/2015
Number of lenders/borrowers	5000/20000	1300/3500	900/2000	670/1500	650/966
Hit-rate possibility of getting funded	1/10 applications	3/10 applications	6/10 applications	1/20 applications	-
Total of disbursal	Rs.2 Crore	Rs.90 lakhs	Rs.75 lakhs	Rs.61 lakhs	-
Lenders mandate	Rs.10,00,000 of investible funds,above 25 years of age,investment in stocks,possession of immovable property.	Annual Income of 8 lakhs,Pan card,only graduates	Pan card,ID proof,one cheque leaf	All Banks, NBFCs, inancial institutions,all Indian nationals with a bank account	Minimum age 21 years/Company PAN Card Valid Bank Account Address proof
Borrowers mandate	Salaried borrowers, SME owners with cash flows	Salaried borrowers(25000 p.m.,6 months continuous employment)	No salary/income limits(3 scurity cheques)	No salary constraints,last two years IT returns,12 month bank statements,Pan /Aadhar card	Pan/Aadhar/ bank statements(one banking transaction from bank account favouring

					Loanmeet)
Amounts one can borrow (personal loan)	30000-5 lakh	25000-5 lakh	25000-5 lakh	50000-5lakhs	25000-3 lakh
Loan tenure (years)	0.6-3	0.5-2	0.5-3	0.3-2	0.5-3
Average loan disbursement time(days)	5-7	5-7	5-7	1-3	4
Min. number of lenders to fund a loan	5	3	2	-	1
Presence	Pan India	Hyderabad	30	Pan India	Pan India
No. Of parameters to evaluate borrowers	Over 250	Over 25	120	Multiple	25
Collateral security	Post dated cheques ,No collateral security	Post dated cheques ,No collateral security	Post dated cheques, No collateral security	Post dated cheques ,No collateral security	Post dated cheques ,No collateral security

Source: 1.Companies websites 2.The Economic Times 3.Business Standard

Analysis and Interpretation:

1. Although P2P financing is at a nascent stage in India, with pioneering companies such as Faircent.com.,Lendbox,lenenclub,lendenmeet and ILendIn entering this arena only in the last few years but seeing the number of lenders and borrowers entering online space it is evident that the adoption and reception, however, has been tremendous from the public. Faircent has disbursed loans up to Rs.2 crores since its inception in 2014.

2. Comparing the number of lenders with number of borrowers it can be concluded that very few lend but most borrow. It clearly shows demand supply mismatch. Faircent which started its operations in 2014 claims to have over 5,000 registered lenders and 20,000 borrowers. The reason can be that conservative investors stays away from such investments as higher return also brings itself higher risk which is the basic fundamental of finance. It can be attributed to the fact that although, P2P lending platforms collect a range of documents including post-dated cheques from borrowers, the loans made through these platforms are unsecured. If the Borrower's cheque gets bounced then the lender is himself liable for the trial under Negotiable Instrument Act. This, along with the lack of lender protection leads to a lack of lender confidence.

3. Many salaried persons don't get unsecured loans from banks, due to strict guidelines from the regulator. These platforms provide loans to the borrowers with low salaries. Banks restrict doing so to borrowers who are employed with reputed companies.

4. The loan amount and time period differ from platform to platform. However the loan amount can be as low as Rs 25,000 and as high as Rs 5 lakh, for tenures between three months and three years.

5. Depending on the platform eligibility criteria for being a lender differs.like one you has to be an Indian resident, at least 21/25 years of age, have a valid bank account, PAN or other governmentIds.

Those looking to use these platforms to make extra money by lending to individuals also have to go through the KYC.Some don't allow a single lender to fund the entire requirement of a borrower. Faircent, for example, requires a minimum of five borrowers to fund a loan and i-lend three. Rajat Gandhi, founder and chief executive (CEO) says the idea is to build a loan portfolio that spreads the risk for lenders, in case one goes bad.

6. Unlike taking a loan from a bank, these platforms are do-it-yourself. So, there will be no executive visiting to collect documents and provide other services. A borrower needs to scan and upload documents for KYC, such as photo, PAN card, Aadhaar card and passport. Then, they

need to provide income-related documents such as bank statement, salary slip and income tax returns.

7. These platforms use big data to analyze the credit worthiness of the borrowers. Sources of getting credit information can be credit bureaus, non-banking finance companies and also applicant's friends and connections on social networking sites such as Facebook and LinkedIn.As a result, the CIBIL score is now just one criteria out of 120 in Lendbox one of the major P2P lenders, which brings millions of people who have been denied credit previously under its ambit. This is the reason that it has hit rate possibility of getting loan of 6 out of every 10 applications.

8. These platforms also focus on providing good terms to borrowers with good credit rather than chasing borrowers with bad credit. Faircent decline over 90% of the loan applications they receive. That’s the price it pays to deliver predictable performance to investors.

9. Presence of most of P2P lending platform is Pan India i.e. .their services are available in all parts of India.

10. P2P lending platforms ensure quick processing of loan applications. The loans are mostly disbursed within 5-7 days working days post receipt of the application.

Table4. Commission, Registration, Processing charges and Interest rates

	Faircent.com	**I lend.In**	**Lendbox**	**Loanmeet**	**Lendenclub**
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**	**1-3% from borrower**
Registration Fee for borrowers/lenders	**Rs.1500(refundable if funds not raised)/1500**	**Rs 500/nil**	**Nil/1%0f invested amount or Rs.1500**	**Rs.1000(50% r efundable if funds not raised))**	**Nil/nil**

			whichever is higher		
Processing fee for borrowers/lenders **(% of loan amount)**	**Nil** /Nil	**3**/1	**2-6**/Nil	**2-5**/Nil	**2**/Nil
Interest rates	**0-36**	**0-24**	**12-36**	**11-31%**	**12.5-30**

Source: 1.Companies websites 2.Economic Times 3.Business Standard

1. Many of these platforms charge a registration fee and also a processing fee from borrowers. I-lend.In, one of the oldest players, charges Rs 500 for registration and one per cent as processing fee. Another popular platform, Faircent.com, does not charge any processing fee but charges 2-6% of the investing amount on listing of the loan.charges Rs 1,500 for registration, later adjusted in the processing fee when the borrower gets a loan. "The registration fee is to ensure only serious borrowers come to the platform. In the early days of operations, many borrowers backed out at the last minute," says Rajat Gandhi, at Faircent. Many of these companies also have registration charges to cover the costs associated with KYC and physical verification. Also, as per prevalent tax laws, interest income will be taxed as regular income and the investor will be liable to pay the same. P2P lending platforms usually provide an annual interest income statement to the investor, which he/she can refer to while paying taxes.

2. Most of these platforms don't charge lenders any registration or processing fee.

3. Borrowers with lower credit risk get a lower interest rate and vice versa. The rate varies between nil and 36 per cent at Faircent.com. The borrower can get loan at as low as 11% at Loanmeet.com and 12% at Lendbox. So peer-to-peer lending system is cheaper for borrowers as they do not have to pay any of the bank charges and the interest rate is based on their actual financial capability based on a comprehensive credit assessment. Please note that lenders have the final say on interest rates, and the borrower has the option of saying NO to the lender.(Source:Loanmeet.com) According to Shankar of I-lend, interest rates are capped at 24

per cent — thereby ensuring that professional moneylenders do not use the platform. However, many others don't have any cap.

Conclusion

Potential of P2P lending in India is immense as more than 50% population in India is unbanked. Those whose applications are rejected by banks due to strict lending norms fixed by regulatory bodies can also avail loans on these platforms as these platforms do not ask for collateral securities and use big data to analyze the credit worthiness of the borrowers. P2P lending thus might be able to come to the rescue when traditional doors are closed. However lack of regulatory control on this industry can prove to be a hindrance in tapping millions of potential clients as most of loans sanctioned on these platforms are unsecured in nature. This issue needs to be tackled so that investors can enter p2p space with greater confidence.

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