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Study about Digital Financial Services: Opportunities and Risks During COVID-19 Pandemic

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Abstract- During the COVID-19 pandemic digital financial services came into limelight and gave significant fillip to consumers digital- centric financial activities and changing consumers using habits of fintech services during the lockdown period and the need of social distance over the last couple of years, the result is that more new consumers have influenced to use digital financial services for meet their basic financial needs such as saving, payments, credit, insurance etc. A great number of families and organizations were able to quickly access online payment and other financing operations as a result of the epidemic, which created potential and problems for extending digital financial inclusion. During the course of the pandemic, governments had raced to give financial help to local inhabitants. This paper studies the opportunities and risks that financial technology innovation presents during the COVID-19 health crisis due to enhanced usage of digital financial services. This paper also focuses on the country's strategy during the global crisis to manage which is useful to expanding digital financial services.

Keywords: *Digital Financial Services, Opportunities, Challenges, COVID-19 Pandemic*

I. Introduction

Digital financial services (DFS) refer to financial services that are accessible and supplied using digital technologies and channels, including mobile devices. These services are used by consumers for various purposes such as payments, remittance, and credits. These services include traditional financial instruments such as Debit cards, Credit cards, and Prepaid cards provided by banks, as well as innovative solutions based on cloud computing, digital platforms, and distributed ledger technologies (DLT), covering mobile payments and peer-to-peer (P2P) applications. These recent solutions are sometimes referred to as fintech.

Digital transformation of other industries made users more trusting and convenient with tech-based financial solutions. There is also increased demand for immediacy and customized financial products and services. For this instant finTech companies play a prominent role. FinTech companies are meeting these users' demands with low cost and convenient ways to transfer money, borrow, and invest. FinTech-enabled digital financial services have the capacity to reduce expenses through the maximization of economies of scale, thereby enhancing transaction speed, security, and transparency. Additionally, these services enable the provision of more customized financial provisions that cater to marginalized and weaker segments of society, as well as individuals with low incomes.

The COVID-19 pandemic has heightened the significance of employing fintech to ensure the functionality of financial systems and the safety of individuals amidst social distancing measures, declining input supply, constricting credit conditions, and increasing uncertainty. So as not to exacerbate the difficulties presented by this crisis, these new technologies must be meticulously designed and implemented in the interim with their risks meticulously managed, with a particular focus on the impoverished and vulnerable. Additionally, investments in the prerequisites for the development of digital financial services—such as the expansion of digital identification, mobile broadband infrastructure (including in remote areas), and open application programming interfaces—are urgently required. Complementing these investments with the appropriate legal and regulatory frameworks would enable the majority of individuals to utilize digital financial services and guarantee a competitive environment. The current crisis has brought attention to the manifold advantages of digital financial services and their indispensable contribution towards the realization of sustainable development objectives.

The corona virus outbreak and restrictions on physical contact have boosted demand for online financial services, making it more imperative for banks to accelerate digitalization. The COVID-19 pandemic has highlighted the advantages of DFS expansion, as it greatly minimizes the need for in-person interactions in financial transactions and facilitates quicker government responses to provide liquidity to businesses and individuals most vulnerable. DFS has made distant payments and transactions possible, especially via the use of mobile money, facilitating the social separation that is advised to reduce spread. With digital payments, customers may transact money, settle debts, and make purchases from the comfort of their own homes or from a market or retail location with little to no in-person interaction. DFS makes it possible for governments to quickly and securely provide social transfers and other financial aid to those in need, particularly in situations where travel inside the nation is hazardous or restricted.

We can hasten the resolution of the health issues, aid in economic recovery, and provide the groundwork for a return to economic growth by encouraging the broad use of digital financial services. Over time, it will promote economic expansion and end poverty.

II. Review of Literatures

Several scholars have examined "factors influencing consumer adoption of digital financial services during the pandemic. (Daragmeh et al., 2021) found that the fear from infection of coronavirus was a critical factor to influence elder generations including generation X to adopt mobile payment during the pandemic, as they consider it as a preventive tool to avoid the infection instead of using cash or contact based payment that could be carrier of virus. The study highlights the role of the COVID-19 pandemic in encouraging populations that were less willing to use digital financial services before the pandemic. (Immanuel et al., 2020) have used the Technology acceptance model to study the factors that affect Indonesians to adopt mobile payments/cashless payment during the pandemic. The study revealed that consumers' personal attitude towards m-payments was influenced by their knowledge of the health role of this kind of payment during the pandemic. (Daragmeh et al., 2021) studied the potential for consumers' continued usage of electronic wallets through an integrated model of the Technology Continuous Theory (TCT) and Health Belief Model (HBM). The study found that while the COVID-19 pandemic strongly influenced the current use of e-wallets; the pivotal factor affecting their continued use is based on consumer self-efficacy. Researchers have suggested the protective behavior during the pandemic COVID-19 as a way for policy makers to encourage customers to use e-wallets. They also suggested that banks and FinTechs should develop further strategies to attract customers to e-Wallets by reassuring them the value and benefits of this kind of financial service. Moreover Perceptions of health risk which includes perceived susceptibility and perceived severity have been shown to influence intentions to continue therapy through consent, feelings of usefulness, and satisfaction (C.C.S, -Prathap SK, 2020). Due to the growing threat of covid-19 in India, the study's authors urged policymakers to resort to mobile payments and banking to differentiate themselves from the public".

III. Objectives

1. To examine the potential benefits of increasing digital financial services in response to the covid-19 problem.
2. The objective is to assess the risks associated with the expansion of digital financial services in response to the covid19 pandemic.

IV. Research Methodology

This study is based on the secondary data collected from different journals, magazines, research articles, periodicals, and websites.

V. Findings

The use of DFS is seeing significant growth in India. The Government's initiatives to enhance financial inclusion and reduce reliance on cash have effectively stimulated the use of digital financial services, namely electronic payments, resulting in notable growth.

The Reserve Bank of India (RBI) has developed the Digital Payments Index (DPI) to measure the performance of digital payments in the country. The index is based on March 2018 data, with a score of 100 assigned to that period. The DPI scores for March 2019 and March 2020 were 153.47 and 207.84 respectively, demonstrating significant increase in digital payments. Additionally, the regulatory body predicts that the volume of digital transactions will increase to 87 billion in 2021, up from around 40 billion in 2020. According to statistics from the RBI, the volume of digital payments has grown by about sevenfold between 2015 and 2020.

India has many advantageous features that support the development of digital financial services. These include a substantial and expanding middle class population, a well-established digital identity system known as Aadhaar, and a rising prevalence of smartphones and high-speed internet. The fintech industry is garnering international attention. India's fintech industry is drawing investment from international venture capital firms, highlighting its significant development prospects. Fintech start-ups have secured over $10 billion in capital financing over the previous six years.

Only in the year 2019, a total of over 200 startups managed to secure around $3.2 billion in funding. Aside from venture capital companies, Amazon.com Inc. and Facebook have also made investments in this industry. Furthermore, DBS Bank Ltd from Singapore has established a digital bank in India.

Furthermore, international incubators and accelerators such as Startupbootcamp, Barclays Rise, and Swiss Re InsurTech have launched programs in India.

Opportunities for Expanding Digital Financial Services in Light Of COVID-19 Health Crisis

In order to maintain the running of economies when mobility is constrained, COVID-19 has established a platform that will facilitate the acceleration of digital financial services all over the globe. This will be driven by a fast development of digital payment methods.

1. Payment and Transfer by Government

During the COVID-19 epidemic, "governments engage in digital transactions to provide payments and remittances to people and companies. Government payments to households, sometimes referred to as Government-to-Person (G2P) transfers, include tax refunds, subsidies, salaries, pensions, scholarships, emergency relief payments, and remittances. Government-to-business (G2B) payments are now being facilitated via a range of digital payment methods. Although digital payments facilitate uninterrupted transactions and provide financial assistance to those requiring help, health protocols pose challenges for alternative payment methods. Implementing digital payment systems for public salaries and other public transfers in both the government-to-person (G2P) and government-to-business (G2B) sectors will result in increased cost-efficiency. Digital payment technologies improve the capacity to provide financial aid to specific groups, particularly those without bank accounts, women, and workers in the informal sector. These technologies have the potential to accelerate the speed of remittances, which is especially beneficial during the COVID-19 crisis since several poor nations heavily rely on informal sectors and need immediate assistance. In addition, his G2B digital payments during the crisis included grants for employee salaries, an employee retention fund for small and medium-sized firms, and a company financing program. Recent developments in financial technology have facilitated the ability of governments to monitor consumer spending patterns in real-time".

2. Payment by Businesses

Distributed computing may transform back-office operations, securities settlement, and payments by reducing costs and enabling direct business-to-business (B2B) transactions without the need for intermediaries. If your intermediary has been impacted by the COVID-19 situation, it can be advantageous to circumvent your middleman. For example, banks may have delays in processing payments owing to reduced staffing caused by quarantines or sickness. In addition, certain forms of payments, especially those involving transactions across borders, may include a sequence of intermediaries, such as correspondent banks, and may be susceptible to global economic circumstances.

3. Payments by Households

It may be possible to maintain social distance policies and reduce the danger of COVID-19 transmission by using contactless digital payments for person-to-person (P2P) transfers and purchases made in physical shops and online. Digital payment apps, prepaid bank cards, unified payment interface services, mobile wallets, debit/credit cards, and unstructured supplementary services data are just a few of the digital payment methods that households throughout the globe are gradually embracing. An analysis of Indian homes reveals a surge in digital payment transactions within the ongoing coronavirus pandemic. Aside from the advantages of maintaining social distance, the digitization of person-to-government (P2G) payments also presents prospects for augmenting tax collection. The use of digital tax payments should improve the transparency of tax payments, so aiding in the fight against tax evasion and corruption.

4. Lending to Businesses

The Digital company Lending Provisions enable social distancing measures during the COVID-19 pandemic by minimizing the need for company owners to personally visit banks in order to engage with loan personnel and submit documents. This is anticipated to enhance the level of security. The diverse range of technologies now accessible have shown their advantageous impact on providing loans to enterprises, particularly in times of crisis. Machine learning algorithms may aid non-bank lending platforms and digital banks in remotely evaluating the creditworthiness of small and medium-sized organizations. This can expedite the loan distribution process by automating the due diligence procedure. The use of big data analytics has the potential to automate the process of loan approvals and assist in ensuring adherence to regulatory requirements and detecting instances of fraud. Fintech businesses, which integrate lending with other services like payments and social media, have access to data sources that are not accessible to other lenders, within the boundaries of data and privacy legislation and competition standards. Such financing may be particularly important for the informal sector, small and medium-sized enterprises, and micro entrepreneurs, where public information is relatively scarce and access to credit through traditional banking channels may be difficult. During crises, the importance of this factor is heightened since knowledge asymmetries may exacerbate credit restriction. Consequently, in times of crisis when banks' financial positions are weakened and lending is limited, emerging non-bank financing platforms are gaining significance.

5. Lending to Households

Granting digital loans to families may benefit society within the COVID-19 problem by diminishing the need for people to physically visit banks in order to engage with loan officers and submit documentation. It may also be useful for ensuring physical distance. Person-to-Person (P2P) lending platforms have low overhead costs and offer their services cheaper than traditional financial institutions. In particular, small and medium-sized financial institutions are participating in such platforms. FinTech companies are innovating methods to expedite loan processing, while lenders strive to access untapped areas and demographics. As a result of recent advancements in lending technology and the adoption of fully automated lending processes, P2P lenders that are just getting started often provide better services than traditional financial institutions. Securing bank loans might be challenging during economic downturns. Nevertheless, because of their modest size and possible lack of documentation, these platforms could provide a trustworthy source of loans for residences and businesses that would otherwise be refused credit.

There are inherent hazards in expanding digital financial services in the midst of the COVID-19 health crisis.

An ecosystem for digital banking that operates efficiently has the potential to boost competition in the financial services industry, which in turn might assist to lower prices, enhance quality, and make things more convenient for consumers. However, there are also concerns associated with the fast spread of digital financial services, particularly for users who have not previously used formal finance or who have limited access to digital resources, technological expertise, and experience.

1. Stability and Integrity

The impoverished and elderly often encounter challenges while attempting to use digital banking services. Furthermore, the adjustment might prove to be especially challenging for these specific groups. Following the Indian government's decision to demonetize in 2016, there was a significant drive to promote the use of digital payments. Multiple studies indicate that the lower-income and less technologically proficient portions of India's population are disproportionately impacted by this disruption.

2. Operational Constraints

The COVID-19 pandemic has resulted in operational limitations, including cyber-attacks, digital fraud, and money laundering. Digital financial services are susceptible to increased vulnerability from cyber-attacks, digital fraud, and potential exploitation. This assertion holds particularly true if the endeavors to swiftly enhance digital transactions during the COVID-19 pandemic are not accompanied by similarly swift advancements in cybersecurity. Even in areas where the digital payments infrastructure is already established, the quick development of service offerings might result in operational risks. These risks include “possible limitations of the system and the unavailability of essential workers, particularly if individuals are impacted by quarantines or sickness. Moreover, digital financial services mostly reliant on social media applications may be more prone to panics. This phenomenon may be attributed to the use of message, including the dissemination of false information, on social media platforms”.

3. Increased Inequalities

Ramping up digital financial services during the COVID-19 pandemic period may have increased the inequalities between different groups. The rapid transition to Digital Financial Services (DFS), which may be encouraged during the epidemic, might initially worsen economic and gender inequality, as well as amplify the gap between rural and urban areas and among young people. Women exhibit lower frequency of mobile phone Internet use compared to males. Additionally, people in rural areas are less likely to use mobile internet and digital financial services compared to people in urban areas.

4. Data and Privacy Issues

The rapid proliferation of digital financial services during the pandemic may have given rise to concerns around data and privacy. The extensive use of digital financial services may raise worries over the creation of a surveillance state. This situation may arise when firms have restricted access to data, which may possibly lead to problems around privacy and data monopolization. The concerns about the use of payment data by governments and commercial entities are consistently significant. However, during times of crisis, there exists a potential for democratic scrutiny and corporate regulation to be circumvented.

5. Infrastructure and Connectivity Issues

The expansion of digital payments and digital finance is closely tied to infrastructure, which encompasses dependable energy, widespread mobile phone use, and internet access. Although not directly related to the financial industry, infrastructural issues might hinder the efficiency of digital payments. It is crucial to consider these challenges when implementing solutions, whether by governmental or private entities. This entails the development of goods that are compatible with feature phones and the establishment of an ecosystem that addresses deficiencies in connection. Investments in infrastructure are further justified by the long-term potential of conducting financial, commercial, and government activities remotely, facilitated by digital finance.

Policy Responses during COVID-19 Pandemic

The crisis reaction was spearheaded by the public sector, which aimed to “minimize the damage and facilitate the revival of the economy. Since 2020, the Reserve Bank of India (RBI) and the Government of India have implemented significant measures to support microfinance consumers and institutions”.

The RBI used a dual strategy that included injecting liquidity and implementing restructuring measures. The Reserve Bank of India (RBI) has granted permission to lenders to provide moratoriums on loan repayments. Additionally, the RBI has instructed that the status of an account in credit bureau reporting should be maintained while it is under moratorium. This measure aims to safeguard clients' credit records and ensure their future access to credit. The suspension imposed a significant strain on Non-Banking Financial Company-Microfinance Institutions. In June 2021, a survey conducted among members of the Microfinance Institutions Network (MFIN) revealed that Non-Banking Financial Company-Microfinance Institutions (NBFC-MFIs) had granted a moratorium for almost one-third of their payback installments. This has resulted in significant challenges in managing liquidity, since NBFC-MFIs depend on client repayments to fulfill their own debt commitments. Due to their set personnel and infrastructure expenditures, the majority of MFIs have little flexibility to rapidly modify their operating expenses.

Furthermore, the RBI's August 2020 "Resolution Framework for COVID-19 Related Stress" was a singular resolution designed for loans that were not in default for more than 30 days. Subsequently, the Reserve Bank of India granted permission to financial institutions to modify the terms of individual and small company loans. Both settlements offered significant respite to microfinance clients. The Reserve Bank of India (RBI) introduced specific liquidity de-stressing initiatives and eased loan provisioning criteria for Microfinance Institutions (MFIs). The Ministry of Finance enhanced its initiatives by providing partial credit guarantees, implementing a "ex-gratia" program to cover the disparity between compound and simple interest for a period of six months for certain loan categories, and introducing the PM Svanidhi scheme which offers loans and credit guarantees to support street sellers. Although beneficial, these actions were insufficient in completely alleviating the liquidity difficulties faced by lenders.

In September 2020, the situation ameliorated as clients' repayments recommenced. Simultaneously, officials acknowledged the importance of microfinance in promoting inclusive economic development, sending a clear and positive message to the market on its potential for recovery. However, the microfinance industry began the 2021-2022 fiscal year with an unpredictable and unprecedented challenge posed by COVID-19. The sector faced a second wave of infections and partial lockdowns, which adversely affected the lives of consumers and restricted the operational mobility of lenders. The government has created an additional credit guarantee program that encompasses a wider range of Microfinance Institutions (MFIs). This initiative is based on recommendations by MFIN, an organization that collaborated closely with the Ministry of Finance.

The government has also introduced supplementary fiscal measures, which are as follows:

Assistance provided to homes includes:

- Provision of food and cooking gas as well as monetary assistance to older residents, widows, handicapped individuals, farmers, and women Jan Dhan Account holders refers to those who participate in a national savings system specifically designed for those who did not have a bank account before.
- Healthcare workers will receive insurance coverage.
- Wage increases will be provided to individuals working under the Mahatma Gandhi National Rural Employment Guarantee Act, as well as support for building and construction workers.
- Self-help groups will have access to collateral-free loans.
- Retirement fund contributions will be reduced. • Migrant workers will have employment opportunities.

Assistance provided to MSMEs encompasses:

- Loans without collateral that come with a complete assurance of repayment
- Financially distressed MSMEs will get subordinate loans along with a partial guarantee.
- Public sector banks would get limited guarantees on loans provided to NBFCs, home finance providers, and MFIs.
- A collection of investment funds especially tailored to provide financial assistance to Micro, Small, and Medium Enterprises (MSMEs) via equity investments.
- Provide further support to farmers by giving them access to funding with reduced interest rates.

Measures for compliance and regulation consist of:

- Tax-filing and other compliance deadlines will be delayed.
- Penalties for delinquent goods and services tax filings will be reduced.

- Government procurement laws will be modified.
- MSME dues will be cleared more quickly.
- MSMEs will get relaxations linked to the insolvency and bankruptcy legislation.

The Indian economy successfully mitigated the impact of the COVID collapse with the implementation of exceptional fiscal and monetary measures, supported by the world's biggest immunization campaign. As of March 2022, the microfinance sector exhibited evident indications of recuperation: loan disbursements had reached levels comparable to those before the COVID-19 outbreak, repayments exceeded 95 percent, and no microfinance institutions declared bankruptcy over the two-year duration of the pandemic.

Conclusion

This research study predicted that digital financial services will effectively and reasonably facilitate the connection between entrepreneurs and banks, workers, suppliers, and emerging market trends. Peer to peer transactions, such as remittances, are enabled, allowing governments to effectively and rapidly provide assistance to underprivileged individuals and enterprises. Amidst the COVID-19 issue, these aspects gain more significance as governments endeavor to effectively distribute monies to the needy, while several families and companies endeavor to swiftly shift towards online payments, banking services, and other financial transactions. Simultaneously, DFS enables the practice of social separation, which is especially valuable in the midst of the epidemic. DFS has the potential to enhance financial inclusion in distant and marginalized communities where traditional financial institutions are not physically present. Moreover, endeavoring to promptly evaluate digital financial services inside a constrained timeframe, while a pressing response is being formulated, is not just arduous but also potentially perilous. The potential hazards linked to stability and integrity, including functional constraints, cyber assaults, fraudulent activities, money laundering, data breaches, and sequestration issues, persist constantly and may escalate when the use of digital financial services is heightened during periods of exceptional circumstances. Carrying out a fast expansion of DFS during a crisis poses fewer dangers if sufficient safeguards and limitations are not put in place. Furthermore, since there are already large disparities between genders and age groups in the use of DFS (Digital Financial Services), increasing the drawbacks of DFS exacerbates these inequities. Similarly, if there is no guarantee of access to a substantial informal sector or if there is a considerable limitation in financial understanding, the aforementioned statement remains valid. During times of instability, the process of facilitating the transfer of funds between banks may become precarious, especially during the period of economic recovery. The government has implemented steps to incentivize banks to provide loans by offering them stimuli, such as guarantee programs or non-supervisory adjustments. In the event that the severity of the crisis also has an effect on nonbank lending, there may still be potential for digital nonbank financial services to offer the essential support in situations when banks and other traditional financial intermediaries are unable to meet the requirements of consumers and enterprises. Digital advancements in payment systems and other banking and financial services have the potential to deliver value for all persons during times of pandemic crisis and beyond, provided that the possible problems are appropriately managed. This is after the potential issues have been adequately handled.

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