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Impact of Fintech on Emerging Economy

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Abstract

Over the past decade, innovation in Fintech, such as Digital Banking, Embedded Finance, Cybersecurity, Neo Banking, and various other services, has massive impact on financial inclusion and economic development in emerging economies. It focuses on the significant growth in global financial account ownership, rising from 51% to 79% in recent years, illustrating how digital technologies have bridged gaps for households and MSMEs. The study investigates the influence of UPI transaction data in income tax enforcement using the example of Bangalore's GST notices that unintentionally reverted MSMEs back towards cash transactions, thereby weakening the digital payment ecosystem. Moreover, it focuses on the challenges arising from the previously uncontrolled digital lending environment, which allowed exploitative lending practices and data misuse, damaging borrower trust and increasing financial risks. Through a mixed-method analysis based on secondary data sources such as the World Bank's Global Findex and regulatory documents, the study reveals a major impact of Fintech: while few digital tools have enhanced tax compliance and expanded credit access, they have similarly introduced administrative burdens and risks of exclusion for unprotected groups. The research concludes with policy recommendations that are aimed at balancing innovation with consumer protection. These include raising the GST threshold to ease burdens on small MSMEs, enhancing the credit support mechanism along with the government-backed guarantees and digital platforms for invoice financing, and implementing the RBI's Digital Lending Guidelines that promote transparency and fairness in digital lending. Thoroughly, the research emphasises Fintech's dual role as an enabler of economic growth and a sector requiring careful regulatory oversight to foster sustainable development in India's emerging digital economy.

***Keywords**: Fintech, Economic, GDP, Finance, Digitalisation, Digital technology, RBI's Digital Lending Policy, Digital Banking*

Introduction:

Fintech is the operation of digital technology to fiscal services. There are various applications of digital technologies in fintech, such as digital payments, Mobile banking, Online lending, robo-advisors, InsurTech, RegTech, cryptocurrencies, and digital assets. It has accelerated after COVID-19 hit. As financial services are digitalised, it helps to bridge the gap between money and financial services for households and firms, and it also promotes economic development. The latest World Bank Global Findex data shows that global financial account ownership grew from 51% of the adult population in 2011 to 76% in 2021 and to 79% in 2025. Access to basic financial services, such as transactions, payments, savings, credit, and insurance, helps people manage risks, build wealth, and invest in businesses. Yet many people and firms still lack access to essential financial services that can help them grow. Technology can lower transaction costs by overcoming geographic access barriers; increasing the speed, security, and transparency of transactions; and enabling more accommodated fiscal services that better serve consumers, including the poor.

Review of Literature:

Sneha Ghosh (2025) demonstrates how the Fintech industry in India has changed over a period that directly impacts the nation's economy through enhanced economic efficiency, massive financial inclusion, and digitalisation. The rise of digital payments, peer-to-peer lending, robo-advisory services, and blockchain applications has revolutionised traditional banking, making financial services more accessible and efficient. Fintech has played a major role in expanding financial involvement by reaching unbanked and underbanked communities through mobile banking, digital wallets, and microfinance solutions.

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The switch of consumers toward digital transactions reflects their changing behaviour and reduced dependence on conventional banking.

Nenavath Sreenu (2025) states in their study how fintech serves a crucial role in empowering India's financial sector and driving its digital economy. Using the CRITIC technique, it analyses fintech and digital economy indicators across all 28 Indian states from 2010 to 2022, resolving complex linkages between technological innovation, financial inclusion, and economic development. The results state that fintech not only promotes innovation but also reduces financial decentralisation at the local government level, enabling streamlined financial processes. Moreover, the study highlights that regional financial regulatory resources significantly enhance fintech's positive impact, particularly in advanced financial regions where stronger regulatory frameworks expand innovation and digital transformation. By representing multiple theoretical frameworks, including innovation diffusion, technology acceptance, and economic growth theories, the research builds a comprehensive understanding of fintech's role in shaping India's evolving digital prospect.

Maja Pejkovska (2018) has shown the potential negative impacts of Fintech on the global financial services sector, focusing on three core elements: blockchain and cryptocurrencies, alternative payment methods, and innovations in investment and banking. By studying empirical evidence from the European Union (EU), India, and the United States (USA), it analyses how Fintech disrupts traditional financial institutions, the reasons behind its massive expansion, and the current state of Fintech regulation in these regions. The study finds that existing regulatory frameworks in all three areas are insufficient to address the complexities and risks emerging from Fintech's swift growth. This regulatory gap increases the concerns over cybersecurity threats, data privacy breaches, and the possibility of Fintech platforms being used for unlawful purposes. Therefore, the paper emphasises the urgent need for regulatory authorities in the EU, India, and the USA to establish well-defined and comprehensive policies that can support innovation while safeguarding the stability and security of the global financial ecosystem.

Srinivas Subbarao Pasumarti (2024) finds and summarises how fintech is transforming India's financial sector while introducing complex legal challenges. With India emerging as a global fintech hub, issues like data privacy, AML/KYC compliance, and regulatory ambiguity demand attention. Fintech firms handle a massive bulk of sensitive financial data, yet India's evolving legal framework, governed by the Information Technology Act (2000) and the forthcoming Personal Data Protection Bill, creates compliance complexities. Similarly, stringent anti-money laundering (AML) and know your customer (KYC) rules require robust systems for verifying customers and monitoring transactions. Furthermore, the fragmented regulatory environment, involving bodies such as the RBI and SEBI, often leaves fintech companies operating in uncertain legal territory. This lack of clarity poses risks and can slow innovation. Consumer protection is another major concern, as many fintech services fall outside traditional banking regulations, increasing potential risk for users. To address these challenges, fintech companies must prioritise data security, maintain strong compliance frameworks, and actively collaborate with regulators. Striking a balance between innovation and regulation will be essential for encouraging a secure, inclusive, and globally competitive fintech ecosystem in India.

Research Methodology

The research involves analysis from secondary sources with a mixed method approach, combining qualitative and quantitative techniques to comprehensively investigate the question arising during research. Qualitative data was gathered through books related to Fintech published from 2018 to 2025, while quantitative data was extracted from reports generated by the World Bank Group and many more.

Objective:

1. To understand the influence of Income Tax, using UPI transaction data and MSME outcomes.
2. To analyse RBI's Digital Lending Guideline and its impact on Fintech operating and revenue models in India's Digital Economy.

Hypothesis

Rising issues of the MSME sector influencing income tax

Income tax influences MSME outcomes through various digital transactions data through its applications, such as instant payments, faster credit access, improved cash flow, streamlined operations, market expansion, enhanced creditworthiness, government & financial integration for audit under Section 56(2), treating them as a taxable income from other sources. UPI's machine-readable trails support tax hubs that auto-generate pre-filled returns and invoices, boosting compliance but increasing administrative burden for informal MSMEs. Due to this digital footprint reduces cash dependency while exposing turnover for deduction like 6% on digital vs. 8% on cash under Section 10AA, which provides income tax deductions (tax holidays) to businesses or units operating within a Special Economic Zone (SEZ) to promote exports, and attract investment and Section 80IA, which provides tax deductions for eligible businesses.

Tax analysis via UPI data leads to GST notices on informal vendors, causing them to return to cash, diminishing the digital framework, and profit margins, among added compliance costs. Positively, 50% of surveyed MSMEs reported turnover/profit growth in 2023-24 via digitalisation. But according to the recent news, Karnataka's Commercial Taxes Department issued GST notices to over 14,000 unregistered small vendors and MSMEs in Bangalore based on their UPI transaction data from FY 2022-2025, targeting those with annual inflow exceeding ₹40lakh (goods) or ₹20lakh (services). The Bangalore UPI tax notices case harms India's emerging economy by driving

MSMEs back to cash, raising compliance costs, and slowing financial inclusion.

Recommended Policies for Sustainable Growth

- **Policy Reforms for Balance**
  Raise GST threshold to ₹1crore for small MSMEs and introduce refined exemptions for exempt goods in UPI-based notices to reduce compliance burdens while sustaining revenue. Offer composition schemes for turnover up to ₹15crore, bid interest or penalties via GST Council exempt, preventing cash return.
- **Support and Capacity Building**
  The Union Budget 2025-26 is enhancing the credit guarantee cover for MSMEs from ₹5 crore to **₹10 crore**, enabling ₹1.5 lakh crore additional credit over five years, and launching customised **₹5 lakh credit cards** for 10 lakh micro-enterprises on the Udyam portal for working capital needs. Adding to this point, digital literacy programs like Mahila Utkarsh Yojna will be introduced to economically empower women, which provides micro-finance and loans; all these schemes aim to promote women entrepreneurship, self-employment and financial independence.
- **Enforcement and Incentives**
  SBI Research urges sensitive GST enforcement to verify taxable vs. exempt inflows before notices and simplified rules with few digital tools or staff training. Promote the Merchant Discount Rate (MDR) on UPI transactions for sustainability, promoting digital payment by 2028 in emerging economies.

Impression of RBI’s Digital Lending Guideline

RBI’s Digital Lending Directions, 2025, effective from November 1, 2025, combines prior rules to boost borrower protection, transparency and accountability for Regulated Entities (Res) and Lending Service Providers (LSPs) by setting clear norms for data privacy, fees, recovery, and disclosures in digital loan apps, ensuring fair practices, prohibiting dark patterns, requiring app registration on Centralised Information Management System (CIMS) portal, and capping Default Loss Guarantees (DLG) at 5% with 120-day invocation. Before the RBI’s 2025 Digital Lending Directions, unregulated fintech apps exploited borrowers with outrageous interest rates, hidden fees, and acquisitive recovery tactics like harassment, extortion, and blackmail, leading to suicides and eroding trust in India's digital economy.

Recommended Policies for Sustainable Growth

Identifying Issues

Understanding from the Digital Lending Direction 2021’s Working Group report addressing unfair loan practices, data misuse, and regulatory gaps, which has now recommended consolidating norms for borrower protection, transparency in disclosures, and oversight of Lending Service Providers. It includes calls for Digital Lending Guideline caps at 5% direct fund flows without settlement, and Centralised Information Management System (CIMS) portal registration for Digital Lending Application (DLA) to reduce harassment and fraud.

Major Policy Shifts Implemented

Expanded scope to All-India Financial Institutions (AIFIs) like NABARD/SIDBI, reduced the cooling-off period to 1 day for all loans, and mandated redressal via RBI-CMS with data localisation. Digital Lending Guideline has been banned for revolving credits/P2P loans, required precise borrower consent for credit limit hikes, and prohibited dark patterns in multi-lender platforms.

Operational and Compliance Reforms

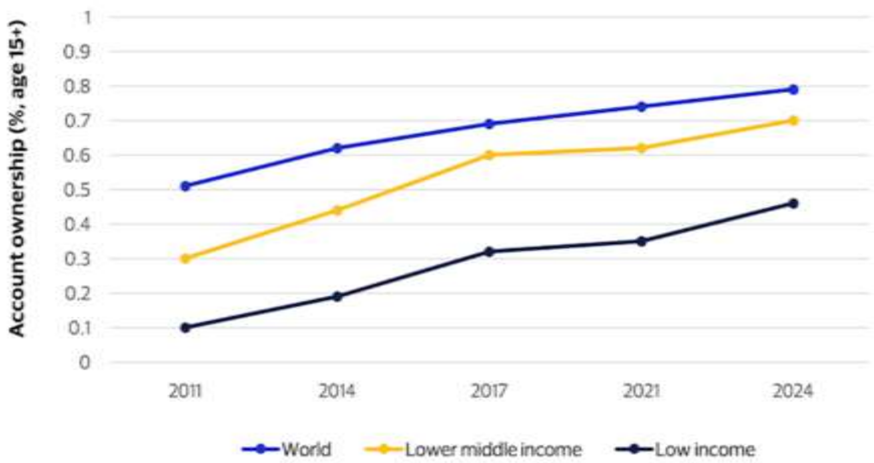
Regulated Entity must audit Learning Service Providers and ensure Key Fact Statement before agreements, phasing out unclear algorithms for fair loan matching. These address pre-FY issues like unethical recovery and privacy breaches, fostering trust in India’s digital credit market.

Data Interpretation

The increasing speed of digitalisation around the globe has continued to remodel various sectors, fostering innovation and consumer convenience. In the payments sector, more accessibility has enabled greater adoption of digital payment services. Development in technology has also enabled increasingly fast and secure ways to pay.

The Global Findex Database 2025, which the World Bank released in July, confirms that the use of financial services with respect to technology has been on the rise. The report was launched in 2011 and updated every three years. The Global Findex database has been collected through worldwide survey data to record a database of measures on how people save, borrow, make payments, and manage risk using financial services. The database provides valuable insights into trends in financial inclusion and opportunities to expand financial access towards the emerging economy.

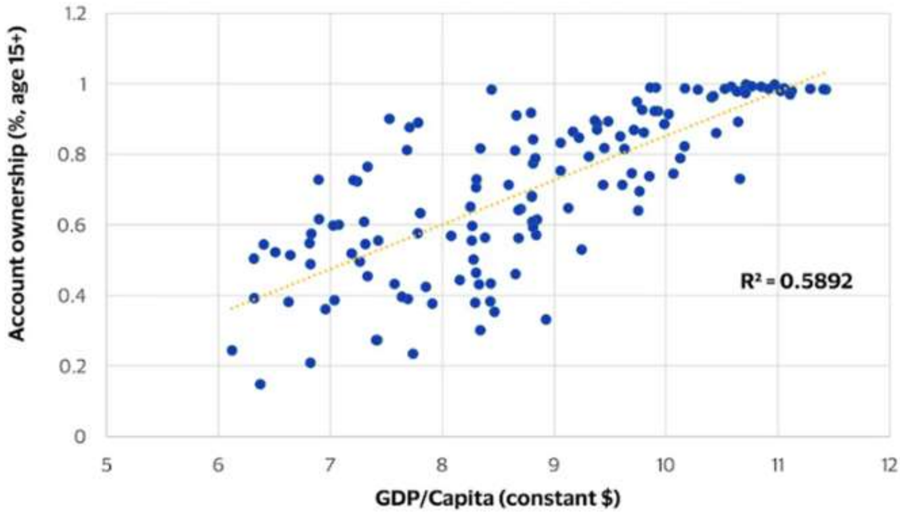
Chart 1: Shows an increase in the rate of global financial account ownership



Source:https://corporate.visa.com/en/sites/visa-economic-empowerment-institute/world-bank-global-findex-2025-insight.html

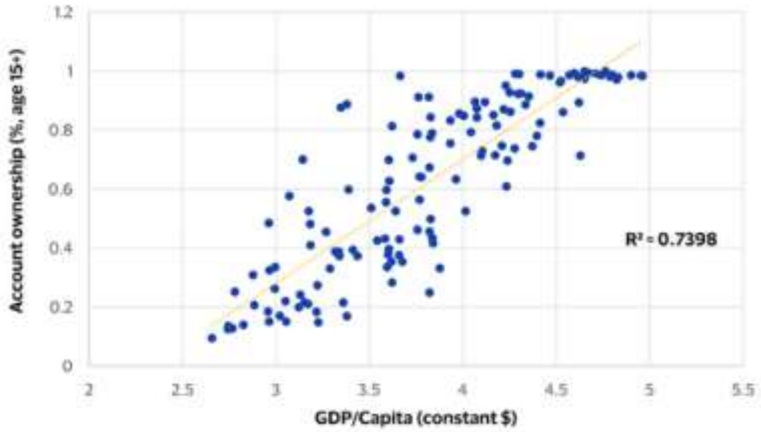
The latest World Bank Global Findex data shows that global financial account ownership grew from 51% of the adult population in 2011 to 76% in 2021 and to 79% in 2025.

Chart 2: GDP/Capita and FI Account Ownership, 2024



Source:https://corporate.visa.com/en/sites/visa-economic-empowerment-institute/world-bank-global-findex-2025-insight.html

Chart 3: GDP/Capita and Any Account Ownership, 2024



Source:https://corporate.visa.com/en/sites/visa-economic-empowerment-institute/world-bank-global-findex-2025-insight.html

Based on 2025 Findex data analysis, there appears to be a difference in correlation between GDP per capita and financial institution (FI) accounts compared to the correlation between GDP per capita and any account, Charts 2 and 3. This suggests that the financial sector provides only a limited range of services, which may not contribute much to the overall economy. Still, it also highlights the need to create policies and financial products designed around the specific needs and habits of different customer groups to achieve better economic results.

Future Prospective

The Global Findex 2025 data reflect inspiring achievements in digital and financial inclusion. The average worldwide rates of ownership of mobile phones and financial accounts are 86% and 79%, respectively, and represent significant development successes, as do the notable increases in rates of formal saving and use of digital payments, which contribute to emerging economies.

The report underlines two major challenges despite the progress made in fintech inclusion. The first challenge is that a large group of the global population are insufficient for the digital economy and formal financial systems. Over 850 million adults, including 325 million, still do not own a mobile phone, and many others only have basic devices, limiting their ability to participate in digital finance or earn through online platforms. Dealing with this issue not only requires providing free phones; it demands a systematic approach that includes affordable devices, an improved network framework, digital literacy, and addressing community attitudes toward technology. Moreover, half of the world's 1.3 billion unbanked adults are settled in a small set of countries, each with difficult economic and regulatory contexts, implying that solutions effective in countries like India or China may not work in smaller economies with low inclusion rates. Special strategies are also needed for those without both accounts and mobile phones, as they remain disconnected from the most effective channels for financial inclusion.

The second challenge concerns financial health. Although access to financial services has increased over a period of time but many people continue to face financial insecurity, struggling to meet daily needs, handle emergencies, or save for the future. Global data show that little improvement is needed in financial resilience, and also disclose a need to help individuals build short-term stability alongside long-term financial security. Furthermore, extending mobile access or services related to it could help bridge these gaps by expanding digital financial services to more people, enabling them to use formal savings, credit, insurance, and digital payments. However, actual progress requires coordinated efforts from governments, financial providers, and policymakers to align regulations, strengthen consumer protections, and design products that match people's real-world needs. Such initiatives would make financial systems more inclusive and capable of supporting sustainable economic participation and long-term well-being.

Conclusion

Fintech has a life-changing potential in emerging economies, exhibited by UPI's role in formalising MSME transactions and RBI's guidelines by limiting exploitative lending, underscoring progress toward 79% global financial inclusion, yet it reveals constant tension from the rapid increase in tax enforcement and prior regulatory gaps. The Bangalore UPI tax case demonstrates how digital trails expose the informal sector to GST research, reducing margins and reversing adoption gains, while pre-2025 fintech immoderation, like harassment, reduces borrower trust and amplifies systemic risks. Eventually, targeted reforms- raising GST thresholds to a certain limit, enhancing MSME credit via a few crore guarantees and enforcing transparency- will mitigate these issues, ensuring Fintech sustains GDP contribution from MSMEs and the underserved population without holding back innovation.

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Conflicts of interest
The authors declare that there are no conflicts of interest regarding the publication of this paper.

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