

Taking P2P Online Lending as An Example

-- Reflecting On the Development of Internet Finance Based on Regulatory Mechanisms

Yuancheng Huang^{1,*}

¹Business school, Zhejiang Wanli University, Ningbo, Zhejiang, 315100, China

*Corresponding author's e-mail: AnckinHuang@outlook.com

Abstract: This paper is based on the critical reflection of P2P online lending, with the supervision mechanism as the main analysis Angle, credit assessment and risk prevention and control as the auxiliary to carry out the discussion of P2P online lending, hoping to provide more thinking for the future development of China's Internet + finance. The main research method adopted in this paper is case study, mainly based on typical cases at home and abroad to carry out analysis. After case analysis, the conclusions are as follows: 1. In terms of supervision mechanism: (1) Let the platform and the bank reach a commercial cooperation relationship. (2) When the debt relationship is formed, it is suggested to sign smart contracts. (3) When the debtor registers as a user on the platform, it can use the bank to evaluate the assets and liabilities. (4) The platform can also learn from the Dutch supervision mechanism for creditors on the Internet platform. 2. In terms of credit evaluation, China can build a credit evaluation system belonging to Internet finance in the credit investigation system of the People's Bank of China. 3. In terms of risk prevention and control, default records should be synchronized with banks and default costs should be raised.

Keywords: P2P online lending; Internet finance; Supervision mechanism; Credit evaluation; Risk prevention and control.

1. Introduction

With the central bank promoting the digital RMB to start trial operation in pilot cities in China, and it is also widely used during the Mid-Autumn Festival and National Day holidays, Internet + finance has entered a new stage. Looking back at the development of Internet + finance in China, P2P online lending can be said to be a leading example. The failure experience and success can provide reference for the further development of digital RMB. Although P2P online lending, as a new financial instrument, has the characteristics of rapid lending and relatively low entry threshold, allowing more ordinary people to access inclusive finance and providing a faster financing channel for small and medium-sized enterprises, it is not difficult to find that it has gradually become an experimental site of opportunism in the explosion incident after the rapid development momentum. After analyzing the typical mine explosion event, insufficient supervision mechanism, insufficient credit evaluation and inadequate risk prevention and control are important factors inducing such events. This paper will focus on the discussion of supervision mechanism, credit assessment and risk prevention and control as a supplement to carry out the discussion.

2. P2P Network Loan Case Specific Problems Review

2.1. P2P network loan concept and its evolution track

Although P2P online lending originated in the United Kingdom in the 1990s, it really began to develop in the international capital market in the United Kingdom in 2005. At the beginning of its operation, this mode overcomes the disadvantages of traditional financial intermediaries such as asymmetric bank information and long loan cycle of the

borrower, and can help small and medium-sized enterprises alleviate the difficulties in using short-term funds.

The introduction of P2P online lending to China was marked by the establishment of PPDai in Shanghai in 2005, and related companies have mushroomed in the Chinese market. From 2013 to 2015, P2P online lending entered a stage of rapid development in China, but problems gradually emerged during this stage, and the regulatory mechanism was the main aspect of these problems.

2.2. The case of the development of P2P online lending in China

In the development process of P2P lending in our country, although many website operators are illegal fund-raising for the purpose, such as the explosion of Jingyi wealth, but there are also more excellent websites, such as Renren loan. The following content takes the two websites as a reference to analyze their outstanding and inadequate parts in the supervision mechanism.

First of all, on the outstanding side, take Renrendai as an example. Renrendai was founded in 2010 and received 130 million US stock A round of financing in 2013. In addition, Renrendai is also a council member of the Internet Finance Association of China. In terms of supervision mechanism, it can make excellent achievements because the platform will conduct credit review on the users who apply for loans, and evaluate them according to the personal credit risk analysis system after the verification of the information. Only after passing the review will the customers' loan needs be displayed and recommended to the lenders on the platform.

Secondly, on the side of relative failure, it takes Jing Yi Wealth as an example. The explosion of the website can be seen as the founder of the platform used the platform to achieve the purpose of running money away, exaggerating the investment and income of the actual project to attract investors, false publicity and fake projects to attract more

investors to inject funds. In the three dimensions of investors, debtors and admission projects have failed to do strict supervision, to a large extent created the Jingyi wealth explosion event.

Finally, some scholars have noticed that the online loans realized by P2P are realized under the online loans without mortgage or guarantee. If the borrower and the borrower enter the

litigation process, the evidence they can enumerate is electronic data, and its authenticity is the key factor affecting the court's decision. The fidelity of electronic evidence and the amount

claimed by both parties are more difficult to determine. [1]

2.3. Successful cases of P2P online lending in foreign countries

At present, the supervision mechanism of P2P online lending in foreign countries has also made great progress. Some countries in the European Union (such as the Netherlands), the United States and Indonesia have integrated their regulatory mechanisms into the operation of P2P lending platforms. Here are the detailed measures taken by each country.

First of all, when dealing with the problem of P2P platforms, the Netherlands has refined the supervision mechanism for platforms and creditors. They set an investment ceiling for creditor investment projects, actively confirm and review through email when selecting investment projects, and the real capital transaction can only be reached after it has been standing on the platform for a period of time. In addition, countries represented by the United States have taken a series of measures such as online restrictions on the loan interest rate and return rate on P2P platforms to ensure the interests of the platforms while taking into account the interests of both donors and recipients. [2] Thirdly, the current P2P platform in Indonesia is also a sign of vigorous development, and the factors of rapid development can be attributed to the relative perfection of Indonesia's own regulatory mechanism. (On the one hand, authorized platforms are regularly evaluated, and if they fail to pass the assessment, the right to operate is withdrawn. On the other hand, it evaluates whether the borrower can repay within 90 days.) And Indonesia has set up a central financial evaluation system called SLIK (Financial Information Services System) and Pusdafil (Fintech Loan DataCenter). These two systems can be used to assess online credit risk.

3. A Case Study of P2P Online Lending

In the author's opinion, the reasons why P2P online lending is difficult to effectively serve small and medium-sized enterprises in China will be discussed from three dimensions: the shortcomings of Chinese national character, the effective design of regulatory mechanism and the comparison between home and abroad.

First of all, there is a shortcoming in the dimension of Chinese national character that hinders the development of this model either explicitly or implicitly. Its disadvantage is that the users who participate in P2P online lending for the purpose of speculation and short-term realization do not want to consider long-term stable development, that is, to earn excess returns with a low level of funds. As a result, most of the founders of the platform and the creditors and debtors registered as platform users expect to achieve rapid financing

in a short period of time to alleviate the difficulties in using funds.

Secondly, if we compare Renrendai with Jingyi Wealth, the loss of regulatory mechanism is a factor that cannot be ignored. The supervision mechanism of Renrendai is divided into two steps, first credit review and then risk review. The effective implementation of these two steps can filter out a part of potential defaulters for the platform, thus reducing the probability of debtors' default or faithless behavior. On the other hand, Jingyi Wealth has not made strict screening and selection of those who are eager to use funds immediately after the introduction of the project, so the loss of supervision mechanism has laid the groundwork for its subsequent "explosion". At the current level of domestic academic research, in her paper "Research on Credit Risk and Prevention of P2P Online Lending", Dr. Quan Ying elaborated that the digital assessment model of Credit Risk+ has high credibility for users' credit assessment. In particular, this model can effectively predict the default risk of debtors [3]. If this analytical model can be effectively combined with P2P online lending platforms, it can, to a certain extent, help the platform evaluate the credit of users and improve the supervision mechanism for debtors.

Thirdly, when we further enlarge the perspective, if we compare the domestic P2P online lending platform with the foreign platform, we can positively confirm that this behavior can be combined with the specific situation in China. Positive confirmation means that when one party holding funds decides to invest in the other party through the online lending platform, the platform will send an email to the investor to confirm this behavior. If the investor confirms this behavior, he needs to reply to the platform and will flow to the investee at a certain interval. In this way, not only can the investor re-evaluate whether the investment behavior is reasonable and can bear the corresponding risk to a certain extent, but also allow the investor to withdraw the investment during the interval.

4. My humble Opinion on The Development of Internet Finance

After reviewing and analyzing the situation of P2P online lending platforms at home and abroad, the author tries to put forward measures that can be further implemented based on the specific national conditions of China from the relatively successful platforms in domestic development and the effective measures that have been implemented abroad. The proposal mainly focuses on the regulatory mechanism, credit evaluation and risk prevention and control of China's Internet + financial platforms in the future:

4.1. In terms of the supervision mechanism of Internet financial platforms

(1) Allow the platforms to reach commercial cooperation with banks. The platform shall pay a certain cooperation fee to the bank, and the bank shall provide the platform with credit consulting services. The cooperation enables the platform to check the credit status of registered users, and synchronizes the default record to the bank once the user defaults. (It can be used as a reference with Renrendai)

(2) When the debt relationship is formed, it is suggested to sign smart contracts (the technical feasibility and application scenarios have been discussed in the papers of Wang Wenhui and Chen Xianzhong). [4] The benefits of smart contracts can

be discussed from two aspects: one is the regulatory efficiency of the government, and the other is the benefit of creditors. The smart contract relies on the characteristics of blockchain technology distributed ledger, which allows the government to intervene in supervision when forming each node. Once suspicious transactions are found, they can intervene in investigation or become evidence. From the perspective of the benefit of creditors, if the debtor defaults, creditors can use this method to claim their legitimate rights and interests to the court.

(3) Before the debtor registers as a user on the platform, it can use the bank to evaluate the assets and liabilities. When the debtor proposes a financing plan, on the one hand, it can first stand on the platform for about 20 days to prevent irrational financing and later failure to repay debts. On the other hand, it can allow the platform to show the liabilities of users who have been

investigated by the bank for endorsement in the early stage. If the platform finds that the user's debt is too high or the bad credit record is too high through the bank in the early stage, it cannot allow the user to become a platform user.

(4) The platform can also learn from the supervision mechanism of the Netherlands for creditors on the Internet platform, which can protect the rights and interests of creditors to a certain extent (in the early P2P platform explosion incident, investors believed that the return rate of investment was high and blindly followed the investment regardless of the risk, resulting in the failure to recover funds in the later stage). The aspects that can be used for reference include: Investment restrictions (e.g., a hierarchy of the amount of online investment that can be made on an Internet finance platform each year based on an investor's annual income), active confirmation and cancellation options (if an investor decides to invest in a certain project, the investor should confirm the action by email, and then reply to the platform by email when the investor has confirmed the investment method). , asset segregation (platform assets, borrower assets and lender assets should be segregated.)

4.2. In terms of credit evaluation of Internet financial platforms

China can build a credit evaluation system belonging to

Internet finance in the credit investigation system of the People's Bank of China, and establish a general mechanism based on the scoring logic of FICO scoring system in the United States and the credit investigation system of online financial platforms in Indonesia (the main criteria are the length of previous credit use, the number of new credit accounts opened, and the type of credit normally used). The weighted average is used for the calculation. The weights assigned to each category can be provided by the government after investigation, and then each platform adjusts the weights based on its own business). On this basis, the Credit Risk+ model can be used to assess the approximate default risk of borrowers.

4.3. In the prevention and control of Internet financial platforms

After reaching commercial cooperation with banks in the early stage, the platform should raise the default cost to some extent, which can include fines after contract default, and can also synchronize with the bank to restrict the debtor's more loans and lower the debtor's credit rating.

5. Outlook

As our country gradually enters the Internet + era, the Internet + finance also becomes a great trend of financial development. If the digital RMB is further integrated with the blockchain technology, China's financial industry will enter a new era. When we gradually improve the combination of the regulatory mechanism in the Internet + financial industry, the field will be greatly developed.

References

- [1] Xiao, J., and Liu, D. (2015) Legal procedures related to online lending disputes: Study on P2P lending regulation. *Renmin Chinese L Rev.*, 3(92):106-112.
- [2] Tanja, J. (2018) Legal challenges of P2P lending. *Nordic Journal of Commercial Law*, 231-260.
- [3] Quan Y. (2018) Research on credit risk and prevention of P2P online lending. Thesis of Northeast Normal University.
- [4] Wang, W., Chen, X. (2019) Blockchain solution of P2P online lending. *People's Forum*, 07:78-79.