Crypto Literacy in Peer-To-Peer Lending

by

Laura Gonzalez - California State University, Long Beach

One fintech innovation that has emphasized its intention to democratize finance since inception in 2005 is peer-to-peer lending (P2P). P2P lending platforms facilitate lending to strangers online, and although the institutional participation is growing, the retail participation also keeps growing. Allied Market Research has reported a 2019 global P2P market of $67.93 billion, with a 2027 projection to reach $558.91 billion (Allied, 2020). Overall, P2P services are convenient, but financial inclusion is limited (Gonzalez, 2023).

Besides financial inclusion goals, fintech firms introduce much appreciated financial education that intends to decrease risk aversion and increase client base. Just in May 2021, for example, award-winning *social investment* app Invstr announced a partnership with Vast Bank and Coinbase. The official announcement title reads: "*Financial education & investing app* offers commission-free crypto trading through a nationally regulated bank*, providing additional trust for new investors in the crypto economy*". In addition, the official statement said: "We are delighted to be working with Vast Bank and Coinbase to offer everyone all the *fun*, *social engagement, financial education*, convenience, and security of Invstr with the comfort of holding crypto in a US bank and the liquidity of Coinbase. For many people, investing in crypto currencies is a *big leap of faith*. Our partnership with Vast Bank and leveraging Coinbase's exchange platform *reduces the perceived risk* of investing in crypto currencies and should *encourage many more people to take the plunge* for the first time" (Invstr founder and CEO, Kerim Derhalli).

The 2008 and 2020 crises reinvigorated discussions on the democratization of finance. Peer-to-peer (P2P) lending is a valuable option worldwide, but credit risk is high. To encourage investors, P2P platforms use blockchain and the option of crypto as collateral. This study examines lender views on crypto and options to effectively support financial literacy and inclusion. It considers 663 pro-social lending decisions by finance students on a mock P2P site where testimonials conditioned participants towards pro-social decision making. After making three lending decisions, participants were asked about changes in the case of different collaterals. Overall, pro-social P2P lenders find crypto riskier than traditional collateral. More specifically, loan applications can be funded more quickly with a pledge of 20% in traditional collateral but not in crypto assets or crypto currency. Furthermore, loan popularity among other lenders also persuades investors, and lender projections of financial literacy influence decision confidence, unlike traditional collateral. Thus, crypto collateral options in P2P platforms do not seem to support financial inclusion. However, upcoming more stable digital currencies backed by central banks are arguably more likely to be considered reliable collateral. This would effectively democratize P2P lending provided there is behavioral financial literacy as well.

References

Allied Market Research (2020), "Peer-to-peer lending market", available at: https://www.alliedmarketresearch.com/peer-to-peer-lending-market (accessed 27 July 2021)

Gonzalez (2023), "Doing Well While Doing Good?: Gender Effects in Pro-Social Peer-to-Peer Lending", Managerial Finance, Vol. 49 No. 4, pp. 661-678, https://doi.org/10.1108/MF-07-2021-0352