Financial and Economic Risk in Developing Markets
Volume 1, Number 2, 2022

Financial Technology and Financial Inclusion in Indonesia: Opportunities and Challenges

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Abstract

Article history:
Received: August 19, 2022
Revised: September 18, 2022
Accepted: October 17, 2022
Published: December 30, 2022

Keywords:
Digital Financial Literacy,
Financial Inclusion,
Financial Technology (FinTech),
MSMEs,
OJK Regulations.

Identifier:
Zera Open
Page: 107-126
https://zeraopen.com/journal/ferdm

This study aims to analyze the role of Financial Technology in encouraging financial inclusion in Indonesia by using qualitative-based conceptual research methods and literature review. The background of this research is based on the rapid growth of FinTech that offers digital financial service innovations, such as online payments, peer-to-peer lending, and online investments, which can reach unbanked and underbanked groups. The results of the literature review show that Financial Technology contributes to the expansion of formal financial access, the empowerment of micro, small, and medium enterprises, as well as increased access for vulnerable groups such as women. However, the challenges that arise include the digital divide, low financial literacy, consumer protection issues, and the dynamics of the relationship between Financial Technology and traditional financial institutions. Therefore, the success of FinTech is highly dependent on adaptive regulation, increased digital financial literacy, and multi-stakeholder collaboration. The research is expected to make a theoretical contribution to the literature on FinTech and financial inclusion, as well as practical benefits for regulators, industry players, and society. Thus, FinTech has the potential to become the main instrument to support inclusive and sustainable economic development in Indonesia.

1. Introduction

The development of digital technology has brought significant changes in the landscape of the global financial industry. Financial Technology (FinTech) is one of the disruptive innovations that accelerate the transformation of financial services, including digital payments, peer-to-peer (P2P) lending, online investment, and application-based financial management. The existence of FinTech not only increases transaction efficiency, but also expands people's access to formal financial services, so it has great potential in driving financial inclusion. In various countries, FinTech has proven to play an important role in bridging groups of people who were previously unbanked to gain access to modern financial products.

In the Indonesian context, the development of FinTech shows very rapid growth. Supporting factors include increasing internet penetration and smartphone ownership, a young population that is technologically literate, and regulations from the Financial Services Authority (*Otoritas Jasa Keuangan* /OJK) that are increasingly adaptive. OJK noted that the number of licensed FinTech operators continues to increase every year, indicating positive dynamics in the digital ecosystem. In line with this, the National Survey on Financial Literacy and Inclusion (*Survei Nasional Literasi dan Inklusi Keuangan* /SNLIK) also shows an increase in the financial inclusion index, although there is still a gap with the financial literacy index (Hasan et al., 2021). This means that even though access to financial services is increasingly open, public understanding of financial products is still limited.

Academic literature confirms that FinTech has a real contribution to encouraging financial inclusion in Indonesia. Agustia and Anridho (2020) show that digital financial services have helped expand the reach of traditional banking services, especially in areas with limited physical infrastructure (Agustia & Anridho, 2020). Furthermore, Saraswati et al. (2020) revealed that the level of financial inclusion affects the effectiveness of monetary policy in Indonesia, where FinTech penetration can strengthen the transmission of macroeconomic policies (Saraswati et al., 2020). This shows that the existence of FinTech not only has an impact on the micro aspect, but also on the stability of the national economy.

In addition, FinTech has proven to be able to have a positive impact on the small and medium enterprises (SMEs) sector. Hamidah et al. (2020) emphasized that the combination of FinTech, financial literacy, and financial inclusion improves the financial performance of SMEs in Indonesia, especially in overcoming limited access to financing from conventional banking institutions (Hamidah et al., 2020). During the COVID-19 pandemic, research by Natile (2019) shows that FinTech plays an important role in expanding financial access for women, who are often marginalized in the formal financial system. This confirms FinTech's role as a catalyst for more inclusive and gender-equitable financial inclusion.

However, the development of FinTech in Indonesia also faces a number of challenges that need to be considered. First, there is still a digital gap between urban and rural communities, where internet access and technological literacy are not evenly distributed. Second, the consumer protection aspect is a crucial issue, considering that there are still many cases of fraud, data misuse, and illegal online lending practices. Third, the synergy between FinTech and traditional financial institutions still needs to be improved, in order to create a financial ecosystem that complements each other and does not compete destructively with each other. Setiawan et al. (2021) emphasized that FinTech adoption among SMEs is influenced by trust, ease of use, and regulatory support, so a collaborative strategy is needed between regulators, industry players, and conventional banking.

Based on these problems, this study aims to describe the role of FinTech in promoting financial inclusion in Indonesia, as well as identify the opportunities and challenges that come with it. In addition, this study also aims to provide an overview of the potential synergies between FinTech and conventional financial institutions in creating a more inclusive, secure, and sustainable financial ecosystem. Theoretically, this research is expected to contribute to the literature on the relationship between FinTech and financial inclusion, especially in developing countries such as Indonesia. Practically, the findings of this study can be an input for regulators such as the OJK, FinTech industry players, and the wider community in maximizing the benefits of digital technology in the financial sector. Thus, this research is not only relevant at the academic level, but also has broad policy and socio-economic implications.

2. Literature Review

2.1. FinTech Development and Financial Inclusion

The development of Financial Technology (FinTech) globally has driven the transformation of financial services towards digitalization. Indonesia, with its large population and increasing internet penetration, has great potential in the use of FinTech. FinTech has become an important tool in supporting Indonesia's financial inclusion agenda, which is part of the G20 commitments. Agustia and Anridho (2020) mentioned that FinTech is very effective in reaching community groups that are difficult to access by traditional banking. FinTech also provides innovative solutions tailored to the needs of the local market. For example, digital payment applications that do not require extensive physical infrastructure, are well suited to be implemented in rural areas. In addition, the P2P lending business model provides complicated unconditional access to credit, which is often a barrier in traditional banks (Broccardo et al., 2021).

This finding is reinforced by Loo (2019), who shows that FinTech's contribution to improving financial access in the Southeast Asian region, including Indonesia, is very significant compared to other developing countries. With the development of services such as digital payments, P2P lending, and online investments, FinTech has become a key catalyst for accelerating financial inclusion. These services offer convenience, speed, and more affordable costs, breaking down the geographical and economic barriers that have prevented people from accessing formal financial services. This increase in inclusion is in line with the goal of more equitable economic development.

Despite its positive role, there are still significant challenges to overcome, especially the financial literacy gap. Data from the National Survey of Financial Literacy and SNLIK shows that there is a gap between the literacy and inclusion indexes. People may have access to digital financial products, but many do not yet have an adequate understanding to manage risk or choose the right products. Therefore, although FinTech plays a positive role in the expansion of access to financial services, synergistic strategic efforts are needed to improve consumer literacy and protection. Without sufficient understanding, increased access can pose new risks to society.

2.2. The Role of FinTech for MSMEs and Community Empowerment

FinTech plays an important role in supporting financing and empowerment of micro, small, and medium enterprises (MSMEs). The combination of FinTech and financial literacy significantly improves the financial performance of MSMEs in Indonesia, as found by Hamidah et al. (2020). This shows that financial technology provides access to financing that was previously difficult to obtain through conventional banking. FinTech offers a fast and flexible solution, overcoming bureaucratic and collateral barriers that often stand in the way of MSMEs. In addition, Rosyadah et al. (2021) found that FinTech has a positive influence on the financial inclusion of MSMEs in Makassar. FinTech platforms increase MSMEs' access to credit and other financial services, making transactions more efficient. The availability of these services allows MSMEs to manage funds, make payments, and obtain working capital more easily, which in turn drives the growth of their business.

More than just supporting MSMEs, FinTech also contributes to the empowerment of vulnerable groups, such as women, who often face limited access to formal financial services. Through digital services, women now have greater opportunities to access loans and save, allowing them to start or grow businesses from home. FinTech serves as a more inclusive economic empowerment instrument, not only providing financial solutions, but also accelerating economic participation for all levels of society. Overall, FinTech is a key catalyst for more equitable and inclusive economic growth.

2.3. FinTech Challenges and Synergies with Traditional Financial Institutions

While FinTech offers great opportunities, there are various challenges that must be overcome to ensure its optimal development. Setiawan et al. (2021) identified that trust, regulation, and ease of use are the main factors driving FinTech adoption among Micro, Small, and Medium Enterprises (MSMEs). This shows the importance of synergy between regulators, service providers, and the community so that FinTech adoption is more optimal and sustainable. On the other hand, the relationship between banks and FinTech is also an important issue. Zalan and Toufaily (2017) highlight this dynamic, where the two are sometimes seen as competitors. However, they argue that collaboration between the two can actually create a healthier and more inclusive ecosystem.

This collaboration allows banks to leverage FinTech innovations to reach new customers, while FinTechs can rely on the trust and established infrastructure of banks. In addition to regulatory and collaboration issues, consumer protection is a critical issue. The still rampant practice of illegal online lending and misuse of personal data threatens public trust, which can ultimately hinder the growth of the industry. Therefore, the success of FinTech is not only determined by technological innovation, but also by a strong and adaptive regulatory framework. This framework must be able to ensure transparency, accountability, and consumer protection comprehensively. Without these guarantees, FinTech risks losing public trust and failing to reach its full potential in driving financial inclusion.

3. Methods

This study uses a conceptual approach with a qualitative method based on literature review. The conceptual research aims to analyze the theory, concepts, and results of previous research related to the role of FinTech in supporting financial inclusion in Indonesia. Thus, the focus of the research is not on the collection of field data, but rather on the excavation of theoretical thinking and empirical evidence from various relevant literature. The source of research data comes from academic journals published and available, official reports of the Financial Services Authority OJK, the National Survey of Financial Literacy and Inclusion (SNLIK), and related publications. The selection of sources was made based on the criteria of relevance, novelty, and contribution to understanding the relationship between FinTech and financial inclusion.

Data analysis was carried out by a thematic synthesis method, which is to group the results of the literature review based on the main themes: FinTech development and financial inclusion, the role of FinTech in supporting MSMEs and community empowerment, and the challenges and synergies of FinTech with traditional financial institutions. Each theme is analyzed in depth to find patterns, similarities, differences, and research gaps that can be used as the basis for policy recommendations and further academic studies.

In addition, the validity of the research is maintained through triangulation of sources, namely by comparing the results of academic research with official empirical data from the OJK and SNLIK. In this way, the conclusions produced are not only theoretical, but also reflect the factual conditions in Indonesia. This conceptual research also pays attention to the latest developments in FinTech regulations and practices, making it relevant to the dynamics of the current digital finance industry. Using a qualitative-based literature-based approach, this study is expected to be able to provide a comprehensive overview of how FinTech contributes to financial inclusion in Indonesia, as well as identify opportunities and challenges faced. The results of the research are expected not only to enrich academic treasures, but also to be a practical reference for regulators, industry players, and the wider community.

4. Results

The results of this study are based on a review of the latest literature on the role of FinTech in encouraging financial inclusion in Indonesia. In general, the results of the study show that FinTech has contributed in three main areas: expanding access to finance, supporting the growth of MSMEs, and facing regulatory challenges and consumer protection. This study in-depth explores how these digital innovations have transformed the national financial landscape, bringing significant positive impacts to all walks of life, from individuals to the business sector. FinTech is no longer only seen as a technical tool, but as a strategic instrument to achieve the goal of more equitable and sustainable economic development in Indonesia. This transformation is key to realizing the government's vision to achieve higher financial inclusion.

The development of Financial Technology (Fintech) in Indonesia has made a significant contribution to increasing financial inclusion. Through technological innovation and digital financial services, previously underserved communities can now access various financial products and services (Broccardo et al., 2021). FinTech has proven to be effective in expanding access to finance, especially for people who previously did not have access to formal banking services or are known as the unbanked. Agustia and Anridho (2020) stated that digital financial services are able to reach remote areas in Indonesia, which are difficult for conventional banking institutions to reach due to limited physical infrastructure and high operational costs. The availability of digital services through smartphones or simple internet networks allows individuals in remote areas to make transactions, pay bills, or send money without having to visit a bank branch. The presence of this technology fundamentally changes the way people interact with financial services, eliminating geographical barriers that have been the main obstacles.

This is supported by the findings of Saraswati et al. (2020), who emphasize that financial inclusion through FinTech also strengthens the effectiveness of national monetary policy. By expanding the base of formal financial participation, more and more people are involved in the banking system. This means that the more people access digital financial services, the greater the influence of monetary policy issued by Bank Indonesia on economic stability. For example, policies related to interest rates or other macroprudential instruments will have a wider and more equitable impact on all levels of society, not just limited to groups already served by banks. This increase in participation creates a stronger and more volatile economic foundation, as money circulation and economic activity become more structured and recorded.

In addition, FinTech also facilitates the creation of a more dynamic and competitive financial ecosystem. The emergence of various types of FinTech services, such as peer-to-peer (P2P) lending, e-wallets, and crowdfunding platforms, provides more diverse options for consumers (Horn et al., 2020). This competition encourages traditional financial institutions to innovate and improve the quality of their services. People can now compare various financial products, choosing the one that best suits their needs, both in terms of cost and ease of use. This diversity also drives efficiency in the financial system as a whole, ultimately benefiting consumers with lower costs and better service.

Second, FinTech has a real contribution to the development of MSMEs in Indonesia, which is the backbone of the national economy. Hamidah et al. (2020) prove that the integration of FinTech with financial literacy improves the financial performance of MSMEs. This integration provides easier access to capital and helps small businesses deal with credit limitations from traditional banks that often require guarantees that are difficult for MSMEs to fulfill. Through the P2P lending platform, MSMEs can apply for loans with a faster process, more flexible requirements, and without the need for burdensome physical collateral. This opens up opportunities for MSMEs to develop their businesses, expand market reach, and increase their production capacity.

Rosyadah et al. (2021) also found a positive influence of FinTech on MSMEs in Makassar, where FinTech provides faster and more flexible financial services. This speed and flexibility are crucial for MSMEs that need immediate cash to fulfill orders or address urgent operational issues. Digital payment platforms also make it easier for MSMEs to accept payments from customers, which not only improves transaction efficiency but also creates neater financial records. This research confirms that FinTech can be an instrument for local economic empowerment, especially in the informal sector which has been struggling to get formal financial support. With access to digital financial services, MSME actors can transact more professionally, which ultimately increases their credibility in the eyes of business partners and consumers.

More than that, FinTech also allows MSMEs to adopt more modern business models. E-commerce platforms that are integrated with digital payment services make it easier for MSMEs to market their products to a wider market, even abroad. The ease of managing cash flow and tracking sales through FinTech apps gives small businesses better control over their finances. They can make more informational and strategic business decisions, based on accurate data. FinTech not only provides capital, but also essential management tools for sustainable business growth. From a social perspective, FinTech also drives gender inclusion significantly. A study by Natile (2019) shows that women in Indonesia have benefited significantly from digital financial services, especially during the COVID-19 pandemic. During the pandemic, mobility was limited and social interaction was reduced, making digital services the only way for many people to transact financially.

For women who often play an important role in managing household finances, access to digital loans and savings provides flexibility and security. They can make transactions from home, without having to travel to a bank, which reduces the risk of exposure to the virus and provides a sense of security. With greater access to digital loans and savings, women can improve household economic stability as well as expand their participation in productive economic activities. Digital loans allow women to start or grow small businesses from home, such as online businesses or handicrafts. The ability to save digitally also gives them the tools to manage income and plan for the family's financial future. This financial empowerment not only improves economic well-being, but also strengthens women's social position and gives them greater confidence. FinTech, in this context, acts as a catalyst for gender equality by providing equal and easy access for women to participate in the economy.

Even so, the development of FinTech cannot be separated from the challenges that must be overcome. Setiawan et al. (2021) identified that consumer trust, ease of use, and regulatory support are the main factors in the adoption of FinTech by MSMEs. Without data security and consumer protection guarantees, FinTech's potential will not be optimal. The public and MSME actors are still hesitant to use digital services for fear of their personal data being misused or becoming victims of fraud. Cybersecurity and privacy protection issues are very important to build public trust. In addition, synergy between banks and FinTech is still a prominent issue. Zalan and Toufaily (2017) highlight the importance of collaboration, not competition.

Banks often view FinTech as a competitor that eats away at their market, even though collaboration can create a more inclusive and robust financial ecosystem. Banks can capitalize on FinTech's speed and innovation, while FinTechs can leverage the bank's extensive customer database and network. This collaboration is important to strengthen consumer trust while expanding the range of services. For example, banks can partner with FinTech companies to provide more efficient microlending or digital payment services. The regulatory aspect also plays an important role. Loo (2019) emphasized that the success of FinTech in Southeast Asia is largely determined by government policies in encouraging digital adoption while protecting consumers. In Indonesia, regulations from the Financial Services Authority (OJK) that are increasingly adaptive are a key factor in controlling the growth of the FinTech industry to remain healthy and sustainable. The OJK continues to strive to create flexible rules, which allow innovation to develop without neglecting the safety and protection aspects of consumers.

This is in line with the OJK report which noted an increase in the number of licensed FinTech operators as a form of commitment to creating a trusted digital financial ecosystem. The results of the study show that FinTech has become a major driver of financial inclusion in Indonesia. Through digital innovation, people who were previously not served by banks now have access to formal financial services. FinTech also contributes to the empowerment of MSMEs and vulnerable groups such as women. However, the sustainability of FinTech's role is highly dependent on effective regulation, increased public financial literacy, and collaboration between FinTech and traditional financial institutions. This challenge requires a holistic approach from all parties, including the government, regulators, industry players, and the public, to ensure that FinTech innovations can provide maximum benefits to all Indonesians in a sustainable manner.

5. Discussion

The results of this study confirm that FinTech has a strategic role in expanding financial inclusion in Indonesia, but its implementation is inseparable from various challenges. This discussion outlined three important aspects: FinTech's contribution to financial inclusion, the barriers faced, as well as strategic recommendations for the future. First, FinTech's contribution to financial inclusion is very real. FinTech helps reach unbanked and underbanked groups through digital payment services, online loans, and app-based savings products. These services make it easier for individuals and micro, small, and medium enterprises (MSMEs) who previously had difficulty obtaining formal financial services. This wider access not only increases people's economic capacity, but also creates a fairer and more equitable financial ecosystem throughout Indonesia.

Furthermore, research by Natile (2019) shows that women as a vulnerable group have benefited greatly from access to digital financial services, especially during the pandemic. The ability to transact and obtain loans online provides significant financial autonomy for them, strengthening women's economic position in families and communities. This shows that FinTech not only expands financial inclusion quantitatively, but also supports social equality and gender empowerment. The increase in Indonesia's financial inclusion index from 76.19% in 2019 to 85.10%

shows FinTech's real contribution to the achievement of national targets. These figures reflect the successful collaboration between governments, regulators, and industry in creating an environment conducive to FinTech growth.

Second, there are significant obstacles in optimizing the role of FinTech. Loo (2019) emphasized that regulation and digital infrastructure are the determining factors for the success of FinTech in Southeast Asia. In Indonesia, there are still many regions, especially in rural areas, that face a digital divide. Limited access to the internet and digital devices hinders the equitable adoption of FinTech services. In addition, the rampant practice of illegal online lending and weak consumer protection pose a serious risk to public trust. Many cases of fraud, suffocating interest, and intimidation carried out by illegal online lenders have harmed the public, thus fostering a fear of using FinTech services, even legal ones. Saraswati et al. (2020) also added that although financial inclusion is increasing, the imbalance between literacy and inclusion is still a major challenge. People may have access, but do not have enough understanding to manage digital finances wisely, which could potentially hinder the effectiveness of monetary policy and lead to personal financial problems.

Third, to strengthen the role of FinTech, a synergistic strategy is needed that involves regulators, industry, and society. Collaboration between conventional banks and FinTech companies is essential to create a complementary financial ecosystem, not destructive competition. Banks can leverage FinTech innovations to reach new market segments, while FinTechs can leverage the capital and trust that banks have. Regulators need to ensure a balance between innovation and consumer protection through adaptive policies and strict oversight. Policies that are too strict can stifle innovation, while policies that are too loose can harm consumers. On the other hand, increasing digital financial literacy must also be a priority so that people not only become service users, but also be able to manage existing risks and utilize services optimally. A structured and massive educational program is needed to increase public understanding of FinTech products, the associated risks, and how to protect themselves from illegal practices. Thus, this discussion emphasized that FinTech is an important instrument to expand financial inclusion in Indonesia, but its success depends heavily on adaptive regulation, adequate consumer protection, and increased digital literacy. Multi-stakeholder collaboration is key to creating an inclusive, secure, and sustainable digital financial ecosystem.

6. Conclusion

This study concludes that FinTech plays a significant role in encouraging financial inclusion in Indonesia, especially through digital payment services, P2P lending, and alternative financing solutions for MSMEs. The presence of FinTech not only expands formal financial access for previously unbanked communities, but also supports the empowerment of vulnerable groups such as women and micro-entrepreneurs. These findings confirm that FinTech is able to function as an instrument of socio-economic transformation that strengthens people's economic resilience. Nevertheless, the development of FinTech in Indonesia is inseparable from challenges. The digital divide, low financial literacy, and consumer protection issues are still the main obstacles. In addition, the dynamics of the relationship between banks and FinTech also demand closer synergy in order to create an inclusive and sustainable financial ecosystem. Adaptive regulations from the OJK and the government's efforts to improve digital literacy are important factors in overcoming these obstacles.

Theoretically, this study contributes to the literature on the role of FinTech in financial inclusion in developing countries. Practically, the results of this study provide input for regulators, industry players, and the public regarding strategies for optimizing the role of FinTech. Key recommendations include increasing digital financial literacy, strengthening consumer protection regulations, and close collaboration between FinTech and traditional financial institutions. With these steps, FinTech is expected to continue to be a driving force for financial inclusion in Indonesia, while supporting the achievement of sustainable development goals through more equitable, equitable, and sustainable access to finance.

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