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- Bowersox, Donald J., Closs, David J., (1996), "Logistical Management." Tata McGraw, Hill, New Delhi.
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PAYMENTS BANKS IN INDIA: A STIMULUS TO FINANCIAL INCLUSION

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ABSTRACT

The Government of India have been making rigorous efforts to promote financial inclusion. Continuous need has been felt to review & revolutionize the present banking set up. Payment Banks are a step in this direction. Dr. Nachiket Mor Committee (September 2013) proposed to set up Payments Banks. RBI gave approval to 11 applicants out of 41 applicants, based on criteria like infrastructure, banking penetration, popularity, technology and past experience in their respective domain like postal offices, telecom service provider (TSPs), mobile wallet, banking services, consumer goods, business correspondence. Payment banks are aimed at providing small savings accounts, meet payments and remittance needs of small businesses, unorganized sector, low income households, farmers and migrant work force. These new kind of banks are designated to reach people outside the ambit of formal banking services. This paper attempts to review business model of payment banks.

KEYWORDS
payments bank, financial inclusion, rural banking, small savings accounts.

1. INTRODUCTION

Traditionally, India has been cash dominated economy. There has been limited penetration of formal banking and financial services. Access to formal financial services such as remittance, micro credit has been extremely limited especially for the low income groups in India, because banking sector considers high cost of acquisition associated with small amounts transactions. Thus these low income segments of population are either deprived of access to such services or approach unorganized service providers and avail these services at steep rates.

The Government of India and Reserve Bank of India have been making rigorous efforts to promote financial inclusion and financial access in India.

To study 'Comprehensive financial services for small businesses and low income households' RBI constituted a committee headed by Dr. Nachiket Mor in September 2013. The purpose was to suggest solutions to address the needs of financial inclusion in unbanked and under-banked segments of the society in sustainable way. The committee submitted its report in January 2014. One of the prime recommendations of the committee was to introduce Payments Bank. These will be specialized banks catering to financial services needs of niche area. The report also suggested criteria to assess 'Fit and Proper' status of the Payments bank license aspirants.

2. OBJECTIVES OF THE STUDY

1. To scrutinize the need of Payments Bank in India.
2. To examine the strengths, weaknesses, opportunities & challenges of Payments Bank in India.
3. To analyse how will 'payments banks' change the Economic landscape in India.
4. To study Business model of Payments Banks.

3. METHODOLOGY OF THE STUDY

The kind of research conducted here is exploratory research. Information has been collected from various secondary sources to study the potentiality of payments banks and its effect on changing the payment landscape of India and justify the above mentioned objectives.

4. APPROVED COMPANIES FOR PAYMENT BANKS

On 19 August 2015, the Reserve Bank of India gave "in-principle" licences to eleven entities to launch payments banks:

1. **ADITYA BIRLA NUVO LIMITED**

Payment bank is joint venture between ABNL and Idea Cellular (51:49).

2. **AIRTEL M COMMERCE SERVICES LIMITED**

Bharti Airtel owns 80% of Payments Bank unit and Kotak Mahindra Bank holds the rest. It is the first of its block to launch payment bank on 12th January 2017, aiming at taking banking services to those who are outside the ambit of payments bank.

3. **CHOLAMANDALAM DISTRIBUTION SERVICES LIMITED**

It has abandoned its plan to set up a Payments Bank considering Competition and long gestation period to become profitable.

4. **DEPARTMENT OF POSTS (INDIA POST PAYMENTS BANK)**

It is Incorporated as a Public Sector Bank under the Department of Posts with 100% GOI equity, IPPB has launched on January 30th, 2017.

5. **FINO PAY TECH LIMITED**

ICICI bank has partnered with FINO to venture into Payments bank. ICICI Group owns a 20 per cent stake in the bank.

6. **NATIONAL SECURITIES DEPOSITORY LIMITED**

NSDL, the biggest security depository, has plans for launching up Payments bank within 2017 under managing director and chief executive GV Nageswara Rao.

7. **RELIANCE INDUSTRIES LIMITED (JIO PAYMENTS BANK)**

Reliance Industries Limited (RIL) has entered into partnership with State bank of India (SBI) for Payments Bank. SBI will be the joint venture partner with equity investment of30% and RIL is the promoter having 70% stake in venture.

8. **SHRI DILIP SHANTILAL SHANGHVI, FOUNDER OF SUN PHARMACEUTICALS**

Payment bank was a planned partnership between Shri Dilip Shantilal Shanghvi, founder of Sun Pharmaceuticals (41%), IDFC bank (20%) and Telenor (39%). But now they have opted out their plans.

9. **SHRI VIJAY SHEKHAR SHARMA, CEO OF PAYTM**

Paytm Payments Bank started its operations on 23rd May 2017. Renu Satti is the CEO OF Payments bank. Bank will partner with insurance companies and various lenders and make them available to customers and small businesses.

10. **TECH MAHINDRA LIMITED**

The bank was planned to be an independent unit under Mahindra Group led by Mahindra Finance and Tech Mahindra. But now it has opted out.

11. **VODAFONE M-PESA LIMITED**

Vodafone had issued open mandate to bankers to find best partner. But because of planned merger of idea cellular and Vodafone, Vodafone would surrender its in principle license as it cannot compete with Aditya Birla Nuvo, which owns idea cellular, which also has a banking licence. The major reason for Vodafone to surrender would be its foreign ownership. Vodafone India is wholly owned subsidiary of its UK parent and it needs to reduce it to less than 50%, to be able to set up a payments bank

The "in-principle" licence was valid for 18 months within which the entities had to fullfill the requirements. They were not allowed to engage in banking activities within the period. The RBI after being satisfied that the required conditions have been fulfilled will grant full licences under Section 22 of the Banking Regulation Act, 1949.

5. OBJECTIVE OF SETTING UP OF PAYMENTS BANKS

Financial inclusion is the primary objective of setting up of payment banks. They should help the financial inclusion by

a. Opening of small savings account and enabling high volume-low value transactions in deposits.
b. Smooth and easy payment/remittance services to migrant labourers, small business people, low income households and other unorganized entities etc.
c. Secured Technology driven environment

6. BUSINESS MODEL OF PAYMENTS BANKS

- Financial inclusion is the key objective of these banks and unbanked & under-banked segments of Indian population are the priority target market.
- RBI does not visualize a Payments Bank to become virtual or branchless bank, however internet banking services has been encouraged.
- Cost to serve unbanked & underbanked population is lower due to technology adoption right from the very beginning.
- Fee earned from various transactions (like deposit, remittances etc.) is primary product for revenue generation. It is doubtful that payments bank will be able to feed on transaction revenues alone. Without diversified revenues, the road to profitability will be difficult.

7. MAJOR REGULATIONS FOR PAYMENTS BANKS

1. The banks should have fully networked and technology driven systems from the inception. They have to conform to generally accepted standards and norms relating to data storage, security and real time data update. Detailed technology plan should be furnished to the RBI. Technology is the backbone and plays a central role across all functions and processes.
2. For the first five years, the promoter's share should be at least 40%.
3. FDI is allowed in Payments banks subject to FDI rules for banking institutes.
4. Minimum capital required for payments bank is ₹ 100 crores.
5. They cannot engage in lending activities. Credit Cards cannot be issued.
6. These banks are not allowed to have subsidiaries for undertaking non-banking activities.
7. The deposits are restricted to ₹ 1,00,000 per customer, but it may be raised by the RBI later on based on the performance of the bank.
8. Appointment of directors will be as per Reserve Bank of India guidelines. Independent directors should have the majority.
9. Voting rights of shareholder have been restricted at 10% which can be raised to 26% by Reserve Bank of India.
10. At least 25% of bank branches must be set up in rural areas.
11. The payments banks will be licensed under Section 22 of the Banking Regulation Act 1949 and will be registered as public limited company under the Companies Act 2013.
12. The bank must use the phrase "payments bank" in its name.
13. The Payments Banks must maintain a leverage ratio of not less than 3% i.e. it's external liabilities should not exceed 33.33% of it's net worth (capital and reserves).
14. **Deployment of funds:** They can hold upto 25% of demand deposit balances in current & fixed deposits with other scheduled commercial banks for operational purposes & liquidity management. Further they have to invest at least 75% of Demand deposit balances in statutory liquidity ratio (SLR) eligible government securities\treasury bills with maturity upto one year.
15. **Minimum capital adequacy ratio to be maintained by the payment banks:** Payment banks are required to maintain a minimum capital adequacy ratio of 15% of its risk weighed assets (RWA) on a continuous basis, subject to RBI guidelines. Tier1 capital should be at least 7.5% of RWAs. Tier2 capital should be limited to a maximum of 100% of total tier1 capital.

8. SCOPE OF OPERATIONS OF PAYMENTS BANK

Payment banks are allowed only certain restricted activities under the banking regulation act, 1949

a. Payment banks can accept current and savings deposits from the individuals, small business and other entities. Non Resident Indian (NRI) deposits will not be accepted. The customers can deposit and withdraw money, use cheque books, transfer funds, buy mutual funds and insurance from payments banks. There will be deposit insurance and credit Guarantee Corporation of India (DICGCI) cover for the deposits. Payment banks can issue Debit card but not credit card.
b. They can issue pre-paid payment instruments (PPIs).
c. Payment banks can offer internet banking and thus leverage technology.
d. Payments bank can act as a business correspondent (BC) of another bank, following RBI guidelines.
e. Payments banks can send or receive remittances (RTGS/NEFT/IMPS) under a payment mechanism approved by RBI.
f. Payment bank can engage in only non-risk sharing simple financial service activities not requiring any commitment of their own funds such as distribution of mutual fund, insurance products, pension product etc. with prior approval of RBI.
g. The payment bank can undertake utility bill payments on behalf of its customers and general public.
h. Subject to RBI approval, Payment banks will be permitted to handle international fund payments or remittances.

9. SWOT ANALYSIS OF PAYMENTS BANK

STRENGTHS OF PAYMENTS BANK

- The business model is very innovative.
- It is spread nationwide and able to cover last mile.
- Banking can be done anywhere and anytime.
- Servicing cost will be lower.
- The customer base will be very large.
- It will work towards furthering the objective of Financial Inclusion.
- It will be highly uneconomical for traditional banks to open bank branches in every rural area but the mobile phones coverage is an economical platform for quickly taking basic banking services to every village. This is the Unique selling proposition of payment banks.
- Payment banks can be very crucial in implementing the direct benefit transfer (DBT) scheme of government, where subsidies on healthcare, education and gas are paid directly to beneficiaries accounts.

WEAKNESSES OF PAYMENTS BANK

- Due to poor networking and internet facility there will be loss of business.
- There is lack of awareness among people on latest technology and products

- It is quite a low margin business.
- Only limited products are being offered. No lending activities will be undertaken. No credit cards will be issued.
- There are issues related to security because of use of internet and technology.
- The payments banks face high costs of compliance associated with the banking regulatory framework
- The banks will need significant capital infusion to meet high ongoing capital requirements.
- They will face high overheads (e.g., technology and personnel) and direct costs (e.g., free ATM withdrawals).

OPPORTUNITIES OF PAYMENTS BANK

- There is immense potential for extensive reach in rural areas.
- Innovative business model will help to offer unique products and services
- Offering right product to right customer at right time.
- New offerings in the form of unique products will help Enhance customer relationship beyond core business.

CHALLENGES OF PAYMENTS BANK

- There is intense competition in banking sector with so many already established banks.
- Payments bank will have a narrower product portfolio.
- India is more of a cash dominated economy.
- Business viability would be a challenge. It is difficult to ensure sustained profitability as cost of acquisition is high. It is likely to be a low profit margin business.
- Technology inexperience amongst general public specifically rural areas will lead to lower acceptance.
- There is lack of awareness amongst unbanked segments for this new model
- Customers may easily switch over between banks, so there will be low customer loyalty.
- Regulatory restrictions exist in form of stringent guidelines issued by RBI.
- Three of the 11 in-principle payments bank licensees have withdrawn their applications, highlighting the investment and commercial challenges of the business model. These are as per following:
  - Cholamandalam Distribution Services Limited
  - Shri Dilip Shantilal Shanghvi, founder of Sun Pharmaceutical
  - Tech Mahindra Limited

10. IMPLICATIONS ON FINANCIAL LANDSCAPE

The major financial implications of Payments Banks in different areas:

1) FINANCIAL INCLUSION OF REMOTE RURAL AREAS: Every rural area citizen with a mobile data connection will be able to avail banking services using the online electronic medium. Thus, digitisation will be the vehicle for banking.

2) ELIMINATION OF BLACK MONEY: By reducing cash transactions Payments bank will help in reduction of black money from the financial Landscape of India.

3) SECURE MEDIUM MINIMIZING THE NEED FOR ATMS: Payment Banks will help in creating cashless economy. Thus gradually the need for Debit / Credit Cards and ATM units will reduce. Thus they will help in saving space which is a scarce resource in cities.

4) EFFICIENT IMPLEMENTATION OF SUBSIDY SCHEMES: Payment banks can be very crucial in implementing the direct benefit transfer (DBT) scheme of government, where subsidies on healthcare, education and gas are paid directly to beneficiaries accounts.

5) BENEFIT TO GOVERNMENT: These banks will benefit the government in acquiring loans at low cost loans because Payments bank can only lend to Government.

6) DIGITAL INDIA CAMPAIGN: They will provide an impetus for creation of Digital India because of the propagation of payments banks will stimulate the need for a digital infrastructure.

7) IMPACT ON TRADITIONAL BANKS: Increasing competition between traditional banks and payments banks will help in reducing the banking costs.

11. FEASIBILITY ANALYSIS OF PAYMENT BANKS

To evaluate the feasibility of Payment Banks**,** the following factors have to be considered:

1) COSTS INCURRED FOR THE PAYMENT BANKS

Rural areas might have limited number of smartphones and mobile data connectivity as well. Thus, the success of these Banks will depend largely on their ability to go beyond the digital medium and reach out to these areas via physical medium i.e. by opening branches. Thus, there will be heavy costs involved for building the Physical infrastructure.

'India Post Payments Bank' will be relatively well off in this area because of their massive presence already in rural areas. However, for other players it might be difficult.

2) NOT ALLOWED TO ENGAGE IN LENDING ACTIVITIES

A major drawback for these entities is that they are unable to lend money to account holders. This affects the revenue stream of Payment Banks to a large extent. Traditional Banks generate revenue from difference in lending interest rate and deposit rates. Thus they are enabled banks to make profits.

However, in case of payments banks, the only borrower is government and 75% of their deposits have to be compulsorily invested in government bonds whose yield is quite very low approximately 7.45-8%.

Payments banks will further need to have aggressive deposit rates to lure customers if they want to be successful. This will further shrink the profitability of the Payments Banks.

Moreover, deposit amount is capped at INR 1 Lakh, thus these banks will have to deal in low value & high volume markets.

3) LIMITED DIGITAL INFRASTRUCTURE OF INDIA

The digital infrastructure of India is still in the growing phase. Digital India is yet to be fully materialized.

Vodafone, Idea and Airtel might be able to handle digital transactions in a better manner since they are already in the mobile connection service providers category.

4) 3 PLAYERS ALREADY OPTED OUT

Within 9 months of the selection, out of 11 applicants, 3 have already pulled out citing profitability issues and long gestation period.

12. CONCLUSION

As the ecosystem around Payments Banks develops, it is critical for the regulatory and operational environment around them to evolve as well. Payments Banks are expected to be catalysts for broadening access to the banking system by offering innovative products and solutions with efficient customer service. Payments Banks have the benefit of being legacy-free and unlike established banks, they are under no pressure to grow credit volumes or meet priority-sector lending requirements. Therefore, they can focus on managing basic accounts and should have the freedom to do so in innovative ways.

In addition to the regulator providing an encouraging environment, the Government could also play a significant role in furthering the cause of Payments Banks through country-wide initiatives involving communication and consumer-education programs. Measures such as these could provide significant stimulus to broadening the customer base of Payments Banks and consequently furthering the cause of financial inclusion in the country, while enabling these banks to build sustainable businesses. Indeed, there is a question about who will take care of the credit needs of the unbanked. RBI evoke that Payment Banks will serve as a channel to allow people to eventually migrate to full-service banks, which is quite likely. Certainly payment banks will be a game changer.

Payments banks will face competition from the existing lenders. Besides, profitability will also remain a challenge as they will be working on narrow margins. To this end, due to ever-growing customers' expectations for faster-easier-simpler banking facilities what will drive the bankers is to work with creativity and passion, which contributes to growth of cross sections of our society, and so the challenges.

Banking costs will come down due to intense competition driven by the expected proliferation of payment banks. Currently, the customers are required to pay heavily for services like ATM transactions beyond a prescribed limit, additional cheque-books, non-maintenance of minimum balances etc. These costs will come down as payment banks start offering zero-balance, barefoot accounts with low-cost services and potentially higher rate of interest on deposits. The customer is finally going to be the king in the banking sector.

Thus payments banks and traditional bank will complement each other on the changing financial landscape of India.

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