REVIEW ARTICLE

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Indian Post Payment Bank: Financial inclusion revolution in India

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Abstract

The Indian financial system has seen several significant changes since 1991. The banking industry is one of the few that has thrived since liberalization, and its success is unquestionably tied to the considerable financial reforms adopted by RBI and the significant technological improvements that have occurred over the years. In 2014, the Reserve Bank of India (RBI) broadened the variety of banks operating inside the Indian financial sector. Payment banks and tiny banks are two names for these modern financial institutions. The major objective in creating these banks is to increase financial inclusion in underserved rural communities by increasing access to banking goods and services. The unbanked and underbanked populations may be able to get access to financial services via payment banks, a new kind of financial institution. Expanding the availability of financial services is a top priority for them. In this paper, we discuss the payment banking infrastructure and the benefits that are expected to accrue from it. The Post Payment Banks of Indian financial system will be a great first step in providing access to banking services for underserved populations, especially those who are transient or from low-income families. Is the Indian Post Payment Bank the second phase of financial inclusion following the Pradhan Mantri Jan Dhan Yojana?This research aims to fill in some of the gaps in our understanding of payment banks by providing a high-level overview of their functioning processes and demonstrating how the idea of payment banks accomplishes two goals at once. All of the information in this study comes from secondary sources. As a starting step toward its financial inclusion strategy, it is increasing its digital payment infrastructure. The second positive effect is that it promotes a more tech-savvy mindset in the Indian banking industry. These results show promise for increasing financial inclusion and access throughout India, especially in rural areas and with a focus on low-income people and small businesses.

Key words: Payment Banks, Financial system, Financial Inclusion, Post Payment Banks,

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Introduction to payment banks:

The Reserve Bank of India and the Government of India have undertaken various initiatives to enhance citizens' access to financial aid and improve the state of the financial sector in India, with a greater emphasis on rural residents, people of lower socioeconomic status, smaller businesses, and migrant workers. These initiatives include the introduction of electronic fund transfer methods like NEFT and RTGS, the promotion of mobile payments, and the implementation of schemes like Pradhan Mantri Jan Dhan Yojana (PMJDY) and the Digital India Campaign. As part of this drive, new payment banks have been established with the aim of expanding access to banking services across India, particularly in rural areas and to serve low-income families and local businesses. These banks specialize in high-volume, low-value transactions, and are a part of the Reserve Bank of India's efforts to bring financial inclusion to all.

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With Dr. Nachiket Mor at the executive chairman, the Reserve Bank of India formed a committee in September 2013 to look into "Comprehensive financial services for small companies and low-income people." The committee was commissioned to write up a comprehensive report detailing its findings. As part of its charge, the group was asked to figure out how to increase and diversify people's access to financial aid.

The commission handed its report to RBI in January 2014. With the utmost goal of allowing any Indian

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person to open a global bank account on January 1, 2016, the committee recommended establishing specialised banks or "payments banks" to serve individuals with modest incomes and small enterprises. The Reserve Bank of India (RBI) plans to reach out to more rural areas of the country by utilising payments banks to provide access to banking services. The Reserve Bank of India approved eleven applications for payments bank licences "in principle" on August 19, 2015, out of a total of forty-one.

The Reserve Bank of India came up with this innovative framework for the financial sector (RBI). A payments bank operates similarly to a traditional bank, however its commercial activities are scaled down to a more manageable level, and the bank does not take on any credit risk. Although it may perform a wide variety of banking services, this bank cannot make loans or issue credit cards, unlike the bulk of its competitors. It also offers traditional banking services including ATM/debit cards, internet banking, third-party financial transfers, and remittance services. Demand deposits are currently capped at Rs 1 Lakh per customer, though that figure may rise in the future.

There are currently 12 payment and small finance banks open for business, with more likely to follow soon. The Reserve Bank of India authorised India Post to begin processing payments in August of 2015. In August of 2016, it was formally established as a public limited government corporation for the purpose of establishing a payments bank. The IPPB was formally introduced in both Raipur and Ranchi in January 2017 after a successful pilot project in both cities. On September 1, 2018, the nationwide inauguration officially started off.

Following its incorporation as a Public Limited Company within the purview of the Department of Posts and with strong endorsement from the Government of India, the India Post Payments Bank is now open for business. Established under the aegis of the Ministry of Communication's Department of Posts, India Post plans to utilise its extensive branch network to open 650 locations across the country.

Objectives of the study:

- Examine the development of Payment banks in India.
- To investigate the features that distinguishes payment banks apart from conventional banks.
- To better understand how post payment banks in India contribute to the broader goal of financial inclusion.

Methodology:

This work employs a descriptive and conceptual approach based on secondary sources of information. The information comes from a variety of sources, including newspapers, websites, and national and international periodicals. Analyzing, reinterpreting, or revisiting previously collected data is what's known as "secondary research", aid in comprehending past and current events.

Literature review:

The government's direct benefit, transfer systems rely heavily on the services of payment banks, and this trend is accelerating the progression toward financial inclusion. Payments for things like medical care, tuition, and gas assistance are all transferred straight into the recipients' bank accounts through these systems. This has the potential to boost competition between conventional banks and payment banks, leading to an increase in the range and quality of banking services available at affordable prices. This, in turn, might expand the number of people who have access to financial services. (Dr. V. Ramesh Naik, Mr. P. Firdous, Miss P. Harika)

People are able to utilize payment systems because of the wide variety of payment banks that may be used for even the small of payments at odd hours. Another distinguishing feature of the Indian system is that most transactions are conducted in cash. Simply put, the Indian system also serves as a mandated currency management system, and it is this system that digitally records even the smallest of transactions."(Madhavi Damle, PushpendraThenuan, JimitRaval)

While the creation of a payment bank is certainly ground-breaking, it is important to remember that payment banks differ significantly from traditional commercial banks in a variety of crucial ways. Even though the Minister of State for Communications claims this would bring off the "another round of financial inclusion," the inaugural phase of the PMJDY has not yet been carried out to its full potential. *(J.Vaishnavi and N.Shruthi)*

In order to thrive in this high-volume, low-margin industry, businesses must use scalable technology to reduce the cost of client acquisition and service provision. To ensure their long-term viability, payments institutions must adopt a more flexible pricing model *(Anand Ramachandran, CFO of Paytm)*

Research that has been done Due to the lack of regulation over rural branches of commercial banks and regional rural banks, rural residents were unable to keep up with the digital banking revolution. The means through which the payment bank's function will be augmented and improved in order to contribute in the larger mission of expanding access to and understanding of financial services. One must weigh the expenses of running a payment bank against the advantages it offers. *(J.Vaishnavi and N.Shruthi)*

Financial institutions like these stand to gain from the widespread use of digital money. Despite the fact that over 90% of transactions in India are typically relied on cash, demonetisation has offered a substantial boost to payments banks as a consequence of its focus on digital transactions. Businesses throughout India, from street vendors and grocery store owners to mom-and-pop shops, are seeing a rise in the number of customers who prefer not to carry cash. Acceptance rates are expected to climb steadily over the coming years, and payments banks will play a key role in facilitating this digital transformation.

An increasing number of individuals are using payment banks, which is helping to speed up the expansion of financial inclusion via government-run direct benefit and transfer systems. Payments are deposited into the bank accounts of the recipients and used for things like medical expenses, tuition, and giftcards. This might increase competition between payment banks and conventional banks, which could lead to better financial services at more affordable rates. The consequence might be an increase in the number of people who have access to banking and other forms of structured credit. *(Mr. P. Firdous, Ms. P. Harika, and Dr. V. Ramesh Naik.)*

Current findings from studies have Incorporating modern banking technology might be challenging for rural communities due to a lack of regulation for commercial bank and regional rural bank branches in outlying regions. How the payment bank's function will be expanded and improved so that it can help achieve the greater objective of spreading financial education. It's important to weigh the pros and cons of running a payment bank.

These financial institutions anticipate gaining market share as a result of the extensive use of digital money. Despite the fact that over 90% of transactions in India are traditionally based on cash, the focus on digital transactions brought about by demonetisation has delivered a substantial boost to payments banks. The rising number of individuals who would prefer not deal with cash is having an impact on businesses of all sorts throughout India. This encompasses everyone from hawkers and grocery store proprietors to entrepreneurs with one-person operations. The surge in acceptance rates over the next several years indicates that payments banks will play a significant role in facilitating this digital transformation.

RBI's Key Guidelines for Payment Banks

The use of prudent regulation:

The prudential regulatory system for payments banks (PBs) will be based on the Basel standards. While these institutions are committed to expanding access to financial services, appropriate adjustments will be made to ensure that the regulations are suitable for their unique operating model. The Basel standards provide a framework for maintaining the financial stability of banks, including guidelines for capital adequacy, risk management, and liquidity. By adopting these standards, payments banks can ensure that they are operating under a solid foundation that promotes sound banking practices. However, given the PBs' focus on expanding financial inclusion, it is important that the regulations are appropriate and flexible enough to support their mission. These adjustments can help to ensure that PBs can continue to serve underserved and remote populations while also maintaining the necessary standards of the banking industry. Ultimately, by striking a balance between regulatory compliance and innovation, payments banks can contribute to the broader goal of financial inclusion in India.

Financial institution borrowing:

Both Payment Banks and their customers will be able to borrow and lend from each other in the call money and 'collateralized borrowing and lending obligation' CBLO market. But the ceiling on call money borrowings for scheduled commercial banks would apply to these loans as well.

Loan and advance restrictions (including those imposed on lending to nonbanking financial institutions)

Payment Banks are restricted from lending loans to anyone, even its own management. Although Payment Banks are prohibited from lending to outside parties, Payment Banks are allowed to lend to their own personnel using bank money, subject to limits established by Board policy.

The approval for the Product:

As part of the application for a licence, Payment Banks are required to provide RBI with a comprehensive list of the financial products they would like to offer.After then, PBs need to let RBI know about any new financial product they plan to release. Depending on the particular circumstances, RBI may impose appropriate limitations on the product's architecture, operation, or other characteristics, or even force the product's discontinuation.

Handling risks:

The rules for managing market risk at Payment Banks will be the same as those at commercial banks. Derivatives will be allowed for use by Payment Banks exclusively for the purpose of hedging foreign currency holdings resulting from operations authorised under Authorised Dealer Category II.

The Reserve Bank of India (RBI) has mandated that payment banks submit data on operational losses and otherwise conform to the operational risk management rules outlined for scheduled commercial banks.

Liquidity risk management regulations for pay should be the same as those applicable to scheduled commercial banks, with appropriate modifications to account for PBs' unique liquidity risk characteristics.

The regulations for managing strategic and operational risks should be the same as those applicable to scheduled commercial banks, with appropriate enhancements to address potential liability resulting from the employment of agents.

When it comes to ICT-related elements and activities via intermediaries, payment banks must adhere to the same regulations as scheduled commercial banks in terms of internal controls, audit, and compliance.

Corporate Governance:

Bank holding companies, or payment banks, are required to adhere to the same regulations as traditional banks. This includes regulations related to director appointments. For converting corporations, the current directors' appointments will be honored until the end of their standard contracts. Payment banks are also required to follow the same requirements as commercial banks in this regard. These regulations help to ensure that payment banks operate under the same guidelines as traditional banks, promoting transparency and accountability in the financial industry. By adhering to these regulations, payment banks can continue to serve the underserved and promote financial inclusion while also maintaining the necessary standards of the banking industry.

Bank Deposits:

According to the current RBI guidelines, only savings and current deposits may be accepted by payment banks. Per the terms of the Licensing Guidelines, the maximum amount that may be charged to a single customer in a given period of time is limited at rupees 100,000. Nonetheless, the RBI will not object if the payment banks make agreements with another scheduled commercial bank or Scheduled Financial Banks to sweep any balances in excess of the permitted limits into an account created for the user at that bank. The customer's prior written approval is required before this agreement may go into effect.

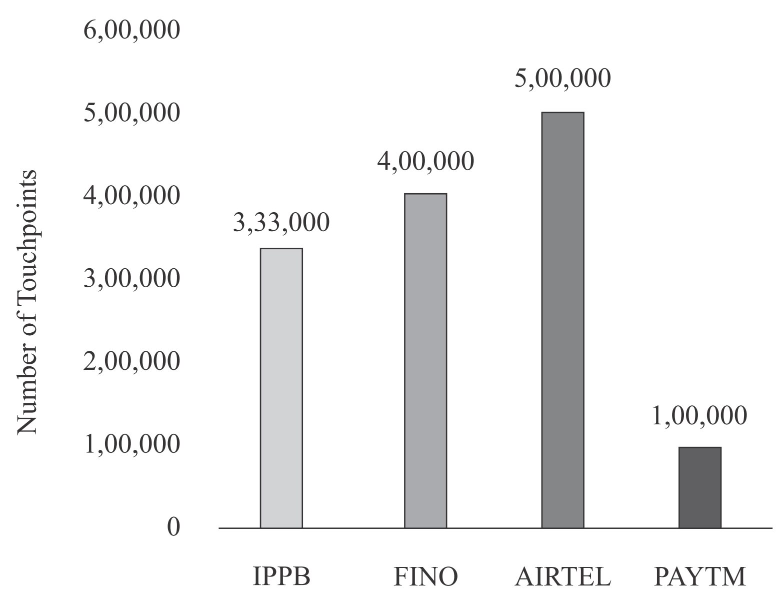
The above restriction applies only to deposits from customers and not to any security or eager money deposits the bank may require of its service providers.
All provisions of the RBI and the Banking Reconciliation Act and all directions issued by the RBI with respect to minimum balances, nonfunctional accounts, unclaimed deposits (including the transfer of such deposits to the Depositors Education and Awareness Fund maintained by the RBI on a regular basis), nominations, cheques/drafts, etc., will apply to the PBs.

Evidences from Branches and Business Correspondences of Payment Banks

The extensive network of touchpoints established by PBs has been instrumental in expanding financial access to underserved and remote regions. In addition to leveraging their parent companies' infrastructure, PBs has also entered into partnerships with other entities to further widen their reach. For instance, Fin-Payments Bank has partnered with the Rajasthan state government and Bharat Petroleum to expand its agent network. PBs' extensive network of touchpoints has also proved to be beneficial for full-service banks, which can use them as Business Correspondents (BCs) to provide banking services in previously unviable regions.

Furthermore, PBs have taken advantage of technological advancements to enhance their services and improve customer experience. For instance, some PBs have developed innovative solutions to cater to the needs of migrant workers, such as facilitating instant money transfers and providing access to microloans. PBs have also been at the forefront of promoting digital transactions in India, particularly in rural areas. This has been achieved through various initiatives, such as educating customers on the benefits of digital payments and offering incentives for adopting them. Overall, PBs have played a critical role in advancing financial inclusion in India, particularly for underserved and remote populations.

Figure 1: "Total Number of Payment Banks Touchpoints"



Source: "(Dvara Research Blog | Have Payments Banks Fulfilled Their Financial Inclusion Objectives?, n.d.)"

Payment banks (PBs) differ from full-service banks as they primarily rely on their agent network to operate. Unlike full-service banks, PBs can effectively expand their network through partnerships. Full-service banks can also benefit from the vast PB touchpoint network by using them as banking correspondents (BCs) to serve previously unbanked areas.

Furthermore, according to the branch authorization policy, 25% of a bank's outlets should be in unbanked rural centers (URCs). Thus, the large PB touchpoint network has the added advantage of providing payment services to unbanked areas through as many as 300,000 touchpoints. To put this into context, as of March 2019, there were 540,000 BC touchpoints in villages, serving around 640,000 villages according to the 2011 Census.

Table 1: Branch Correspondence Touchpoints

Bank	No. of Branches	No. of BC Touchpoints	BC Touchpoint: Branch Ratio
Yes Bank	1,120	31,000	27.7:1.0
Bandhan Bank	986	3,014	3.1:1.0
IDFC First Bank	698	100	0.1:1.0
Au SFB	322	67	0.2:1.0
Fino PB	103	2,00,000	1941.7:1.0
Paytm PB	7	2,00,000	28571.4:1.0
IPPB	650	1,95,000	300.0:1.0

Source:"(*Dvara Research Blog | Have Payments Banks Fulfilled Their Financial Inclusion Objectives?*, n.d.)"

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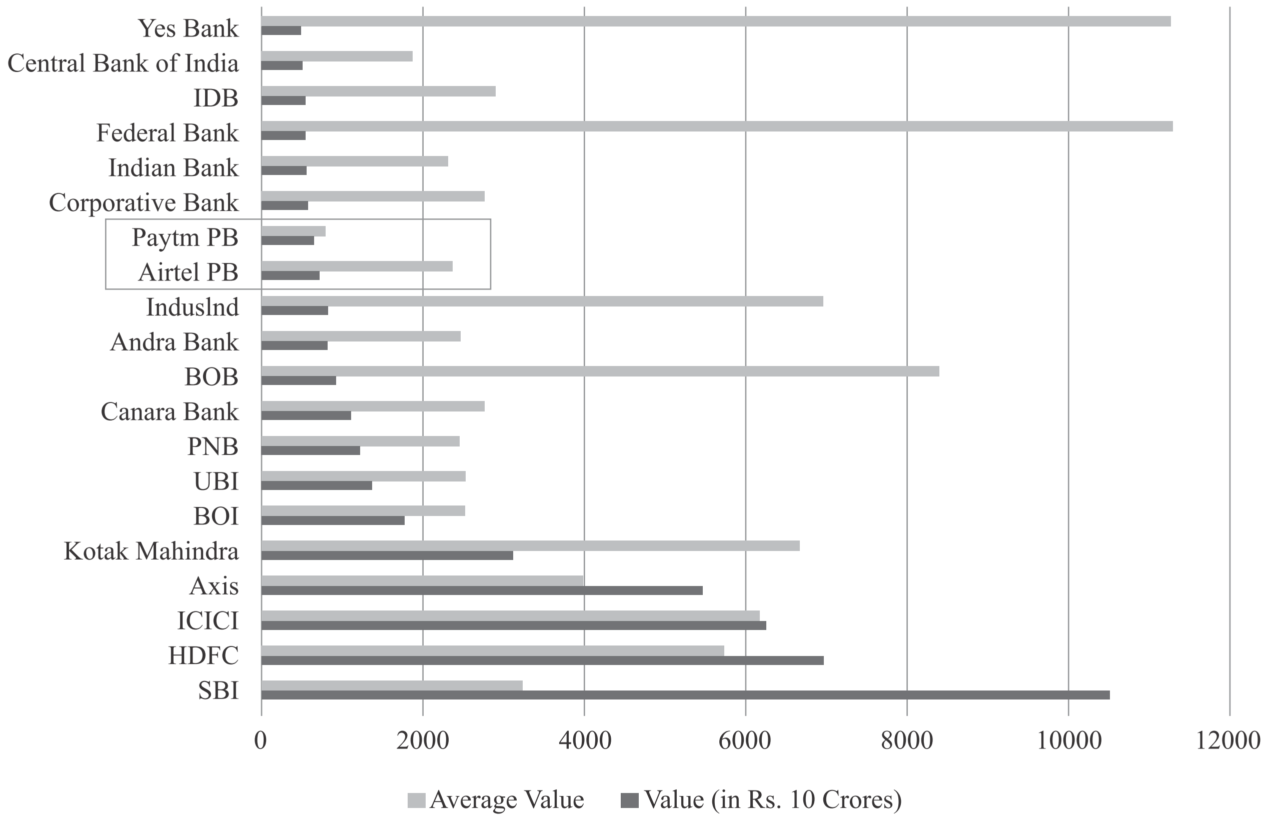
The digital transactions facilitated by payment banks, including Paytm Payments Bank, have exceeded those of most full-service banks. Paytm PB had the lowest average mobile transaction values among the top 20 scheduled commercial banks with the highest value of mobile transactions in March 2020 (refer to Figure 2). However, it is important to note that the low average transaction size of Paytm PB may be due to its payments model, and not necessarily indicative of fulfilling the goal of serving underserved populations. Meanwhile, India Post Payments Bank (IPPB) has a higher average mobile transaction value compared to other payment banks, despite lower transaction volumes and values, suggesting a model that prioritizes larger transactions rather than smaller ones made by underserved or rural customers.

Figure 2: "Mobile Transaction Value"



Source:"(Dvara Research Blog | Have Payments Banks Fulfilled Their Financial Inclusion Objectives?, n.d.)"

Challenges faced by Payment Banks in India

Bank Restrictions on Making a Payment:

Several payment banks have been approved by the Reserve Bank of India (RBI) and are now in operation. Still, surviving in the here and now is no simple process. The obstacles they must overcome are numerous challenges. One of them is that payment banks are not allowed to make loans, which would provide them a steady stream of interest income. Banks that process payments will need to brainstorm new revenue streams. Second, conventional commercial banks also provide payment bank services. Competing with them may increase your blood pressure.

The aforementioned banks are fully digital operations.

Market dominance requires unbreakable, virus-free software. The general public has little understanding about payment banks. One of your main goals should be to spread the word about the company to those living in both urban and rural areas.

Payment banks can't be widely used without a reliable network.

Telecom companies are the only ones to sign up. The Post Payment Bank has been granted authorization to use government resources, and it operates a broad variety of branch locations.

The monetary institutions of PBs do not have a centralized location.

The agreements wouldn't get done without the usage of the internet. A reliable and speedy internet connection is essential in today's corporate world. For maximum efficiency in any given area, a reliable wireless network with internet access is essential.

Customers hesitant to switch.

The hesitancy of some customers to switch to digital payment methods is a new challenge. Several consumers, even in large urban centres, are not yet prepared to do all of their shopping online. Someone's mind has been influenced by the demonization process. The threat that wallets, which provide the same duties, represent to established financial institutions like banks is significant.

Findings:

The Government of India's (GoI) "Digital India" plan remains in its inception. However, the already-prominent Indian Post Payment bank may contribute to the development of even higher usefulness.

The financial needs of economically marginalised individuals in India's much further regions are not being met by the country's centralised banking and finance system. Branch locations of payments banks will appear there. Seventy percent of people have less than one million rupees ($14,000) in the bank. Banking services have mostly centered on this group.

The ability to complete transactions at the customer's doorstep is the primary benefit of Indian post payment banks. One of the friendly neighborhood mailmen is switching careers to become a banker.

Migrant workers, low-income families, small enterprises, and other members of the unorganized sector would all benefit from payments banks' ability to provide modest savings accounts and payments/remittance services, as evidenced by this research.

The number of Indian post payment banks is 2.5 times larger than the conventional banking system. Over time, the payments bank will connect all 1.55 million post offices in the nation, including 1.30 million in rural areas, to provide the service. It serves rural regions by maintaining at least one branch in each district.

Over the period of time, Indian Post Payment Banks will provide a wide variety of services, including checking and savings accounts, money transfers (including RTGS, NEFT, and IMPS), direct benefit transfers, payments to utilities, and payments to businesses and merchants.

Conclusion:

Payment banks are rapidly replacing other digital payment methods as the preferred method of transaction. India is making the transition to a cashless and digital economy because it is more practical and flexible in light of current technical and economic developments. The procedure for ensuring that marginalised communities, such as weaker sections and low-income groups, have access to the right financial services and products needed by them at an affordable cost in a fair and transparent manner from contemporary institutional players is widely regarded as a sound strategy towards financial inclusion. This strategy seeks to ensure that marginalised communities, such as weaker sections and low-income groups, have access to appropriate financial products and services. However, as conventional banks face more competition from payment banks, banking services will expand, improve, and become more affordable for more people. In the absence of more data, it would be unreasonable to say that how well Payment banks perform in contrast to more seasoned financial institutions. To thoroughly utilize the benefits of payment banks, several obstacles must first be removed. As a result, millions of Indians are unable to use financial services. They are not eligible for welfare, loans, insurance, or savings interest from the government. International, Physically Separated, Payment Banks will reach the unbanked and underbanked everywhere. Successful payment banks may benefit most from a culture of constant innovation and a willingness to try new things.

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