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Payment Banks Landscape In India

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ABSTRACT:

India's banking sector has been evolving since 1991, notably due to the technological upheaval that has introduced substantial alterations. One such shift initiated by the Reserve Bank of India (RBI) was the formation of payment banks. The chief aim of setting up payment banks was to boost financial inclusion through the use of technology. Payment banks predominantly target providing payment and remittance services to low-income families, small enterprises, migrant labourers, and others in informal sectors. Payment banks leverage financial technology to infiltrate the economy and access the unbanked segments of the populace. The research aims to examine the functioning of payment banks in India, evaluate the financial performance of payment banks, and pinpoint the obstacles faced by payment banks. The study was executed based on data sourced from various websites, RBI documents, and publications.

Keywords: Banking sector, Payment banks, financial technology, financial system

JEL Classification: G2, G21, G28, O33

Introduction

Since 1991, the Indian financial system has undergone significant transformation. The banking industry is also changing, and one breakthrough that has come about is the introduction of payment banks by the RBI in 2014. The banking industry has undergone significant change as a result of the RBI's significant reforms as well as technological advancements. A sizable section of the Indian population continues to have access to financial services, despite significant reforms and transformations in the banking system. New means to reach clients are being made possible by technological advancements, and the financial services sector is

utilizing technology to increase the size of its business. The RBI established the "Committee on Comprehensive Financial Services for Small Businesses and Low-Income Households" to address the needs of those without access to banking. Dr. Nachiket Mor serves as the chairman of the committee, and its mission is to find and suggest the establishment of a bank that will improve the level of financial inclusion. Payment banking institutions were founded based on the suggestions made by the Dr. Nachiket Committee. These banks mainly offer payments and migration services, rather than the entire spectrum of services offered by regular banks (Naik et al., 2018). Payment banks were founded with the aim of bringing an increasing number of individuals into the general population of the economy and thus making a contribution to the nation's growth. By utilizing technology, they offer payments and basic financial services, hence facilitating wider accessibility to these services. Payment banks are only permitted to receive deposits exceeding two lakh rupees and may only provide a specific set of services to their clients. Along with payment and remittance, deposits may be accepted in the way of current or savings accounts. Additionally, they are not allowed to accept deposit from NRIs or issue credit cards (RBI, 2017).

The current state of affairs in India is considered to be one of the most favourable for the growth of digital payments. Technological advancements such as blockchain technology, artificial intelligence, and machine language are redefining every industry through digitization (Shah & Mehta, 2019). With the emergence of payment banks that specialize in online payments and remittances, it is crucial to comprehend the current state of payment banks in India. The primary goals of the study are to comprehend how payment banks operate in India and to learn about their financial performance.

REVIEW OF LITERATURE

Indian financial sector has experienced a significant transformation in both scope and intricacy over recent decades. The advent of payment banks in India has resulted in the creation of more innovative and revolutionary entities compared to traditional banks, with a notable surge in the use of payment banks following demonetization (Mehta & Shah, 2020). The Reserve Bank of India established payment banks to improve financial accessibility, primarily targeting low-income individuals and small enterprises to access fundamental banking services through technological innovations in financial sector (Singh & Bhadouria, 2019). It was observed that payment banks play a significant role in transitioning India towards a cashless society, and there is a need to increase awareness among middle-aged individuals about the advantages of payment banks (Rathod et al., 2017).

The present scenario in India features a flourishing start-up environment, deeply rooted industry expertise, and technological trends like artificial intelligence, machine learning, and blockchain technology that are revolutionizing the IT sector through digital transformation. Attitudes are shifting with millennials who spend individually, and so forth, all of which vigorously encourage the growth of digital payments. Payment banks are rapidly expanding, with the identified dimensions for their use being user-friendliness, convenience, cost efficiency, security, and ease of cash management. Considering demographic aspects and their impact on

occupation, annual income, and education on payment bank utilization, both age and annual income influence the frequency of use and average spending through payment banks (Shah & Mehta, 2019).

Payments banks will be able to react to shifts in the economy faster and with more agility and accessibility. They will draw in an extensive range of underserved and unserved clients because of their increased responsiveness and approachability to consumer demands. Attracting clients could be easy, but these connections need to be profitable. Payments banks are anticipated to use a new 'hi-tech and hi-touch' digital strategy to enhance and expand their reach, while traditional banks are limited by their outdated business model. The growing demands of customers for quicker, easier, and more straightforward financial services will encourage bankers to work passionately and imaginatively, fostering the development of diverse societal segments and the overall economy (Agarwal, 2016).

Payment banks hold a significant role in the execution of the government's welfare programs, where subsidies for healthcare, education, and gas are credited directly to recipients' accounts. However, rivalry between conventional banks and payment banks will drive the growth and enhancement of banking services, along with cost reductions, which may eventually foster financial inclusion. Numerous challenges need to be tackled before the full benefits of payment banks can be realized. Millions of Indians remain without access to banking services, making them ineligible for government aid, loans, insurance, or even interest on savings. Mobile banking, India Post Payments Bank, and the Pradhan Mantri Jan Dhan Yojana will extend their reach to the unbanked and underbanked across all demographics and regions (Naik et al., 2018).

Establishing an effective ecosystem will be essential for a sustainable banking and payment framework. Integrating the rural populace into the formal banking sector continues to be a significant challenge. Payment banks can play a pivotal role in this regard (Yadav et al., 2019). Payment banks can leverage the extraordinary surge in the e-commerce sector to attract new customers, including those in smaller towns and rural areas (Sikdar & Kumar, 2018).

OBJECTIVES

- a) To examine the operation of payment banks in India.
- b) To know the financial performance of payment banks in India.
- c) To identify the challenges faced by payment banks in India.

METHODOLOGY:

This paper analyses payment banks' financial performance in India and provides a conceptual and descriptive analysis of how they operate. The study makes use of secondary data that was gathered from reliable sources, such as newspapers, journals, and RBI websites and publications. The purpose of this study is to track payment banks' financial performance in the Indian setting and obtain insights into how they operate.

PAYMENT BANKS

Under the direction of Nachiket Mor, the "Committee on Comprehensive Financial Services for Small Businesses and Low-Income Households" made suggestions that served as the foundation for the establishment of payment banks. These banks have tight guidelines for the acceptance of deposits and facilities for payment and remittance services. They are regulated under Section 22 of the Banking Regulation Act of 1949, and registered under the Companies Act of 2013. By offering remittance and small savings account services to migratory labourers, households with low incomes, small business entities, and others in unorganized industries in technologically secured surroundings, payment banks aim to promote financial inclusion. Payment banks must have the term "payment bank" in their name to be distinguished from others (RBI, 2014).

Lending operations are prohibited for the payment banks. It will be necessary to invest at least 75% of its "demand deposit balances" in government securities or treasury bills with time frames of up to one year that have been accepted by RBI as eligible securities to maintain Statutory Liquidity Ratio (SLR) and hold a maximum of 25% in current and time / fixed deposits in other scheduled commercial banks for operations, in addition to the amounts kept as Cash Reserve Ratio (CRR) with RBI on its additional demand and time liabilities. In order to meet the CRR and SLR prerequisites on its "overall outside demand and time liabilities," which include deposit balances and outstanding balances in PPIs issued, the payments bank's "balances outstanding under the PPIs issued" should be flexibly deployed between SLR eligible Government securities/Treasury Bills and bank deposits (both demand and time). In order to manage short-term liquidity, payment banks will be a member of the payment and settlement system and will have access to the interbank uncollateralized call money market, collateralized repo, and CBLO markets(RBI, 2014).

Payment banks are governed by following provisions:

- Banking Regulation Act, 1949
- Reserve Bank of India Act, 1934
- Foreign Exchange Management Act, 1999
- Payment and Settlement System Act, 2007
- Deposit Insurance and Credit Guarantee Corporation Act, 1961
- Statues, directives, other regulations and guidelines issued by RBI from time to time.

Evolution of Payment Banks

According to the direction of Nachiket Mor, the Reserve Bank of India established the committee on comprehensive financial services for low-income people and small companies on September 23, 2013, with the goal of researching financial inclusion issues in India. The committee recommended on December 31, 2013, that payment banks be established, with the main goal being to offer low-income people and small businesses basic financial services including deposit and payment products. Establishing a payments bank

requires a minimum capital of Rs. 100 crores. On January 7, 2014, this committee turned in its final report, which included a number of recommendations (Agarwal, 2016).

It recommended the formation of a payments bank. Draft guidelines regarding the setup of payment banks were released by the RBI on July 17, 2014, inviting suggestions and comments from the general public and interested entities. On November 27, 2014, the RBI issued final guidelines for payment banks also seeking applications. In February 2015, RBI released the list of 41 applicants for licensing payments banks and also announced an External Advisory Committee (EAC) headed by Nachiket Mor to evaluate the license applications. During the budget presentation on February 28, 2015, it was announced that Indian Post will be the largest payment bank. On August 19, 2015, the Reserve Bank of India "in-principle" granted licenses to 11 entities to launch payment banks, out of which three surrendered. A license for a payment bank is granted under Section 22 of the 1949 Banking Regulation Act. It suggested setting up a bank for payments. On July 17, 2014, the RBI announced draft guidelines for the establishment of payment banks and invited recommendations and suggestions from interested parties and the public at large. The RBI released the final rules for payment banks soliciting applications on November 27, 2014. The RBI announced the appointment of Nachiket Mor as the head of the External Advisory Committee (EAC) to review the license applications, and it also disclosed the list of 41 candidates for licensing payments banks in February 2015 (Naik et al., 2018; Thenuan et al., 2016; Yadav et al., 2019).

List of current active payment banks in India as per Reserve Bank of India:

1. Airtel Payment Bank Ltd
2. India Post Payment Banks Ltd
3. FINO Payments Banks Ltd
4. Paytm Payment Banks Ltd
5. Jio Payment Banks Ltd
6. NSDL Payment Bank Limited

RBI Guidelines for Payment Banks

A minimum paid-up equity capital of Rs. 100 crores are required for payment banks. On the basis of their risk-weighted assets, they also have an obligation to continually uphold a capital adequacy ratio of 15%. Promoters must provide at least 40% of the paid-up equity capital within the first 5 years of the company's existence. As permitted by Section 19(2) of the Banking Regulation Act of 1949, a scheduled commercial bank can make investments in the payments bank if the payments bank is founded as a joint venture with the latter. Payments banks' foreign ownership strategy will be in line with private sector banks' foreign direct investment (FDI) strategy. Further, Section 12(2) of the Banking Regulation Act of 1949 will govern the voting rights of shareholders in payments banks. The prudential standards and principles pertaining to these operations do not apply to payments banks because they are not allowed to offer loans or advances. They have to follow corporate governance norms, which include the RBI's "fit and proper" requirements for

directors. Payments banks should run their whole business digitally, using technology to drive operations while adhering to all applicable norms and guidelines. Payments banks must set up a consumer Grievances Cell to handle consumer complaints under the RBI's 2006 Banking Ombudsman Scheme. Furthermore, the bank shall have at least 25% of its branches in rural regions without access to banking services (RBI, 2014, 2016).

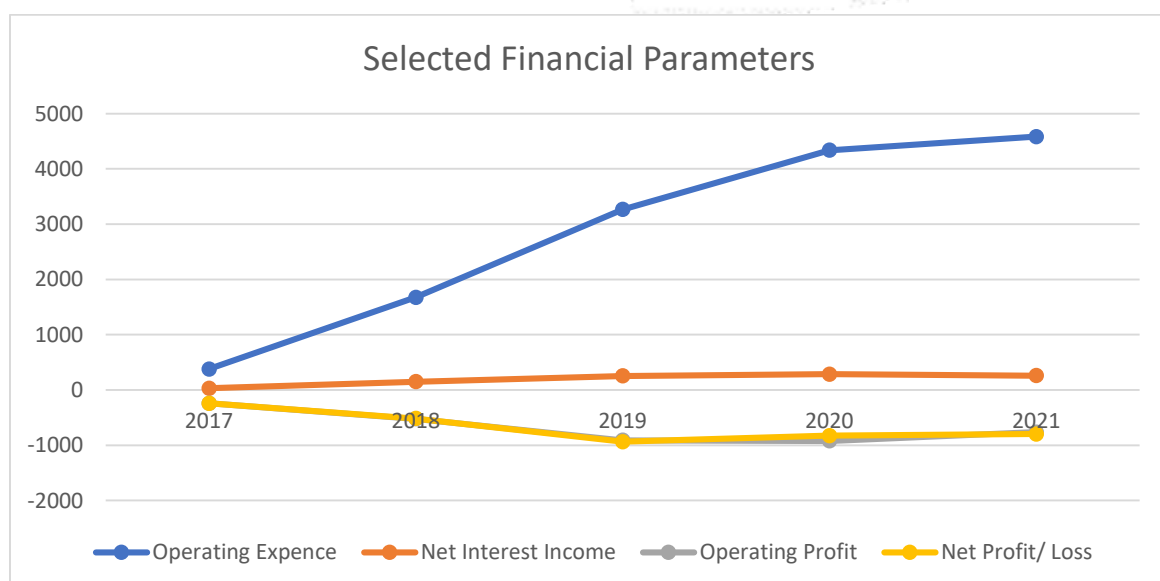
Scope of activities of Payment Banks

Payment banks can receive deposits from homes, small businesses, and other entities except for non-resident Indians. They offer deposit, remittance, and payment services to clients; the highest amount that any one client may have in their account is one lakh rupees. The RBI has raised the maximum amount that can be held at the end of the working day from one lakh to two lakh rupees, nevertheless, to increase financial inclusion. Under the Deposit Insurance and Credit Guarantee Scheme Corporation of India (DICGC), deposits made with payment banks are protected. Payment banks are permitted to provide ATM and debit cards to customers, but they are not allowed to issue credit cards. Their payment and remittance services involve collecting funds from branches and Business Correspondents (BCs), along with cash disbursements through ATMs, branches, and additional BCs. Payment Banks utilize technology to provide economical banking services to clients and must adhere to RBI's guidelines and directives on internet banking, data security, electronic banking, cybersecurity, and related areas. They are authorised to accept remittance via multiple payment methods sanctioned by RBI including NEFT, RTGS and IMPS (RBI, 2014).

Financial Performance of Payment Banks

Table No: I

Selected Financial Parameters



Compiled by the author, Source: Secondary data, (RBI, 2017, 2018, 2021)

Table I presents selected financial parameters of payment banks in India from 2017 to 2021 for a varying number of banks in each year (two, five, seven, six, and six banks, respectively). Due to the differing number of banks each year, the data may not be directly comparable. Notably, both the operating profit and net loss (in crores) have consistently displayed negative values since the inception of payment banks. However, there has been a slight improvement in both net loss and operating profit for the years 2020 and 2021. These negative values can be attributed primarily to the high initial operating expenses incurred during the setup of the initial infrastructure for payment banks. As significant expenditure is invested in establishing the necessary framework, it is expected that some time will be required for payment banks to recover these operating expenses and expand their customer base by offering unique financial services. Nevertheless, it is noteworthy that there has been an improvement in net interest income, indicating positive developments in this particular aspect of the payment banks' financial performance. As the industry matures and operational efficiency increases, payment banks are likely to witness further progress in their financial standing.

Table No: II
Selected Financial Ratios of Payment Banks

Items	Mar-17	Mar-18	Mar-19	Mar-20	Mar-21
Return on Assets	-25.2	-10.6	-13.1	-9.8	-6.4
Return on Equity	-36.4	-27.9	-49.4	-44.3	-44.5
Investments to Total Assets	29.2	50.0	43.7	48.4	56.6
Net Interest Margin	2.8	4.5	6.1	4.8	2.8
Efficiency (Cost-Income Ratio)	272.7	142.2	136.6	124.8	116.9
Operating profit to working funds	-25.1	-10.7	-12.7	-10.9	-6.1
Profit Margin	-172.9	-43.8	-39.2	-23.9	-20.3

Source: RBI Report, (RBI, 2017, 2018, 2021)

Table II presents the selected financial ratios of payment banks in India for the period from the year-end March 2017 to the year-end March 2021, covering two, five, seven, six, and six payment banks, respectively. Throughout these years, the operating profit to working funds ratio and the profit margin ratio displayed negative values; however, there was a noticeable improvement in their values over time. Notably, the efficiency ratio, represented by the Cost-Income Ratio, experienced significant progress, decreasing from 272.7 at the year-end of 2017 to 116.9 at the year-end of 2021. This improvement indicates enhanced cost management and operational efficiency within payment banks during the specified period.

Regarding the Net Interest Margin (NIM), an initial improvement was observed during the early years, but from 2019 onwards, there was a clear decline in NIM. This suggests that payment banks faced challenges in maintaining profitability from their interest-earning assets after 2019.

Analysing the Return on Asset (ROA), although the values remained negative over the years, there was a reduction in the extent of loss as compared to previous years. This indicates some progress in managing assets and generating returns, although profitability remained a concern for payment banks.

In contrast, the Return on Equity (ROE) exhibited a consistent loss trend. While a slight improvement was noted at the end of 2019, there was a significant decline in ROE shortly afterward. Despite a slight recovery, the values remained negative, indicating that payment banks struggled to generate returns for their shareholders during the specified period.

Overall, the financial ratios of payment banks in India showed mixed performance trends over the period covered by Table II. While there were signs of improvement in some areas, negative values persisted in key ratios, highlighting the ongoing challenges faced by payment banks in achieving sustainable profitability and positive returns.

Table No III
Remittance through Payment Banks

(Values given in crore)

Channel	2019-20		2020-21	
	Inward Remittance	Outward Remittance	Inward Remittance	Outward Remittance
NEFT	19,398 (5.3)	43,593 (10.1)	26,295 (9.8)	60,649 (19.8)
RTGS	81,411 (22.2)	56,794 (13.2)	56,460 (21.0)	35,107 (11.4)
IMPS	34,309 (9.3)	1,05,366 (24.5)	37,466 (14.0)	65,866 (21.5)
UPI	1,70,998 (46.6)	1,60,976 (37.4)	1,13,289 (42.2)	1,03,908 (33.9)
E- Wallets	23,427 (6.4)	41,274 (9.6)	20,406 (7.6)	38,317 (12.5)
Micro ATM (POS)	16,746 (4.6)	229 (0.1)	20 (0.0)	45 (0.0)
ATM	-	1,169 (0.3)	-	3 (0.0)
Others	20,740 (5.7)	21,515 (5.0)	14384 (5.4)	2,866 (0.9)
Total	3,67,030	4,30,916	2,68,321	3,06,761

Source: Secondary Data, (RBI, 2021)

Table III presents the total inward and outward remittances through payment banks in India. The data indicates a reduction in the total value of inward and outward remittances through payment banks to approximately 14% during the year 2020-2021. Among the various remittance channels, Unified Payment Interface (UPI) stands out as the highest contributor to the total remittances, followed by IMPS (Immediate Payment Service) and RTGS (Real-Time Gross Settlement). Despite a slight decrease in the total remittance value through UPI during the year 2020-2021, it remains the most prominent and widely used channel for both inward and outward remittances.

This data reflects the significance and popularity of UPI as a convenient and efficient mode for transferring funds, both domestically and internationally, through payment banks in India. However, the overall reduction in total remittance values suggests that other remittance channels, such as IMPS and RTGS, also play essential roles in facilitating financial transactions for customers of payment banks in the country. The data provides valuable insights into the remittance patterns and preferences of users, highlighting the continued importance of digital payment systems in the Indian banking landscape.

Challenges Faced by Payment Banks

- The substantial investments required for the development of distribution network, technical infrastructure, brand building that non-telecom entities must make when setting up payment banks make the first years difficult because revenue from remittance service might not be sufficient to pay for marketing, distribution and other technology related expenses(Yadav et al., 2019).
- Security of data and privacy need to receive more attention. Payment banks must to take into account multifactor authentication, which provides users with extra protection (Bharathi, 2021).
- Lack of awareness about payment banks among the public.
- Acceptance of digital payment as a mode of transaction is still challenging among rural people.
- To encourage individuals to utilize payment bank accounts for transactions on platforms, portals, and online gateways, recognizing these accounts as a viable alternative for transfers is crucial(Shrey et al., 2018).

Conclusion:

Payment banks have become a significant and influential entity in the nation's financial sector. In 2014, the Reserve Bank of India (RBI) unveiled a novel category of banks with the explicit aim of fostering financial inclusion and delivering essential banking services to the unbanked population. Through this innovative strategy, payment banks have been crucial in broadening access to financial services for previously underserved communities, aiding the overall advancement and expansion of the country's economy.

Since their inception, payment banks in India have achieved notable progress. By proactively engaging with underserved communities, they have been instrumental in closing the gap between rural and urban areas, enhancing financial inclusion across the nation. India's payment bank sector is populated with several prominent players, each contributing to the industry's growth.

Among the key players, Paytm Payment Bank has capitalized on its extensive user base from its mobile wallet service, successfully extending banking services to millions of customers. Airtel Payment Bank has also emerged as a significant contender, boasting an extensive network of banking points spread across the country. Noteworthy entities like Fino Payment Bank, Jio Payment Bank, and Indian Post Payment Bank further enrich the market, actively catering to diverse customer needs.

These payment banks have forged strategic partnerships with numerous organizations, including shops, service providers, and government entities, enabling them to offer a comprehensive array of customer-centric services. Through these collaborations, payment banks have expanded their reach and impact, empowering more individuals with access to vital financial services. As these institutions continue to grow and innovate, they are contributing to the transformation of India's financial landscape, making a positive difference in the lives of millions.

Payments banks incurred substantial operating expenses over the past five years, mainly attributed to the considerable investments in creating new infrastructure and covering other initial-year expenditures. These infrastructure-related costs significantly impacted their profitability during this period. As the payments banks seek to expand their operations and customer base, they need to exercise patience and allocate sufficient time to effectively identify and attract customers.

To remain competitive and attract a larger customer segment, payments banks must introduce more innovative financial services. Offering a diverse range of customer-centric products and solutions can serve as a powerful incentive for customers to choose them over other financial institutions. Additionally, providing more accessible services at affordable rates will play a crucial role in appealing to a broader audience and fostering greater financial inclusion. By focusing on innovation, accessibility, and affordability, payments banks can strengthen their position in the market and achieve sustainable growth in the long run.

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